Occupational Pension Schemes Practice Notes

On the Approval of Occupational Pension Schemes
Please note that these relate only to the pre-A Day regime and will not be amended in any way. These should only be used as general guidance and any points of difficulty cannot be relied on as the “final” HMRC view.

These Notes should be read in conjunction with "Pensions Updates" which periodically amend or expand upon them.

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Note 1 - Occasional *IR SPSS* Updates are used to amplify or amend this manual. Where such amendments are announced, substantive changes can be identified in the body text by background shading or high-lighting. Revised headings are not normally highlighted. This high-lighting is removed when a new set of amendments is announced. However, where a change consists of a large addition (such as a new appendix) and the Update clearly indicates that the entire section is new, the new content may at times be introduced without highlighting in the interests of legibility.
Part 1. Introduction

Legislation and Discretion

1.1 The legislation governing the tax treatment of occupational pension schemes is contained in Chapter I Part XIV of the Taxes Act as amended by section 75 and Schedule 6 of the Finance Act 1989 and subsequent Finance Acts. These notes describe the practice of the Inland Revenue in approving schemes under that legislation. They also describe the tax consequences of approval.

1.2 The legislation sets out certain basic conditions which entitle a pension scheme to approval (mandatory approval), and supplements this with discretionary powers to enable the Board to approve schemes which do not fully comply with those conditions. The legislation also contains provision for the making of Regulations which restrict the Board's discretion to approve schemes.

1.3 These notes relate only to occupational pension schemes for which approval is sought under the exercise of the Board's discretion under Chapter I Part XIV of the Taxes Act. They give only general guidance on how that discretion is exercised and reflect the tax position at the time of writing. It should be borne in mind that they are not binding in law and the Board may find in a particular case that there may be special circumstances justifying different treatment, subject of course to any Regulations which restrict the Board's discretion. The Board will not be bound by these notes where a scheme is involved in or used for the purposes of tax avoidance.

1.4 In exercising its discretion to approve schemes, the Board require them to be bona fide established for the sole purpose of providing relevant benefits, and continued approval will be dependent on that sole purpose being maintained.

Practice Notes

1.5 For personal pension schemes approved under Chapter IV Part XIV of the Taxes Act, the guidance notes in IR 76 (2000) should be followed instead of these practice notes. IR 76 (2000) is published on the Inland Revenue website - www.inlandrevenue.gov.uk. Guidance on converting a retirement benefits scheme approved under Chapter I to a Chapter IV approved personal pension scheme is included in both sets of notes.

These notes do not deal with the approval of Free standing Additional Voluntary Contribution Schemes. These are the subject of separate Guidance Notes (IR12 Supplement), which can also be found on the Inland Revenue website.

1.6 Most pension schemes are established under irrevocable trusts and, subject to trust law or the imposition of a pension sharing order, are governed entirely by their trust instrument and rules. Thus where these notes are written in imperative form the scheme rules should be framed to ensure that the requirements are met. Where provisions in these notes are permissive those provisions may come into effect only if the scheme rules authorise them. Where scheme rules are subject to overriding legislation it is necessary to have regard to the effect of such legislation in relation to what is permissible under the scheme.

1.7 These notes deal primarily with the current conditions and practice for approval of new schemes. In this context 'new schemes' should be interpreted to mean not only schemes which are set up following the publication of these notes but also schemes already before the Board for approval prior to the publication but which have not received such approval. The notes also cover requirements for the continued approval of previously approved schemes (other than those with certain reserved rights to previous requirements which were in place when their approval was granted). Schemes may also make provision to protect the position of members with continued rights and thus, where relevant, each Part contains a section setting out the practice which applies to those members.

1.8 Appendix I consists of a glossary of terms used. Such terms will be identified in the text by the use of italics. Where the term used in the glossary also has a statutory definition, in the event of
any doubt over the correct interpretation to be applied to the term, the statutory definition shall prevail.

Appendix II contains details of *IR SPSS* mailing list and forms. Appendix VII contains a checklist of reports required by *IR SPSS* and Appendix X contains an index of Statutory Instruments applying to occupational pension schemes. The other Appendices provide guidance on specific topics as set out in the list of contents.

1.9 References to sections or Chapters and Parts or Schedules will, unless stated otherwise, be to sections or Chapters and Parts of or Schedules to the *Taxes Act* 1988.


1.11 The term approved scheme will, unless qualified, include all approved schemes whether or not exempt approved. It has been assumed that approved schemes which accept contributions from employees or which hold funds will have been set up under trust to obtain the beneficial tax consequences of exempt approval.

1.12 Our internal guidance manuals, the Pension Scheme Instructions (PSI) and the SSAS Guidance Notes, have both been published in line with the aim of the Code of Practice on Access to Government Information. Both manuals will become available on the IR website (www.inlandrevenue.gov.uk) as soon as possible.
Part 2. Establishment of Schemes

Approval and Exempt Approval

2.1 Any retirement benefits scheme may be approved if it satisfies Inland Revenue requirements, and approval will, by virtue of section 596, exempt the members from liability to income tax on the employer’s contributions which could otherwise arise under section 595. An approved scheme, however, will not qualify for the special tax reliefs on contributions, investment income, etc under section 592, nor will any premiums paid to an insurance company qualify for the tax reliefs on "pension business" under Chapter I Part XII unless it is also an exempt approved scheme. Unless a direction is granted (see paragraph 2.2 below) it is a necessary condition of exempt approval that the scheme should be established under irrevocable trusts.

2.2 Where a benefit is secured by paying a single premium to purchase an immediate annuity:

(a) on or after an employee’s retirement or after attainment of age 75 as described in paragraph 6.4 (commonly referred to as a "Hancock" annuity); or

(b) for the widow, widower, surviving civil partner or dependant of a deceased employee; or

(c) under a scheme for one individual set up shortly before retirement;

the transaction, if approved and made the subject of a trust, will be an exempt approved scheme.

Direction by Board

Otherwise a request may be made for the transaction to be treated as an exempt approved scheme by virtue of section 592(1)(b) and the Board will normally make a direction to that effect but exceptionally the Board may consider such treatment inappropriate in which case the transaction will be considered for approval. In some cases the Board may make such a direction despite no request having been made - this will normally only occur where it is considered appropriate that the allowance to the employer of the cost should be spread in accordance with paragraphs 5.8 and 5.9.

Trusts and Trustees

2.3 For a scheme to be held under irrevocable trusts does not mean that the scheme needs a formal trust deed but that the assets (including policies) must be set aside to provide relevant benefits for employees or pension credit members and must be held by a trustee or trustees on trusts that ensure that, apart from any surplus (see Parts 13 and 14) or where reimbursement is appropriate (see paragraphs 7.32(b), 17.23 and 17.39(d)), they are not available to the employer.

2.4 The trust may be established by deed, or by resolution of a board of directors (provided that they have the power to do so) or in the case of a partnership by a resolution of the partners. It may be set up under a separate trust deed or declaration of trust, or by inclusion in one instrument with the scheme rules or, where only a policy is used, in the policy.

2.5 The trustees may be, or include, the employer.

Administrator

2.6 The legislation lays certain duties upon the administrator of a scheme (see Part 16). In the first instance the trustee(s) (or scheme sponsor(s), where the scheme is not under trust) will be the administrator. But they may, at any time, appoint a person who is resident in the United Kingdom to be responsible for the discharge of all the duties of the administrator. The appointment of such a person must be in writing and, if made after the establishment of the scheme, shall constitute an alteration of the scheme for the purposes of section 591B(2).

2.7 There must, at all times, be a person or persons resident in the United Kingdom responsible for the discharge of all the duties of the administrator.
2.8 In accordance with section 606, if at any time there is no administrator or the administrator defaults or cannot be traced, the trustees or scheme sponsors, become responsible for discharging the administrator’s duties. If the trustees/scheme sponsors default or cannot be traced the employer becomes responsible for discharging the administrator’s duties. In this context where the employer is resident abroad the term “employer” includes any branch or agent of the employer in the United Kingdom. If the employer defaults, ultimate responsibility for complying with the administrator’s duties reverts to those scheme members whose entitlement under the scheme (whether from the current or an earlier employment or occupation) derives from controlling directorships or Schedule D earnings.

Protection of Trust

2.9 A scheme set up under trust which is both self-administered and provides benefits on a money purchase basis must protect the trust from being extinguished by the action of one or more members. This should be done by expressing the individual member's rights to benefit as being against the funds of the trust as a whole even though they may be calculated by reference to specific trust assets.

Interim Deed Procedure – for valid applications received before 6th April 2002

2.10 Because of the complex nature of occupational pension schemes many schemes are established by an interim trust document under which the parties covenant to execute definitive documents within a specific period (usually 2 years). The Inland Revenue is prepared to accept that a scheme is effectively established by such documents provided that:

(a) it is clear that any funds or policies are held for the purposes of the scheme under irrevocable trust,

(b) the document sets out the purpose of the scheme,

(c) members of the scheme and every employee who has a right to be a member have been advised of all essential features of the scheme, and

(d) the parties to the document have bound themselves to execute definitive documents within a reasonable time. For schemes established from 6 April 1993 it is expected that definitive documents will be adopted within 2 years.

This paragraph only applies to valid applications received by IR SPSS before 6th April 2002.

2.11 If the conditions in paragraph 2.10 are met and the interim documentation is satisfactory IR SPSS will authorise the scheme to operate on interim documentation. It should be noted that a scheme set up using interim documents cannot be approved before the definitive documents are in place. The approval will normally then be backdated to the inception of the scheme.

This paragraph only applies to valid applications received by IR SPSS before 6th April 2002.

Interim Deed Procedure – for applications received after 5th April 2002

2.12 Approval applications received by IR SPSS from 6th April 2002 should be submitted with definitive documentation unless the scheme falls within the terms of paragraph 2.13 below. Schemes may still be established using an interim deed followed by a later definitive trust deed and rules. However the approval application should be submitted with details of both interim and definitive documentation.

2.13 A scheme set up as a result of a corporate reorganisation may make an approval application using only interim documentation. A scheme falls within this category if,

1. The scheme was set up to receive a block transfer of funds and/or a block of employee members, and
2. The transfer was brought about or resulted from

- A change or an intended change of ownership of an employer, or
- A change or an intended change of ownership of all or part of an employer's trade or business.

Contracting out of public service work may also be regarded as a corporate reorganisation. For example XYC County Council contracts out its refuse collection service to ABC Ltd. The XYZ Council refuse collection employees are now ABC Ltd employees. Their new employer sets up a pension scheme for them and employees concerned move from the Local Government scheme to their new employer's scheme.

SSASs do not fall within the terms of paragraph 2.13 and must submit approval applications with definitive documentation.

2.14 The interim documentation used should contain minimum provisions, which are listed in paragraph 2.15 below. Where the documentation used complies with these minimum provisions and the application is otherwise satisfactory IR SPSS will approve the scheme with a specific condition attached to the scheme approval. This will enable the scheme, employers and members to receive full tax reliefs. The condition attached to the scheme's approval will be that definitive documentation is to be submitted to IR SPSS within 12 months of the scheme's establishment. This condition will be documented in the scheme approval letter. If the scheme fails to meet this approval condition the scheme's approval may be withdrawn.

**Interim Deed Requirements**

2.15 It is expected that the schemes using the interim deed procedure will be larger pension schemes. As such it is probable that in the period between setting up the scheme and executing definitive documents a scheme may have to transfer of funds or pay benefits. So to satisfy IR SPSS requirements and to protect the scheme, employers and members from unnecessary tax charges the interim trust deed requirements are fairly extensive. The required provisions are split into 4 sections as shown below.

**Scheme set up**

a) Create an irrevocable trust (on or after the date of the execution of the deed)

b) Covenants to bring in full rules within 12 months of the establishment of the scheme

c) Sets out the sole purpose of the scheme as the provision of relevant benefits

d) Appoint named trustees

e) Appoint named administrator

**Scheme operations**

a) Power to appoint/remove trustees

b) Power to appoint/remove administrator

c) Power to amend the scheme provisions

d) State scheme shall be operated in a manner consistent with being treated as an exempt approved scheme prior to the adoption of the rules

e) Power to make transfers out

f) Power to permit entry and exit of participating employers
g) Investment powers, i.e. how the scheme assets may be invested

h) Ban on refunds to employers, except on the wind up of a scheme or with prior IR agreement (until IR approval is confirmed and this requirement is formally lifted)

i) Power to wind up the scheme before definitive deed & rules are adopted (but with IR agreement)

**Contributions/Benefits**

a) Sets out basic benefit payment provisions i.e.

   i) Who to (e.g. members and/or dependants)

   ii) When (e.g. on `retirement’ – normal/early/late/incapacity; death in service/in retirement; deferred benefits on leaving service – payment dates/transfers/ return of contributions.)

   iii) How (e.g. as a pension or lump sum. Is any lump sum provided by commutation or separately? Serious ill health and triviality commutation.)

The provisions here do not have to be detailed. What is required is basic enabling provisions that will allow for benefit payment to be made without triggering a tax charge under section 600 ICTA 1988.

iv) What (benefits must be limited to IR maximum as per the PS123 which must be stated in full)

b) Power to accept employee and employer contributions

c) If the scheme is contributory, state the required members’ contribution rate

d) Limit employee contributions to the IR maximum (15%)

e) State that the maximum employer contributions should be based on actuarial advice

**Other IR Provisions**

a) Pension on divorce provisions

b) Provisions that comply with Regulations 5 & 6 of The Retirement Benefits Schemes (Restriction on Discretion to Approve) (Additional Voluntary Contributions) Regulations 1993

c) Restriction on transfers in – cannot be made without prior IR agreement (until IR approval is confirmed and this requirement is formally lifted)
Part 3. Membership of Schemes

General

3.1 Membership of an approved scheme must generally be confined to employees of the employers participating in the scheme. Where, however, the scheme has received a pension sharing order in respect of a scheme member, membership may be offered to the ex spouse or former civil partner of such a member. Employees include former employees of the employer concerned and where the employer is a company, any officer, director or manager of the company.

3.2 Membership need not be open to all the employees in an employer's service or to any particular category of them; a scheme may in fact relate to a single employee or to individuals selected on a discretionary basis, subject to the principle of equal access. But every member of a scheme and every employee who has a right to be a member must be notified of his or her rights under it (section 590(2)(b)). If so desired, membership may be open to ex spouses and/or former civil partners selected on a discretionary basis.

3.3 Scheme membership is not restricted to full-time employees. Part-time, temporary or domestic employees may also be included, but see paragraph 5.6 regarding domestic employees.

Persons Assessed Under Schedule D

3.4 Agents, consultants and others who are assessed to income tax on their earnings under Schedule D cannot be provided with benefits under an approved scheme in respect of those earnings.

3.5 Similarly proprietors and partners assessed under Schedule D may not be admitted to or retained in active membership of an approved scheme. An employee who becomes such a proprietor or partner should be treated as having withdrawn from service. Benefits may not be provided for an individual who has been a partner and becomes an employee of the partnership without the specific prior agreement of IR SPSS.

Directors of a Company

3.6 While a director may be admitted to membership of an approved scheme his or her benefits should relate only to remuneration (whether fees or otherwise):

(a) to which he or she is beneficially entitled i.e. he or she is not under an obligation to account for it to another company or employer, and

(b) which is not being treated for tax purposes as a receipt of a profession in which he or she is engaged e.g. as a principal in a firm of accountants.

3.7 Special consideration may need to be given to the membership of directors of service companies, particularly where the company provides services for a partnership. In these circumstances the Inland Revenue will need to be satisfied that the pensionable remuneration relates wholly to the director's service for the company rather than any obligations to the partnership.

Information Powers Regulations

3.8 Regulation 8 of the Information Powers Regulations requires the administrator to notify IR SPSS within 180 days of the end of the scheme year in which it occurs, of

(a) the admission of any member who is a controlling director of any of the participating employers;

(b) the retention of any member who becomes a controlling director of any of the participating employers, and
(c) the admission of any member who is, or at any time within the 10 years prior to joining the scheme has been a controlling director and to whom a pre Finance Act 1989 basis of calculation is to apply under transitional arrangements.

Particulars should be supplied on the specified form PS 255 - a specimen is included in Appendix II.

3.9 A controlling director of a company which is treated for tax purposes as an investment company cannot be accepted into membership of an approved scheme in relation to that employment. A director of such a company who although not a controlling director is a member of a family which owns more than 50 per cent of the shares, is similarly disbarred. However, IR SPSS do not object to schemes for such directors of an investment company where the investment company is a holding company of a group of trading companies, in which it acts as the co-ordinator for the group.

Spouses or Civil Partners of Directors, Proprietors And Partners

3.10 If it is desired to admit to membership of a scheme the spouse or civil partner of a controlling director, the proprietor or one of the partners, the Inland Revenue will need to be satisfied that he or she is a genuine employee actively working in the business on a regular basis.

Temporary Absence and Secondment

3.11 The approval requirements in respect of temporary absence differ depending on whether the temporary absence is within the United Kingdom or overseas. The following paragraphs deal only with temporary absence in the United Kingdom. For temporary absence or secondment overseas see Part 15.

3.12 An employee who is temporarily absent or is seconded to another employer and remains resident in the United Kingdom may remain in full membership of an approved scheme (even though during his or her absence no remuneration is paid by the original employer), if:

(a) there is a definite expectation of return to service, and

(b) during the period of absence he or she does not become a member of

- another approved retirement benefits scheme,
- a retirement benefits scheme seeking approval, or
- a personal pension scheme other than
  - a "minimum contributions" only scheme, or
  - through eligibility to contribute to a personal pension scheme under section 632B ("concurrency").

Absence during which no retirement benefits accrue (where the benefit of remaining a member flows from aggregation of two periods of service for benefit calculation purposes and/or the provision of death in service cover during the absence) is not subject to the conditions at (a) and (b) above.

3.13 A period of full membership while temporarily absent may, subject to paragraph 3.12 above, continue for up to 10 years without reference to IR SPSS.

3.14 An employee who is absent because of incapacity, whether or not receiving pay under a sick pay or permanent health insurance scheme or directly from the employer, may be retained in full membership for more than 10 years regardless of whether there is a clear expectation of return to
3.15 Where retention in full membership is contemplated in any circumstances other than described in paragraphs 3.12 to 3.14 above, *IR SPSS* should be consulted first.

**Part Time Employees: Retrospective Membership**

3.16 Part time employees retrospectively admitted to membership of their employer's or former employer's scheme as a result of equal treatment law should be treated as new members without *continued rights* even if benefits relate to service before 1 June 1989.
General

4.1 Members may or may not be required to make *basic or contractual contributions* to an approved scheme. Department of Social Security pensions legislation however requires schemes to permit certain members to pay *Additional Voluntary Contributions* to secure additional benefits but subject to the requirements for approval.

Tax Relief

4.2 The tax treatment of any contributions will depend on whether the scheme is *exempt approved*. Contributions to an *exempt approved scheme* are allowable as an expense in assessing the member's liability to tax under Schedule E: contributions to an approved scheme are not eligible for tax relief. Tax relief is given by statute under section 592 and is restricted in any year of assessment to 15% of the member's *remuneration* from the employment being pensioned. While section 592(8) provides for the Inland Revenue to prescribe a higher percentage than 15%, the Board are only prepared to do so where there are exceptional and compelling reasons. Contributions are allowable in the year of assessment in which they are paid. The relief on contributions is further restricted, other than for employees with *continued rights*, to ensure that it does not exceed 15 per cent of the *permitted maximum* in relation to all employments (whether or not the employments are *associated*) being pensioned whether under one or more schemes.

4.3 Tax relief on contributions (other than those to a *Free standing Additional Voluntary Contribution Scheme*) is given through a special arrangement under the PAYE system whereby the contributions are deducted from gross pay before the member's PAYE tax deductions are calculated. In this way the correct tax relief is given automatically as the contributions are paid. Advice to employers on the operation of the net pay arrangement is given in the Employer's Guide to PAYE. Employers who need further guidance should contact their Inspector of Taxes.

4.3a From 6 April 2001, all contributions paid by individuals to a Chapter IV scheme (see Part 24) are treated as paid net of basic rate income tax under section 639(2)(a). This applies to

- employees
- self-employed persons
- non-employed persons
- minors

regardless of whether they are

- non taxpayers
- basic rate taxpayers
- higher rate taxpayers

For example, an individual who wishes to pay £100 a month to their personal pension would only pay a net amount of £78 a month, if the basic rate of tax was 22%. A higher rate taxpayer may claim additional relief of £18, if higher rate tax liability is 40%, through their self-assessment tax return.

The scheme *administrator* will claim the tax at the basic rate from *IR SPSS* (Repayments) and credit it to the individual's *arrangement*. 
Maximum Contributions

4.4 The rules of an exempt approved scheme should preclude the payment by members of contributions in excess of those which qualify for tax relief (but see paragraph 4.8 on temporary absence). Exceptions to this are where:

(a) an employee falls within the circumstances described in regulation 3B of the Retirement Benefits Schemes (Continuation of Rights of Members of Approved Schemes) Regulations 1990 (SI 1990 No 2101) which was inserted by the "Amendment Regulations 1996" (SI 1996 No 3114), or

(b) the rules of the scheme require that an employee make good a deficit of contributions by payment of a lump sum, or

(c) paragraph 15.6 applies.

(d) paragraph 10.65.

In the case of (c) the contributions should not exceed those which would have been payable had the employee’s earnings been chargeable under Case I or II of Schedule E. The rules should not allow a member to contribute or continue to contribute to secure additional benefits which would be expected to cause the limits set out in Parts 6-12 to be exceeded (but see paragraph 13.2 on payment of Additional Voluntary Contributions to fund for early retirement benefits).

Pension Sharing Orders

4.5 Where a member’s benefit entitlement in a scheme is permanently reduced following a pension sharing order and the member does not fall within the administrative easement described in paragraph 7.7, that member’s maximum approvable total benefits are reduced (see paragraphs 7.2, 7.40 and 7.41). Where there is scope to do so, such a member may pay contributions up to the maximum described in paragraph 4.2, to rebuild some or all of the pension debit. These contributions must not be such as would cause the member’s reduced maximum approvable total benefits to be exceeded.

4.6 A pension credit member cannot pay contributions into a scheme in respect of a pension credit held in the scheme for that pension credit member. Where, however, the pension credit member is also entitled to benefits under the scheme as a result of being an employee of a participating employer, contributions may be paid into the scheme up to the maximum described in paragraph 4.2. These contributions must relate solely towards the provision of benefits that arise as a result of being an employee and be subject to the final sentence of paragraph 4.4.

Where an ex-spouse or former civil partner has a pension credit held in a scheme in which he or she is also entitled to benefits as an employee and the scheme does not treat the pension credit rights as separate from the employee rights, the pension credit rights will be taken into account in applying the tax approval limits to the total benefits that the individual receives as an employee scheme member. In these circumstances, contributions must again relate solely towards the provision of benefits that arise as a result of being an employee. This means that those contributions will be based on no more than the reduced maximum approvable total employee benefits for that member (i.e. after taking the pension credit into account).

Repayment of Surplus Additional Voluntary Contributions

4.7 If the payment of Additional Voluntary Contributions causes benefits to be excessive, the surplus funds relating to those contributions must be returned to the member or paid to the member’s estate. Where such contributions have been paid the "relevant date" prescribed by Regulations is the earliest of retirement, leaving pensionable service or death. The surplus is to be calculated in the manner prescribed by the Regulations (see paragraph 16.30). Repayments of surplus Additional Voluntary Contributions are subject to deduction of tax in accordance with section 599A. See paragraphs 16.28 - 16.34 which deal with the administrator’s duties in relation to Free standing Additional Voluntary Contribution Schemes and the calculation of surpluses and
paragraphs 17.35 and 17.36 regarding the taxation of repayments of surplus Additional Voluntary Contributions.

**Temporary Absence**

4.8 During a period of temporary absence (see paragraph 3.11), a member's contributions may be either suspended or continued. If they are continued they should not exceed 15% of the member's remuneration for the year from the employment being pensioned. Where the member is not paid any remuneration or is paid reduced remuneration in respect of the employment being pensioned for the period of absence, contributions should not exceed 15% of what would have been the member's remuneration for the year, in respect of that employment, if he or she had not been temporarily absent. Tax relief will not, however, be due unless the requirements described in paragraph 4.2 are satisfied.

**Continued Rights**

4.9 A member with continued rights is not subject to the requirement that, for the purposes of calculating the maximum contribution qualifying for tax relief, remuneration is to be restricted to the permitted maximum.

**Contributions After Normal Retirement Date**

4.10 Paragraphs 7.44 and 9.1 both provide for augmentation of benefits which have come into payment in part or in full. A member who remains in service after normal retirement date may, whether or not any benefits have been paid (but see paragraph 7.32 in relation to non-continued rights members), start or continue paying contributions to fund any shortfall of maximum benefits. In this context the maximum, or the reduced maximum in the case of a member (not within the administrative easement described in paragraph 7.7) who is subject to a pension sharing order (see paragraph 4.5), may be that appropriate at normal retirement date, or the date of the first payment of benefits, (excluding benefits from an AVC fund paid before employer funded benefits became due and payable – see PartII of Appendix XII) or where no benefits are taken in advance of actual retirement, the date of such retirement subject to paragraph 6.1 where applicable. Payment of contributions in these circumstances has the effect that the employee is regarded as remaining in pensionable service. Where the employer's contributions cease at or after normal retirement date, subsequent contributions by the employee will not prejudice the requirement set out in paragraph 5.1.

**Salary Sacrifices**

4.11 Arrangements whereby the employee takes a reduction in remuneration and the employer pays a corresponding amount to the pension scheme as a contribution for the employee's benefit (commonly known as a salary sacrifice), should be notified directly to the appropriate Schedule E Tax District where the reduction in salary is £5,000 or more per annum. The Schedule E District decides whether or not the sacrifice is effective for tax purposes and notifies IR SPSS of any which are not. Where a salary sacrifice is ruled to be ineffective the payment will be a contribution by the employee. As such it is subject to the limit in paragraph 4.4 above. Should the payment or any part of it exceed that limit it should be repaid to the member at the earliest opportunity. Such a repayment will not be subject to tax under section 598 but the Schedule E Inspector may need to advise on the tax treatment of this amount.

**Contributions Following Introduction of Profit Related Pay Scheme**

4.12 Where an employer has a profit related pay (PRP) scheme which typically results in a reduction in the employee's gross remuneration, benefits may nevertheless be promised by reference to the remuneration the employee would otherwise have been receiving if the PRP scheme had not been introduced (see paragraph 7.12). So long as the benefits are promised by reference to this "shadow pay", contributions by the employee may also be calculated by reference to "shadow pay", provided these do not exceed, in any year of assessment, 15% of the member's actual remuneration from the employment being pensioned.
Excessive Contributions

4.13 If -

(a) a scheme receives an excessive sum by reference to the scheme rules in respect of an employee contribution, AND

(b) the amount has been paid in error

the trustees may refund the excess without seeking the prior approval of the *IR SPSS*. (The above includes payments of premiums in error).

The tax position in respect of the amount refunded should be adjusted through either PAYE or self assessment, as appropriate.

4.14 Any other refund of employee contributions (i.e. where the sums were validly paid, have been held for the purposes of the scheme but have then been refunded) should be reported to the tax district dealing with the tax affairs of the scheme. The district should receive the report form 1(SF) not later than 30 days after the end of the tax year in which the refund was made.

For more details of the tax treatment of such refunds, please turn to paragraphs 17.22-26 and 17.35-36.
Part 5. Contributions by Employers

Need to Contribute

5.1 It is a condition of approval of a scheme (other than a Free standing Additional Voluntary Contribution Scheme, for which there are special rules) that the employer must contribute to it. The Board will not exercise their discretion to approve a scheme if the employer's contributions appear to be mere token contributions of insignificant amounts i.e. less than 10% of the total contributions. In schemes where contributions are calculated separately for each member (viz., individual arrangements, earmarked schemes and small self-administered schemes), this criterion must be applied to each individual member of the scheme in order to justify his or her membership; it is not sufficient for the employer to pay an average of more than 10% in relation to the scheme as a whole.

5.2 To determine whether a particular level of contributions is acceptable it is permissible to take account of the employer's contributions to any other approved scheme relating to the same employee or employees, including personal pension schemes for which the employee(s) are eligible under s632B "concurrency". Nevertheless the employer must make some quantifiable contribution to each occupational pension scheme e.g. in relation to a supplementary scheme set up to provide additional benefits secured by Additional Voluntary Contributions it may be sufficient for the employer to bear the costs of administration.

5.3 Subject to the above and the need to control the scheme's funding (see Part 13) the amount and timing of the employer's contributions are matters for the employer. The tax treatment of contributions is outlined below.

5.4 Contribution holidays of up to 2 years need not be reported to IR SPSS.

Tax Treatment of Contributions

5.5 An ordinary annual contribution paid by an employer to an exempt approved scheme is, subject to paragraph 5.6 below, deductible for the purposes of Case I or II of Schedule D and of the provisions of sections 75 and 76 as an expense, or expense of management, incurred in the chargeable period in which it is paid (section 592(4)).

5.6 The amount deductible must not exceed the amount contributed in respect of employees engaged in a trade or undertaking the profits of which are assessable to tax in the United Kingdom (section 592(5)). An allowance cannot be given in respect of a person who has not been in the employer's service, or in respect of an employee whose duties are purely domestic. Where the employer carries on two or more separate businesses, each with its own employees, the employer's contributions in respect of particular employees can be allowed only against the profits of the business in which they are employed. See paragraphs 21.3 and 21.15 as to centralised schemes for the employees of more than one employer.

5.7 Regulation 7 of the Information Powers Regulations provides that where an employer makes any special contribution to a scheme in a chargeable period which exceeds both one half of the permitted maximum and the employer's total contributions, other than special contributions, to that scheme in the same chargeable period, it is to be reported to IR SPSS on form PS 251 not later than 180 days after the end of the scheme year in which the chargeable period - during which the special contribution(s) were made - ends. A specimen of the form is included in Appendix II. The criterion of one half of the permitted maximum refers to the permitted maximum at the end of that scheme year.

5.8 Section 592(6) provides that the allowance of a special contribution to an exempt approved scheme may be spread over a number of years. IR SPSS will determine the period of spread and notify the appropriate Tax District. Once the period of spread has been determined it will not be varied by reason of a change in the level of the employer's ordinary annual contributions or the
payment of a further *special contribution* in a subsequent chargeable period. Where, however, the employer ceases to trade or its trade is taken over by another employer, *special contributions* which have not been fully allowed when trading ceases will require re-allocation. Depending on circumstances, the unrelieved balance of the *special contributions* will normally be allowed against the profits of the employer whose trade has ceased in the final chargeable period before cessation, or, a re-allocation of the *special contribution* may be made on a time apportionment basis over the whole of the chargeable periods between payment of the contribution and cessation of trade.

5.9 For chargeable periods ending on or after 1 June 1996 the period of the spread is determined solely by the size of the aggregate *special contributions* to that scheme (not, as previously, all approved schemes of the employer). *Special contributions* which amount to £500,000 or over and exceed the total of other contributions made by the employer to that scheme in the same chargeable period will normally be spread on the basis set out below. Aggregate *special contributions* amounting to less than £500,000 will not be spread for tax relief purposes.

<table>
<thead>
<tr>
<th>Special Contributions</th>
<th>Period of Spread</th>
</tr>
</thead>
<tbody>
<tr>
<td>£500,000 or over but less than £1,000,000</td>
<td>2 years</td>
</tr>
<tr>
<td>£1,000,000 or over but less than £2,000,000</td>
<td>3 years</td>
</tr>
<tr>
<td>£2,000,000 or over</td>
<td>4 years</td>
</tr>
</tbody>
</table>

and the allowance of the contribution(s) will be spread evenly over the period e.g. an aggregate *special contribution* of £800,000 will be allowed on the basis of £400,000 in year 1 (the chargeable period in which it was paid) and £400,000 in year 2 (the next chargeable period). Where a chargeable period is not a period of 12 months allowance will be given on a pro rata basis, viz. if in the above example the first chargeable period is 8 months followed by a 12 month period, the allowance would be on the basis of £320,000 (8/20ths of £800,000) in year 1 and £480,000 (12/20ths of £800,000) in year 2.

Where there is evidence of manipulation to reduce the period of spread *IR SPSS* reserve the right, under section 592(6), to determine the spread on some other basis.

5.10 Transitional arrangements apply in relation to relief for *special contributions* paid in a chargeable period ending on or before 31 May 1996. Such relief will be spread as follows (paragraph 5.8 of the 2nd edition of IR12 (1991) refers):

<table>
<thead>
<tr>
<th>Special Contributions</th>
<th>Period of Spread</th>
</tr>
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<tbody>
<tr>
<td>£25,001 to £50,000</td>
<td>2 years</td>
</tr>
<tr>
<td>£50,001 to £100,000</td>
<td>3 years</td>
</tr>
<tr>
<td>Over £100,000</td>
<td>4 years</td>
</tr>
</tbody>
</table>

5.11 A *special contribution* which is actuarially certified to be made solely to finance cost of living pension increases for existing pensioners, or any part of a *special contribution* which is so certified, will not be spread and will be allowed as an expense of the chargeable period in which it is paid. Such a *special contribution* or part of a *special contribution* is not aggregable with any other *special contributions* paid in the same chargeable period for the purposes of determining a spread under paragraph 5.9. Payment of any such amount is not notifiable under the PS 251 procedure (see paragraph 5.7).

5.12 The legal and other expenses of establishing and running a scheme are not contributions to the scheme and do not qualify for allowance under section 592. Nevertheless, they will be allowed as expenses of the chargeable period in which they are paid. Compensation payments made on the order of the Pensions Ombudsman will also be treated as administration expenses of the scheme. Such payments will not be regarded as breaching the sole purpose test (see paragraph 1.4).

5.13 If an employer provides accommodation and equipment for running the scheme and paying out benefits, relief on the cost will be allowed insofar as it represents expenses of a revenue nature which would otherwise have fallen upon the *administrator* and been met by allowable contributions
from the employer.

5.14 Whether contributions to, or expenses incurred in connection with, an approved scheme which is not exempt approved qualify for relief is determined under the ordinary rules of Schedule D by the Inspector of Taxes dealing with the employer's accounts in the light of all the circumstances in which the contributions are made.

**Pension Sharing Orders**

5.15 When a *pension credit* is established within a scheme for an *ex spouse* or *former civil partner*, the employer should not, generally, make any further contributions in respect of that *pension credit*. However, this prohibition does not apply where such contributions are required to be paid in accordance with the pension sharing on divorce provisions in the Welfare Reform and Pension Act 1999 and associated regulations.

5.16 When a member's benefit entitlement in a scheme is permanently reduced following a *pension sharing order* and the member does not fall within the administrative easement described in paragraph 7.7, that member's maximum approvable total benefits are reduced (see paragraphs 7.2, 7.40 and 7.41). Further employer contributions for such a member should be based on no more than the reduced maximum approvable total benefits for that member and not on the maximum approvable total benefits that would have applied for that member had the *pension sharing order* not taken place.

**Refund of Contributions Paid in Error**

5.17 A refund of premiums or contributions paid in error may be made without contacting *IR SPSS* Audit & Pension Schemes Services provided that:

(a) the premiums or contributions were made in error because a direct debit mandate, or the like, was not altered or cancelled immediately the obligation to make the premiums or contribution ceased

(b) the period over which the overpayment occurred was less than one year.

Such refunds are not regarded as subject to the tax charge under section 601 (see paragraphs 17.38 and 17.39). Any tax relief that was obtained when such premiums or contributions were paid will not be appropriate and so the employer must take the necessary steps to correct the tax position.

If the conditions of (a) and (b) above are not met, an application for a refund must be made to *IR SPSS* providing the full facts and circumstances. Only when written authority has been received from *IR SPSS* may a refund be made.
General

6.1 Scheme rules may allow members to retire on pension at any time between age 50 and 75. Pension entitlement for a member under a scheme must come into payment immediately on leaving service at or after normal retirement date or if remaining in service no later than the attainment of age 75 except in the circumstances described in paragraph 6.4. (But see paragraph 6.14 in relation to members with continued rights and paragraph 6A.2 in relation to payment of pension credit benefits.)

Benefits arising from additional voluntary contributions paid to the employer’s main scheme, or paid to a separate scheme of the employer, or benefits coming from Free Standing additional voluntary contributions Schemes may be paid at a different time from the other main scheme benefits. Additional Voluntary Contribution benefits may start at any time between age 50 and age 75 (or at an age earlier than 50 if a person leaves employment because of incapacity) regardless of whether the member retires or leaves pensionable service. See part II of Appendix XII for further information on the flexible use of additional voluntary contributions.

6.2 If retirement is caused by incapacity retirement benefits may be paid immediately whatever the employee's age, and may be the fraction of final remuneration the employee could have received had he or she remained in service until normal retirement date less the pension debit where necessary (see paragraph 7.2). (See paragraph 6A.3 for the circumstances under which pension credit benefits may be paid on the incapacity of the pension credit member.)

6.3 In the case of a controlling director regulation 9 of the Information Powers Regulations requires the administrator to give 28 days prior notice of the intention to retire on the grounds of incapacity. Copies of documents relating to the decision of the administrator of the scheme to permit retirement on grounds of incapacity prior to the normal retirement date, including copies of medical reports and other documents in the possession or under the control of the prescribed person containing details of the medical evidence which formed the basis of that decision, should be furnished. Provided all the information required is furnished by the prescribed time the onus will be on IR SPSS to say before the notification period has expired whether or not the proposal is acceptable. It is implicit in the Regulations that if nothing is heard to the contrary within 28 days the administrator is entitled to assume that the proposals are satisfactory, provided that they are consistent with the scheme rules and IR SPSS requirements in the first place. Notifications should be sent to IR SPSS, Compliance Audit Section. It is acceptable in the first instance for this information to be sent by fax (0115 9741480). The original documents should then be sent by post in the normal way.

6.4 It is permissible to provide retirement benefits for an employee retiring after the attainment of age 75 only if the benefits commence immediately on the establishment of the scheme i.e. the benefits constitute a Hancock annuity.

Normal Retirement Date

6.5 It is a condition of approval that the rules of a scheme (other than a simplified defined contribution scheme - see Part 22) should specify the age at which members will normally retire. For members without continued rights the purpose of the normal retirement date is principally for funding considerations.

6.6 The normal retirement date may differ for categories of member and may be at any age within the range 60-75.

6.7 Exceptionally the age at which some employees, e.g. professional sports people, retire is much
earlier than the range of ages specified in paragraph 6.6. The adoption of an earlier *normal retirement date* for such employees requires the specific agreement of *IR SPSS*. It is popularly believed that, as for *personal pension schemes*, there is a list of acceptable retirement ages for particular employments. This is not true - each case is considered on its own merits. Each agreement is subject to special restrictions depending on the circumstances of the individual case and, in any event, will not be extended to directors. These restrictions may include prohibition of early retirement except on grounds of *incapacity*, a bar on additional benefits accruing for service after the *normal retirement date* or restriction of retirement benefits to no more than a pension of 1/60th of *final remuneration* for each year of service.

6.8 If membership of a scheme is discretionary a *normal retirement date* may be agreed for each member on an individual basis at the time of entry into the scheme.

6.9 The *normal retirement date* need not necessarily be the birthday at which the specified age is reached but may be any convenient date such as the last day of a month or the nearest scheme anniversary date.

6.10 An employee who is a member of more than one scheme of the employer should normally have a common *normal retirement date* under all schemes. But the employee may, subject to the conditions of paragraph 6.15, have a different *normal retirement date* under a supplementary scheme or arrangement which augments the benefits under the employer's main scheme. Provided that the *normal retirement date* under the supplementary scheme is the date at which the employee is expected to retire, that date may be taken as the member's *normal retirement date* under both schemes.

6.11 The normal retirement age specified in a scheme for a category of employees may, and indeed should, be altered if, because of changes in employment policy, the former age has become unrealistic. Furthermore, the *normal retirement date* of a member under an individual arrangement or discretionary scheme may be altered if the parties agree. This may be done without reference to *IR SPSS* if the new date is within the acceptable age range set out in paragraph 6.6 (but see paragraph 6.15 in respect of members with *continued rights*). No change may be made once a member has attained *normal retirement date*.

**Open Market Options**

6.12 The rules of an approved scheme may provide for benefits payable on retirement to be purchased on the open market. In certain types of insured schemes such an option might provide the member with a greater benefit (subject to the limits set out in the following Parts) than under the original scheme policy. The rules of the scheme should provide for a direct transfer of the purchase price to the annuity provider or, if considered appropriate, the payment may be channelled through a pension consultant arranging the transaction.

6.13 Where scheme rules provide for an open market option for a member whose maximum lump sum benefit is based on the initial pension payable, the exercise of that option should be completed before the lump sum benefit is calculated and paid. In practice *IR SPSS* will be content to allow the lump sum benefit to be paid either by the original scheme or the insurer with whom the transaction is arranged provided a binding contract for the provision of the benefits is entered into between these two parties before the lump sum is calculated and paid.

**Members With Continued Rights**

6.14 Paragraph 6.1 which generally requires benefits to come into payment no later than age 75 does not apply to members with *continued rights*. In the case of such members:

(a) there is no requirement for benefits to commence at the latest at age 75;
(b) immediate retirement benefits may be taken on or after *normal retirement date* even when the member remains in service (see paragraph 7.44).

**Change of Normal Retirement Date**

6.15 The *normal retirement date* of a member with *continued rights* may be altered (see paragraph 6.11 above) without reference to *IR SPSS* if the new *normal retirement date* falls:

(a) within the age range set out in paragraph 6.6; and

(b) not less than five years after the date of change.

No change may be made once a member has attained *normal retirement date*.

6.16 Entry into membership of a supplementary scheme or arrangement with a different *normal retirement date* (see paragraph 6.10) must not have the effect of changing the *normal retirement date* other than as described above.
Part 6A. Pension Credit Benefits

Method of Securing

6A.1 Where pension credit rights are allocated to an ex spouse or former civil partner following a pension sharing order, they will be treated independently from the rights of the scheme member from whose benefits the pension credit is derived. They may either:

- be retained in the same scheme as the member's and paid out from that scheme in due course, or
- transferred to another arrangement in accordance with paragraphs 6A.21 et seq.

Where the former applies, then, subject to Department of Social Security (DSS) requirements, it is entirely a matter for the scheme trustees to decide how to give effect to those pension credit rights in the scheme. An ex spouse or former civil partner who is initially given scheme membership may, subsequently, ask for a transfer of the pension credit rights if desired. The transfer of pension credit rights may be exercised independently of any benefit rights the pension credit member has under the transferring scheme as a result of being an employee of a participating employer.

Payment of Benefits

6A.2 Subject to any DSS requirements, scheme rules or the terms of a buy-out policy (see paragraph 10.42 et seq.) may allow pension credit benefits to be paid to the pension credit member at any time between age 50 and 75.

6A.3 The pension credit may be paid earlier than age 50:

- if the pension credit member is in exceptional circumstances of serious ill-health, or
- due to incapacity where the pension credit member is simultaneously taking benefits as a result of service as an employee, also on the grounds of incapacity, from the same scheme in which the pension credit is held, or
- on the death of the pension credit member.

6A.4 When pension credit rights become payable, they may be made under the annuity purchase deferral and income drawdown arrangements set out in Appendix XII.

Form of Pension Credit Rights

6A.5 Subject to any additional DSS requirements in relation to safeguarded rights (section 36 of the Welfare Reform and Pensions Act 1999 refers), the pension credit member may be given rights which broadly follow those available to the employee scheme member. So where, for example, an employee scheme member could exchange part of a pension for a lump sum at the time of retirement, the pension credit member may be given a similar option. Where, on the other hand, a pension credit member’s pension credit rights arise:

- from an arrangement which does not allow for a tax-free lump sum retirement benefit, for example a Free standing additional voluntary contribution scheme, or
- as a result of a pension sharing order which took place after the scheme member had already taken a tax-free lump sum retirement benefit under the scheme

the pension credit member may receive the pension credit rights in pension form only.

6A.6 Subject both to DSS requirements and paragraph 6A.5, the following benefits are available in
respect of pension credit rights:

- a pension

- a tax-free lump sum benefit for the pension credit member

- a tax-free lump sum death benefit payable where the pension credit member dies before the pension credit rights come into payment or, where the pension credit member dies after the pension sharing order is made, but before it is implemented by the scheme

- non-commutable pensions for any widow, widower, surviving civil partner or dependant of the pension credit member payable in the event of the pension credit member’s death, before or after pension credit rights have come into payment

- a pension guarantee (Paragraphs 12.9-12.12 refer)

- full commutation on grounds of triviality or exceptional circumstances of serious ill-health.

Limits on Pension Credit Rights Payable

6A.7 Subject to paragraphs 6A.18-20, there is no limit on the amount of pension a pension credit member may receive from pension credit rights.

6A.8 Subject to paragraphs 6A.5 and 8.3, the maximum lump sum payable to a pension credit member from pension credit rights arising other than under a simplified defined contribution scheme (see Part 22) is an amount equal to 2.25 times the initial annual rate of pension before commutation to be paid. Where the pension credit arises under a scheme whose rules provide for a pension and a separate lump sum rather than a commutable pension, the maximum is an amount equal to 3 times the initial annual rate of the separate pension. Where the pension credit rights arise under a simplified defined contribution scheme, the maximum tax-free lump sum is 25% of the fund underpinning the pension credit member’s pension credit rights at the time of payment (see paragraph 22.21).

Death of Pension Credit Member Before Payment of Pension Credit

6A.9 The maximum lump sum death benefit payable where the pension credit member dies either:

- before the pension credit rights come into payment or,

- after the pension sharing order is made but before it is implemented by the scheme, and irrespective of whether the scheme member’s benefits were in payment at the time of the order

is, where the pension credit rights arise other than under a simplified defined contribution scheme, 25% of what would have been the cash equivalent of the pension credit rights at the date of death. Where the pension credit rights arise under a simplified defined contribution scheme, a lump sum may in the above circumstances be paid out in accordance with paragraph 22.26.

6A.10 The maximum pension payable to a widow, widower, surviving civil partner or dependant of a pension credit member, where the pension credit member dies before payment of the pension credit rights under an approved scheme other than a simplified defined contribution scheme, is an amount not exceeding 2/3rds of the pension, before commutation, that could have been provided for the pension credit member on the date of death from the pension credit rights. Where the pension credit member is below age 50 at the date of death, an age 50 annuity rate should be
used to determine the pension that could have been provided to the pension credit member. For this purpose, the “age 50 annuity rate” must be determined either by an appropriate available market rate or by the scheme actuary.

6A.11 Where the category of widow, widower, surviving civil partner and dependants includes more than one person, separate pensions may be provided for each. No individual pension may exceed the limit set out in paragraph 6A.10 above nor may the total of the pensions to be paid exceed that which could have been provided for the pension credit member at the date of death. Pensions under paragraphs 6A.10 and 11 may be fully commuted on grounds of triviality (see paragraphs 6A.20 and 8.12-16). If there is no widow, widower, surviving civil partner or dependants of the pension credit member to whom such pensions can be provided, the balance of the cash equivalent should be treated as surplus under normal rules.

6A.12 There are no limits imposed on widows', widowers', surviving civil partners' or dependants' pensions where the pension credit rights arise from a simplified defined contribution scheme. Such pensions may be provided in accordance with Part 22.

Death of Pension Credit Member After Payment of Pension Credit

6A.13 Where a pension credit member dies after pension credit rights have come into payment under an approved scheme (including a simplified defined contribution scheme), a lump sum may be paid out under a 5 year guarantee (see paragraphs 12.10 and 22.29). Such a lump sum must not exceed the total of the instalments falling due after the pension credit member’s death.

6A.14 Where the pension credit member dies during the guarantee period and is drawing the pension credit rights under an income drawdown arrangement, the balance of instalments may be based on the amount of pension the pension credit member would otherwise have been receiving if he/she had opted for 100% withdrawal. For these purposes, 100% is determined at the date of commencement of income drawdown irrespective of any subsequent variations. Any undrawn amounts of pension (that is, the difference between 100% withdrawal and the amounts actually drawndown) for periods prior to the date of death may be paid in addition.

Widows', Widowers', surviving civil partners' and Dependents' pensions

6A.15 The maximum pension payable to a widow, widower, surviving civil partner or dependant of a pension credit member, where the pension credit member dies after payment of the pension credit rights under an approved scheme other than a simplified defined contribution scheme, is an amount not exceeding 2/3rds of the pension before commutation payable to the pension credit member from commencement, increased in proportion to the subsequent rise in the Retail Prices Index.

6A.16 Where the category of widow, widower, surviving civil partner and dependants includes more than one person, separate pensions may be provided for each. No individual pension may exceed the limit set out in paragraph 6A.15 above nor may the total of the pensions to be paid exceed that payable to the pension credit member from commencement, increased by the Retail Prices Index as in paragraph 6A.15. Pensions under paragraph 6A.15 and 16 may be fully commuted on grounds of triviality (see paragraphs 8.12-16). Again, where there is no widow, widower, surviving civil partner or dependants of the pension credit member to whom such pensions can be provided, the balance of the pension credit rights should be treated as surplus under normal rules.

6A.17 There are no limits imposed on widows', widowers', surviving civil partners' or dependants' pensions in these circumstances where the pension credit rights arise from a simplified defined contribution scheme. Such pensions may be provided in accordance with Part 22.

Pension Credit Member Also an Employee and Entitled to Benefits as an Employee Under Scheme

6A.18 Benefits paid from pension credit rights to a pension credit member or, in the event of the pension credit member's death, to the widow, widower, surviving civil partner or dependants of a
pension credit member, are not taken into account in applying the tax approval limits set out in Parts 7, 8 (subject to para 6A.20), 10, 11 and 12 to:

- benefits for the pension credit member as an employee scheme member
- benefits for the widow, widower, surviving civil partner or dependants of a pension credit member which arise as a result of that pension credit member’s employee scheme membership

Provided the rules of the scheme contain provisions which treat pension credit rights as provided separately from those rights which arise as an employee or the widow, widower, surviving civil partner or dependant of an employee.

6A.19 Where the scheme does not provide for separate treatment as in paragraph 6A.18 above, benefits paid in respect of pension credit rights, are taken into account in applying the tax approval limits set out in Parts 7, 8, 10, 11 and 12 to:

- benefits for the pension credit member as an employee scheme member
- benefits for the widow, widower, surviving civil partner or dependants of a pension credit member which arise as a result of that pension credit member’s employee scheme membership.

6A.20 As indicated in paragraph 6A.6 above, a pension credit member’s pension credit rights may be fully commuted on grounds of triviality. Where a pension credit member’s pension credit rights are provided from a scheme under which the pension credit member is also entitled to benefits as an employee, the benefits from the pension credit rights must be aggregated with those in respect of the employment for the purpose of the triviality limit in paragraph 8.12.

Transfers of Pension Credit Rights

Scope of transferability

6A.21 Pension credit rights for a pension credit member that have not come into payment may be transferred to another tax approved scheme of the same or different employer provided the pension credit member is already a member of the receiving scheme as a result of being an employee or an pension credit member in relation to the receiving scheme. The conditions set out in paragraphs 10.23-24 also apply to the transfer of pension credit rights.

6A.22 The pension credit member does not have to be an existing member of the receiving scheme of an employer if the transfer occurs due to the employer restructuring its pension arrangements (see Paragraph 10.22).

6A.23 A transfer can be made to an approved personal pension scheme regardless of whether or not the pension credit member is already a member of the personal pension scheme.

6A.24 Provided the terms and conditions of paragraph 10.39 and Appendix VI are observed, pension credit rights can also be transferred to an overseas scheme.

6A.25 Where pension credit rights for a pension credit member are transferred to a buy-out contract, that contract must satisfy the requirements set out in paragraphs 10.44-10.45, although no limit is required on pension (see paragraph 6A.7).

NIL certificates

6A.26 Where a pension credit member’s pension credit rights are transferred in circumstances where those rights cannot be taken in lump sum form (see paragraph 6A.5), a NIL certificate (see paragraph 10.35) must be provided to the receiving scheme by the transferring scheme. This certificate must accompany any subsequent transfer of the pension credit rights.

Transfer benefit

6A.27 Where pension credit rights are transferred to a scheme in which the pension credit member
has rights as an employee, their treatment will depend on whether paragraph 6A.18 or 6A.19 above applies.

6A.28 Where a pension credit member also has benefits in the same scheme as a result of being an employee of a participating employer, the pension credit rights can be transferred independently of the employee benefit rights. In circumstances where paragraph 6A.19 applies, the transferred pension credit continues to be treated as an aggregable benefit. If the pension credit and employee benefit rights are transferred together they may only be transferred in a manner acceptable to the transfer of employee benefit rights generally (see paragraphs 10.21 et seq.).

Taxation of Pension Credit Rights

6A.29 The taxation of pension credit rights is covered in Part 17.

Pension Credit Rights Payable from Annuities

6A.30 A pension sharing order might require an already purchased annuity to be shared following divorce where the terms of that annuity were such that on the pensioner member’s (first named annuitant’s) death, a pension is to be paid to the widow, widower or surviving civil partner of the deceased pensioner member (second named annuitant). Following the pension sharing order, the pensioner member’s ex spouse or former civil partner and the second named annuitant might be the same person. In such circumstances the pensioner member’s re-profiled ongoing annuity payments can be based on the pensioner member’s life only. This is provided that the ongoing amount does not exceed the maximum permissible amount that can be paid to the pensioner member, taking into account the pension debit.

6A.31 Alternatively, the annuity could be re-drawn on the basis of an annuity continuing to be paid on the death of the member to some other individual or individuals who qualify as a dependant of the member but were not originally nominated for such a benefit. This would be subject to the rules allowing for a reallocation of benefits.

6A.32 Basing the ongoing annuity payments on a single life basis would not be acceptable if the scheme to which the annuity relates pays a widow’s, widower’s or surviving civil partner’s pension to whoever is the member’s spouse or civil partner at the time of the member’s death.
Part 7. Total Benefits on Retirement

General

7.1 This Part sets out the maximum total benefits that may be provided on retirement under an approved scheme other than a simplified defined contribution scheme (see Part 22) for members who continue to accrue benefits until retirement. Maximum benefits are calculated by reference to an employee's length of service with the employer (see paragraphs 7.13 - 7.24) and his or her final remuneration.

Maximum Total Benefits

7.2 Total benefits are measured in terms of an annual pension for the member payable for life being the aggregate of any pension payable (including, where the member does not fall within the administrative easement described in paragraph 7.7, any pension debit) and the pension equivalent of any non-pension benefits (again including, where the member does not fall within the administrative easement described in paragraph 7.7, any pension debit). To arrive at the pension equivalent of the cash value of a non-pension benefit for the purpose of these limits on total benefits the cash value should be divided by 12. This applies regardless of the age or sex of the scheme member or of the rate of escalation attaching to the pension. For other purposes schemes may use whatever cash option factors are considered appropriate. (See however paragraph 7.57 for members with continued rights). Where in the case of a member not falling within the administrative easement described in paragraph 7.7, it is necessary to calculate a pension debit, the way in which this should be done is set out in paragraph 16.56.

7.3 The maximum aggregate benefit payable without taking account of retained benefits is a pension (of which part may be taken in lump sum form as described in Part 8) of 1/60th of final remuneration for each year of service (up to 40 years) (but see paragraph 7.10 in relation to controlling directors and paragraphs 7.25 and 7.26 in relation to aggregation of benefits).

7.4 Benefits greater than 1/60th of final remuneration for each year of service may be given up to a maximum of 1/30th of final remuneration for each year of service (up to 20 years) provided that the aggregate of the benefits in respect of service with the current employer together with any retained benefits does not exceed 2/3rds of final remuneration (but see paragraph 7.10 in relation to controlling directors and paragraphs 7.25 and 7.26 in relation to aggregation of benefits).

Administrative easements

7.5 The requirements of paragraph 7.4 are qualified for certain members by an administrative easement introduced in 1991 under which it is no longer necessary for retained benefits to be taken into account. This easement applies to new members after August 1991:

(a) who are not, and have not been within 10 years prior to joining the scheme, controlling directors in respect of the employment being pensioned, and

(b) whose earnings for the first year's employment following entry to the scheme (if a member of more than one scheme of the employer, the test is applied following entry to the first scheme) do not exceed 1/4 of the permitted maximum (determined at its level on entry). Except where it is clear from the outset that earnings exceed the threshold, the test will need to take place 12 months or so after the member joins the scheme. Schemes providing benefits on the basis of this paragraph may therefore wish to qualify any benefit promises given on joining.

7.6 Where a member joins a scheme of a new employer with an accrual rate of N/60ths or lower (N is as defined in paragraph 7.47), no retained benefits check is necessary (see paragraph 7.3 above). The payment of Additional Voluntary Contributions by the member at a later date which takes the accrual rate above N/60ths does not necessitate a retained benefits check provided the member's earnings for the first year following entry to the scheme did not exceed 1/4 of the permitted maximum calculated at the date of entry. Where the payment of Additional Voluntary Contributions
Contributions is commenced by a member who joined the scheme prior to the introduction of the permitted maximum, earnings in the year's employment following commencement of the initial Additional Voluntary Contribution should be used for the purpose of the 1/4 of the permitted maximum test.

7.6a From 5 April 2006 retained benefits can be ignored for any individual, including a controlling director, whose P60 earnings from a pensionable employment did not exceed £50,000 for the 2004/05 year of assessment. If the pensionable employment was not continuous for the whole of the tax year an annual rate for the P60 earnings must be calculated on a pro rata basis. For individuals, including controlling directors, whose pensionable employment ceased before 6 April 2004 retained benefits may be ignored if their P60 earnings in the last complete year of assessment for the employment did not exceed £25,000.

7.7 Under a further administrative easement, pension debits can be ignored in calculating the member's maximum permissible total benefits, both pension and lump sum under paragraph 7.2. This easement applies to members of schemes other than simplified defined contribution schemes except members:

- who are controlling directors (within the meaning in regulation 5(5) of the Retirement Benefits Schemes (Sharing of Pensions on Divorce or Annulment) Regulations 2000 No 1085), or

- whose earnings exceed 1/4 of the permitted maximum determined at its level for the year of assessment in which the marriage or civil partnership was dissolved. For this purpose earnings mean:

  those in respect of pensionable service to which the scheme relates, and which were received during the year of assessment immediately preceding the year of assessment in which the dissolution or annulment of the marriage or civil partnership occurred, and from which tax was deducted under PAYE.

The test is applied as at the date of divorce and once it is satisfied, the pension debit may be permanently ignored i.e. irrespective of subsequent employment changes.

This administrative easement will not generally be capable of being applied where the divorced member has already retired and is in receipt of benefits. In these circumstances, for the purposes of determining the member’s maximum approvable benefits in accordance with paragraph 9.1, the pension debit must always be brought into account.

Money purchase schemes

7.8 The limit in paragraph 7.4 is qualified in respect of a money purchase scheme. Benefits payable from such a scheme prior to normal retirement date cannot be restricted in accordance with that limit as a result of the relevant Department of Social Security (DSS) preservation legislation. In these circumstances the limit is as set out in paragraph 10.13 except that in relation to (b) of that paragraph there is substituted the actuarial equivalent of the total benefit the member could have expected to receive at normal retirement date.

Permitted Maximum

7.9 An employee without continued rights may not be provided with benefits calculated by reference to any measure of earnings greater than the permitted maximum. Thus in a scheme with an accrual rate of 1/80th of final remuneration for each year of service, a member earning more than the permitted maximum cannot be provided with benefits in excess of 1/80th of the permitted maximum for each year of service except by virtue of an augmentation provision in the scheme rules.

Controlling directors

7.10 When applying the limits in paragraphs 7.2 - 7.9 to benefits for a controlling director it is
necessary to treat as benefits provided by the current employer any benefits from retirement annuity contracts or personal pension schemes (including any pension debits derived from these sources) arising from premiums or contributions paid out of relevant earnings from that employer.

7.11 It is a condition of approval that the rules of schemes must specifically limit benefits in accordance with the requirements of this Part. In the light of Free standing Additional Voluntary Contribution Schemes and current DSS pensions requirements that the payment of Additional Voluntary Contributions must be allowed, it is no longer practicable to approve a scheme solely on the footing that the basic accrual of benefits thereunder is well within Inland Revenue limits.

7.12 Where an employer has a profit related pay (PRP) scheme, benefits may, if desired, be promised/targeted and calculated by reference to "shadow pay" (the remuneration the employee would otherwise have been receiving if the PRP scheme had not been introduced), so long as the benefits actually provided do not exceed Inland Revenue maxima calculated by reference to final remuneration. It is not acceptable to include any notional element in calculating final remuneration. If the retirement benefits promised before the introduction of the PRP scheme were close to the Inland Revenue maxima, it may be necessary to reduce the expected benefits. The application of the Inland Revenue maxima must therefore be clearly explained to affected members at the outset. This paragraph applies equally to continued rights members.

Service

7.13 For limits purposes, service means all years of service with the employer up to the date of retirement (but see paragraph 7.26 in relation to connected schemes) or earlier withdrawal from pensionable service (see Part 10). But see paragraph 10.14 in relation to an employee who withdraws from his or her employer's scheme and rejoins it later.

7.14 Benefits may not normally be provided for periods of service for which no remuneration is paid (but see paragraphs 3.11-3.15 in relation to temporary absence and secondment).

Change of employer

7.15 Subject to Part 1, an employer may only provide benefits in respect of service with that employer. Where an employee changes employers, in certain circumstances, the two employments may be treated as continuous for pension purposes. Paragraphs 7.15a - 7.21 set out when continuous service treatment is acceptable. Paragraph 7.21a contains a flowchart giving an overview of the various tests for continuous service treatment.

7.15a To qualify for continuous service an employee must actually move from one employer to another, i.e. leave one employer and then join another employer. Any gap between the two employments should not be more than 3 months. Where two employers employ an employee for any period at the same time (concurrent service) continuous service treatment is not allowable because the employee has not actually moved between employers. The concept of employment for continuous service purposes is wide. Employment includes:

- any period of employment with the employer with remuneration assessable under Schedule E;
- any period as a director of the employer, or as an officer of the company, e.g. company secretary - even if no remuneration was received for these duties;
- any period in which the member took an active part in the management of the affairs of the employer - even if no remuneration was received for these. (This does not include any duties normally carried out as a shareholder.)

There are two circumstances where a member may be in concurrent employment but still qualify
for continuous service:

1. Where the old employer is in the process of winding-up when the member starts employment with the new employer, and the period of overlap is less than 1 year;

2. Where the old employer is dormant when the member starts employment with the new employer. A dormant company is defined in section 249 AA of the Companies Act 1985 (as amended);

For the avoidance of doubt continuous service is not appropriate in the following circumstances:

- The member is employed as a director of company A. Company A becomes an investment company. The member is subsequently employed by company B but retains their directorship of company A. Service with company A as an investment company is no longer pensionable with a discretionary approved scheme under section 591 but the member is still in employment with company A. So the employments with company A and company B are concurrent. The service with company A may be pensioned through a mandatory approved scheme under section 590;

- The member is 'employed' by 2 companies X and Y. The member only receives remuneration from company Y. The member is also a director of company X. Even though the member is not remunerated the member is still in the service of company X, so service with companies X and Y is concurrent. Unremunerated service as a director may be pensioned, and company X may choose to pay the member remuneration at a later date.

7.15b In exceptional circumstances IR SPSS may agree that a period of concurrent service may be disregarded for the purposes of making a claim for continuous service treatment. Typically the circumstances in which concurrent service arose will be out of the control of the employee and could not have been foreseen. IR SPSS must agree the claim to disregard concurrent service. There is no set form for these circumstances. Claims should be made in writing giving all the details of:

- how the concurrent service arose;
- why concurrent service should be disregarded; and
- the details set out in sections A to F of form PS 155.

7.15c Where ( ) a business has been taken over, merged or reconstructed and an employee’s position before and after the change is essentially unchanged ( ) service with both employers may be treated as continuous service for the present employer. There is no straightforward test for whether or not a job is essentially unchanged. Typically the employee will be doing the same job in the same place. It is not a requirement that where an employee is a director for one employer they must be a director of both employers to be doing the same job. It is, however, unusual for an employee to be an ordinary employee, i.e. not a director, of one employer and a director of the other employer, yet still be doing the same job. Being a company director involves specific duties and responsibilities not normally carried out by an ordinary employee. But circumstances can arise where an employee is doing the same job yet moves from being a non-director to being a company director or vice versa. Typically the employee would have been in a senior position with one employer. Factors to consider are:

- the duties with each employer;
- the responsibilities with each employer;
- why the member was not a director of the one employer;
• why the member is now a director of the other employer;
• the circumstances in which the new employer took over the trade (or part trade) of the old employer.

7.16 *IR SPSS* will only accept service being treated as continuous for a controlling director where it can be shown that there is a continuity of trade. The main requirements to be satisfied are as follows:

(a) there has been a succession of trade from one employer to another, and

(b) if the whole of a company’s business has been purchased at least 75% of the vendor's liabilities have been assumed by the purchaser – unless paragraph 7.17 applies. In this context the 'whole of a business' means 90% or more. (See paragraph 7.18 for transfer of part of a trade.)

The following will also be taken into account as they will help to establish that true continuity exists:

(c) the extent to which the business assets and the employees of the predecessor company have been transferred to the successor company; and

(d) the extent to which the successor company serves the same customers as its predecessor.

7.16a Where the whole (90% or more) of the original business is split between two or more new businesses, at least 75% of the liabilities of the old business must be assumed by the new businesses. In these circumstances the fact that less than 75% is assumed by one or other of the new businesses would not in itself necessarily preclude the granting of continuous service. All the relevant facts relating to the transfer would have to be considered before a conclusion is reached. Again this is subject to paragraph 7.17.

7.17 Continuous service will not be accepted where the liabilities of the original company are not taken over by the successor company unless the purchase price for the buy-out of the business takes into account the fact that the liabilities will be retained by the vendor. In such cases a claim for continuous service would have to be supported by a copy of the sale agreement setting out the details.

7.18 Continuous service for a controlling director may be accepted where only part of a trade has been transferred to the new employer. Where the circumstances are such that the legislation on demergers as set out in sections 213-218 is satisfied continuous service treatment will be acceptable and no further evidence needs to be provided to *IR SPSS*. Where the conditions of the demergers legislation is not satisfied continuous service treatment may still be acceptable where there has been a genuine transfer of part of a business. However *IR SPSS* may ask for evidence that a transfer of trade has taken place.

7.19 Where a controlling director dies in service before a decision on a claim for continuous service has finally been reached then the death in service benefit may be given on the basis of continuous service.

7.20 Where an employee (including a controlling director) moves from one employer to another, (other than in a take-over, merger etc situation where paragraphs 7.15c - 7.18 apply), and those employers are associated employers, service may be treated as continuous for the purpose of benefit provision by the second employer. ( ). In the situation where the employers are associated by common control, but do not qualify for group relief under section 402, for a controlling director to qualify for continuous service the employers must have been so associated and carrying on a genuine commercial trading activity for at least one year before the move between employers. Where the move is between two employers who are associated only by virtue of a permanent community of interest, service may not be treated as continuous where the
individual concerned is a **controlling director** of either or both of the employers concerned.

7.21 Where the employee is a **controlling director** of the new employer it is necessary to make a claim for continuous service treatment to **IR SPSS**. A claim for continuous service in respect of a **controlling director** should be made on form PS155 – except where a claim is being made in accordance with paragraph 7.15b. Any claim for continuous service treatment must be made within 6 years of the employee leaving the old employment.

Form PS 155 is a self-certified claim form. **IR SPSS** normally has one year from the date of the continuous service claim in which to open an enquiry into the claim. If no enquiry has been made into the claim after one year continuous service treatment can be taken as accepted. During the one year enquiry window scheme administrators may proceed on the basis that continuous service treatment is acceptable.

The claimant can ask **IR SPSS** to specifically examine and agree the claim rather than waiting for the one year enquiry window to pass in the following circumstances:

- where benefits are to be paid; or
- transferred out of the scheme; or
- there is a **pension sharing order**

within the one year enquiry window. Such a request should be made in writing stating why **IR SPSS** needs to specifically examine the claim and when the benefit payment, transfer etc. needs to be made. There is no provision for this request on form PS155; it may be included in a covering letter.
7.21a Continuous Service Flowchart for Controlling Directors

Have you left one employer and then joined another? 7.15a
(* permitted exceptions to concurrency follow ‘Yes’ path

Yes

Has the new employer taken over the trade or part of the trade of the old employer?

No

Are the 2 employers associated?

Yes

Are you doing essentially the same job? 7.15c

No

Continuous service applies

Yes

Is this a demerger that satisfies the demerger legislation?

No

Is there continuity of trade as per PN 7.15c – 7.17?

Yes

No continuous service

No

Have the 2 companies been trading and associated by common control for at least 1 year before the date of joining the new employer?

No

No continuous service

Yes

Are the 2 companies part of the same group qualifying for relief under S.402?

No

Are the 2 companies associated by common control?

No

The companies must be associated by a permanent community of interest. No Continuous service.

Yes

Continuous service applies

7.22 An employee who rejoins his or her employer's scheme after a break in pensionable service
may be provided with benefits in respect of the aggregate of both periods. The general conditions relating to such provisions are set out in Appendix IV but see paragraph 3.5 about partners and paragraph 10.14 where the employee does not leave the employer’s service. Entitlement if any to continued rights will normally be governed by the date of rejoining the scheme regardless of when the employee first joined the scheme. Aggregation of both periods of service will not be possible where the member is entitled to continued rights for one period of service but not the other (see Appendix IV paragraph (b)).

7.23 Any refund of contributions taken in respect of the earlier period of pensionable service should be repaid to the scheme on rejoining if that earlier period is to be included for benefit purposes under the scheme. Where the employee makes such repayment it is regarded as a contribution for the purposes of paragraph 4.2 (unless the repayment takes place in the circumstances described in the last sentence of paragraph 17.26 in which case no tax relief will be due), but such repayment when aggregated with other contributions made in the same year of assessment, must not result in the total exceeding the amount which would qualify for tax relief (see paragraph 4.4) unless regulation 6 of the Retirement Benefits Schemes (Continuation of Rights of Members of Approved Schemes) Regulations 1990 (SI 1990 No 2101) applies.

7.24 As stated in paragraph 3.3 scheme membership may be extended to part-time employees. Benefits may be provided in accordance with Parts 6 - 12 by reference to years of part-time service and the remuneration from that part-time employment. Where, however, service for the employer consists of both part-time and full-time service the position is much more complex and special rules apply. For this purpose an employee working a basic week of 30 or more hours may be regarded as being in full-time employment. The basis for the calculation of benefits in these circumstances is set out in Appendix V.

Other Schemes

7.25 In determining whether the benefits to be provided under a retirement benefits scheme are within approvable limits, it is necessary to aggregate them with benefits provided for the employee under all other approved retirement benefits schemes or relevant statutory schemes providing benefits in respect of service with the same employer (or, where continuous service is granted, employers), and with some personal pension scheme benefits.

This includes -

- benefits from those sources which have been transferred into a buy-out policy or personal pension scheme (see definition of retained benefits and paragraph 7.10 for controlling directors) and any pension debits where appropriate (see paragraph 7.2), and

- (in respect of controlling directors without continued rights) benefits from a personal pension scheme of the same employer where eligibility to contribute to the personal pension scheme was under s632A (i.e. other than by "concurrency").

It does not include -

- benefits from a personal pension scheme of the employer which arise from contributions to that scheme during a period of eligibility through "concurrency" under s632B, which are ignored, and

- benefits from a personal pension scheme of the employer where eligibility to contribute to the personal pension scheme was under s632A (unless the member is a controlling director without continued rights - see above), which are taken into account as retained benefits.

7.26 For employees without continued rights it is also necessary to ensure that benefits from all connected schemes and Associated employments do not in aggregate exceed the maximum
approvable by reference to the permitted maximum and to aggregate service which gives rise to these benefits (no period to be counted more than once).

**Aggregation Example 1**

Assumptions

(a) no increase in the original level of the permitted maximum,

(b) no revaluation of deferred benefit and/or alternatively no increase in pension in payment during the 8 year period between the dates of leaving employments A and B.

An employee is a member of the schemes of both employer A and employer B which are connected. The employee has no retained benefits and the relevant data is:

Employer A - Service 18 years, 12 full-time and 6 part-time (while concurrently employed by employer B). Equivalent full-time service is 15 years.

final remuneration (full-time equivalent) is £50,000.

Maximum approvable pension would be £25,000 (i.e. 15/30 x £50,000).

Employer B - Service 14 years, 6 part-time and 8 full-time. Equivalent full-time service is 11 years.

final remuneration (full-time) is £80,000.

Maximum approvable pension would be £22,000 (i.e. 11/30 x final remuneration capped at £60,000).

Total permissible benefits are however restricted to £40,000 (i.e. 20/30 x £60,000) and the benefits of one or both of the schemes must be restricted so that the aggregate of the pensions does not exceed that figure.

**Aggregation Example 2**

Assumptions

(a) benefits with Employer A vest at normal retirement date,

(b) there is no increase in pension in payment from Employer A,

(c) the benefit from Employer B vests at normal retirement date.

The facts are as for Example 1 except that the employee has a Retained Benefit of a pension of £20,000 (valuation as at vesting date under employer A's scheme) and the benefits under the two schemes vest at different times.

Employer A

Maximum approvable pension is the greater of:

(a) 15/60ths of final remuneration = £12,500, and

(b) the lesser of:

(i) 15/30ths of final remuneration = £25,000, and

(ii) 2/3rds of final remuneration - £20,000 = £13,333.
Therefore the employee's maximum approvable pension is £13,333.

Employer B

Value of Retained Benefit has increased to £24,000, the unexhausted balance (see paragraph 16.55) is now £10,000 and the permitted maximum is now £64,800.

Maximum approvable pension would be the greater of:

(a) 11/60ths of capped final remuneration = £11,880, and
(b) the lesser of:

   (i) 11/30ths of capped final remuneration = £23,760, and
   (ii) 2/3rds of capped final remuneration (£43,200) less Retained Benefit (£10,000) = £33,200.

Therefore maximum approvable pension would be £23,760 giving an aggregate from both schemes of £37,093. But this aggregate must not exceed £28,080 i.e. the greater of:

(c) 26/60 x capped final remuneration (at the current vesting date) = £28,080, and
(d) 20/30 x capped final remuneration (£43,200) less the current valuation of the Retained Benefit (£24,000) = £19,200.

Thus the maximum pension payable by Employer B's scheme is £28,080 less £13,333 = £14,747.

Benefits From Other Schemes

7.27 A member of more than one scheme of the employer leaving employment before normal retirement date may choose, if entitled to do so (see paragraph 6.1), to take immediate benefits from one or more schemes whilst deferring benefits under the other scheme(s). If maximum benefits on that basis are being provided, no further benefits can accrue but the deferred benefits may be increased in accordance with paragraph 10.12 (but see paragraph 10.8(a) in relation to members with continued rights) or 10.15 - 10.18 as appropriate.

7.28 Paragraphs 7.25 - 7.27 should be borne in mind throughout this Part and other Parts dealing with limits on benefits in particular circumstances.

Department of Social Security (DSS) Contracting Out Requirements Take Precedence

7.29 All references to maximum benefits, whether in this Part or any other, are subject to the overriding requirement that each member of a scheme contracted-out under the relevant DSS pensions legislation must either:

   (a) be provided with a Guaranteed Minimum Pension ("GMP"), where necessary revalued on a statutory basis, or

   (b) be provided with Protected Rights

(unless either is extinguished by the payment of a State Scheme Premium). It may be necessary, in order to comply with the contracting-out requirements, to restrict the exercise of certain options under the scheme rules e.g. the payment of immediate pension on early retirement or the payment of a lump sum benefit before state pension age.

7.30 In a contracted-out money purchase (COMP) scheme, unless the rules limit the definition of "Protected Rights" to benefits derived from the payment of minimum contributions, all money
purchase benefits under the scheme are Protected Rights. If a COMP scheme is to be approved it should so limit the definition of Protected Rights.

Other Conditions For Approval

7.31 No pension shall be capable of being assigned or surrendered (but see Parts 6A and 8 on commutation of pension, paragraph 12.5 on allocation of pension to provide a pension for a widow, widower, surviving civil partner or dependant and paragraph 9.6 on employee's option). However, the ban on assignment or surrender is removed where a pension sharing order is made by the courts. These conditions apply to all pensions payable under approved schemes.

7.32 Subject to paragraph 6.1 and the conditions relating to the flexible use of AVCs – see Part II of Appendix XII a pension for the employee personally may not commence before actual retirement or leaving service (except that the employee's GMP and/or Protected Rights, and no more, may be paid from such date as is specified in the relevant DSS pensions legislation). It must be payable for life (and may be guaranteed to continue for a minimum period not exceeding ten years if longer) except that the rules may provide:

(a) for forfeiture in exceptional circumstances e.g. if the pensioner becomes bankrupt or attempts to assign his or her pension;

(b) for recovery by an employer under a lien rule of any money due to it through any criminal, fraudulent or negligent act or omission by the employee (see paragraphs 17.23 and 17.39(d));

(c) for termination at state pension age (see paragraph 7.33); and

(d) for the suspension of an early retirement incapacity pension should this no longer be justified on these grounds, or for the suspension of an early retirement pension should the employee resume his or her former employment. The basis for the provision of further benefits in circumstances where the employee returns to service with the former employer is set out in Appendix IV.

7.33 Where a pension commences before the employee reaches state pension age it is permissible for the pension to terminate at state pension age or for the annual rate of pension to be varied with a greater amount being paid up to state pension age, so that the pensioner's total income from the occupational and the State schemes taken together remains roughly constant throughout retirement.

7.34 A scheme providing terminating pensions may provide separate lump sum retirement benefits up to the usual limits (see Part 8). The pension may be guaranteed for a minimum period (see paragraph 7.32) or until state pension age if earlier.

7.35 A pension which varies in amount before and after state pension age should be valued for limits purposes as a level life pension of equal actuarial value but disregarding the actuarial value of cost of living pension increases.

7.36 It is permissible for an approved scheme to provide benefits on an accrual rate in excess of 1/60th of final remuneration for each year of service provided that the rules are framed to exclude the possibility that members will become entitled to a 2/3rds pension well before normal retirement date. This can best be done by expressing the entitlement for an employee who on entry, has potential service to normal retirement date in excess of that necessary to produce a 2/3rds pension using the scheme accrual rate, as a pension of 2/3rds of final remuneration on retirement at the normal retirement date. Members with shorter potential service may be promised benefits on the desired accrual rate.

7.37 Other than for members with continued rights (see paragraphs 7.54 - 7.56) or those who joined the scheme prior to 1 October 1991 continued life cover (i.e. cover after retirement or

Schemes with high accrual rates

Continued life cover
deemed retirement) may be provided under an approved scheme only for employees who retire before normal retirement date on grounds of incapacity. Such cover may not continue after normal retirement date nor may it exceed the pre-retirement life cover under the scheme although it may be increased in proportion to the increase in the Retail Prices Index for the period between incapacity retirement and normal retirement date. In these circumstances the cover will not be regarded as a retirement benefit and need not be taken into account for limits purposes. The benefits from such cover may be distributed in accordance with paragraph 11.5.

As an exception to this practice, a lump sum benefit on death in retirement up to a maximum amount of £2,500 may be paid. This applies equally to continued rights members. For the effect on limits see paragraphs 7.54 and 7.55.

Two-stage benefit payments

7.38 Where a member retires / dies during the winding-up of a scheme, it might not be possible to provide the member / widow, widower, surviving civil partner or dependant(s) with his / her full benefit (pension and / or lump sum) entitlement at the benefit payment date due to uncertainties about the values of the assets and liabilities of the scheme. In such circumstances IR SPSS will not object to the member’s benefit being paid in two stages: an initial benefits payment together with a further benefits payment if recalculation as part of the completion of the winding-up process leads to further entitlement. This is subject to the following conditions:

- there must be a suitable enabling provision in the scheme rules, and
- the payment of any further benefits must not cause total benefits to exceed the maximum approvable calculated as at the date benefits were first paid, and
- for individuals without continued rights whose lump sum retirement benefit from the initial benefits payment is calculated on the basis set out in paragraph 8.7, no further lump sum payment will be possible where the final payment is made after the end of the first year in which the pension from the initial benefits payment has been in payment.

Two-stage benefit payments should be an exception and not be regarded as an optional alternative to a single payment where such a payment can be made.

If an individual dies after benefits are paid but before final entitlement is calculated, any consequent further benefits should be dealt with in accordance with the provisions of Part 12 concerning death after retirement.

Continued Rights

7.39 The benefits which can be provided for a member with continued rights depend not only on the member’s length of service and final remuneration on retirement but also on whether he or she is retiring at, before or after normal retirement date. Paragraphs 7.40 - 7.42 deal with benefits payable at normal retirement date separately for the two categories of continued rights. Paragraphs 7.43 - 7.63 set out, for both categories, how those requirements are qualified by early or late retirement and any other differences from the practice set out in paragraphs 7.1 - 7.37.

Rules of schemes may give members the option, exercisable at any time before benefits commence, (but see paragraph A12.208 with regard to the payment of additional voluntary contributions benefits before main scheme benefits) are bought-out or otherwise transferred outside the employer's scheme(s), or attainment of age 75 whichever first occurs, to be granted benefits on the basis that they are and always have been members without continued rights. A member who exercises this option ceases to be entitled to continued rights.

Paragraph 7.3 above applies in respect of retirement at or before normal retirement date for members with continued rights in respect of benefits which may be given without having regard to retained benefits.
7.40 For members with pre 17 March 1987 continued rights, benefits greater than 1/60th of final remuneration for each year of service may be given on retirement at normal retirement date in accordance with the table set out below provided that the aggregate of the benefits (including any pension debits where appropriate (see paragraph 7.2)) in respect of service with the current employer together with any retained benefits does not exceed 2/3rds of final remuneration. Benefits on this scale, however, may be given without reference to retained benefits for a member other than a controlling director (see paragraph 7.5) whose earnings for the first year's employment following entry to the scheme do not exceed ¼ of the permitted maximum. Where such a member joins a scheme of a new employer with an accrual rate of N/60ths or lower and later commences to pay additional voluntary contributions which take the accrual rate above N/60ths, the position is as set out in paragraph 7.6.

Table

<table>
<thead>
<tr>
<th>Years of service to normal retirement date</th>
<th>Maximum pension expressed as a fraction of final remuneration</th>
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<tbody>
<tr>
<td>1-5</td>
<td>1/60 for each year</td>
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<tr>
<td>6</td>
<td>8/60</td>
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<td>7</td>
<td>16/60</td>
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<td>8</td>
<td>24/60</td>
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<td>9</td>
<td>32/60</td>
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<tr>
<td>10 or more</td>
<td>40/60</td>
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Fractions of a year may be interpolated into this scale.

7.40a The administrative easement in paragraph 7.6A also applies to members with pre 17 March 1987 continued rights.

7.41 For members with pre 1 June 1989 continued rights, benefits greater than 1/60th of final remuneration for each year of service may be given on retirement at normal retirement date. The maximum is 1/30th of final remuneration for each year of service (up to 20 years) provided that the aggregate of benefits (including any pension debits where appropriate (see paragraph 7.2)) in respect of service with the current employer together with any retained benefits does not exceed 2/3rds of final remuneration. For members whose earnings for the first year’s employment following entry to the scheme do not exceed ¼ of the permitted maximum and who are not, and have not been, controlling directors (see paragraph 7.5), the maximum benefit is a pension of 1/30th of final remuneration for each year of service (up to 20 years) without reference to retained benefits. Where such a member joins a scheme of a new employer with an accrual rate of N/60ths or lower and later commences to pay additional voluntary contributions which take the accrual rate above N/60ths, the position is as set out in paragraph 7.6.

7.41a The administrative easement in paragraph 7.6A also applies to members with pre 1 June 1989 continued rights.

7.42 The requirements of paragraph 7.10 do not apply to a controlling director entitled to continued rights. For such a director, any benefits payable from the relevant personal pension schemes or retirement annuity contracts are to be taken into account as retained benefits. The maximum total benefits for a controlling director with continued rights will be the greater of an amount calculated in accordance with paragraph 7.39 and an amount calculated in accordance with paragraphs 7.40/7.40a or 7.41/7.41a as appropriate.
Late retirement

7.43 For members with continued rights, the requirement at paragraph 6.1 that pensions should come into payment at age 75 does not apply and pensions may be enhanced by virtue of coming into payment later than normal retirement date. There are a number of options as to how and when benefits are taken and the extent to which they are enhanced.

7.44 Where the member remains in service all benefits may nevertheless be taken at normal retirement date or at any later date prior to actual retirement. Alternatively the member may take either the pension or the whole of the lump sum element of the benefits at normal retirement date or a later date while remaining in service and defer payment of the other element. After taking all or part of the benefits no further benefits can accrue for service after the date on which those benefits are taken except that any deferred pension may be:

(i) increased actuarially in respect of the period of deferment, or

(ii) increased in proportion to the increase in the Retail Prices Index during that period (see paragraphs 8.33 and 8.34 in respect of deferred lump sums), or

(iii) augmented to the maximum approvable at the date benefits were first taken.

Where the pension is increased under (iii) the augmented element may be increased in accordance with (i) or (ii).

7.45 Where the payment of all benefits is deferred beyond normal retirement date total benefits may be enhanced as follows:

(a) to take account of the full service to and final remuneration at the actual date of retirement as if that date was the normal retirement date, or

(b) by the addition of a further 1/60th of final remuneration (calculated at the date of actual retirement) for each extra year of service both after normal retirement date and in excess of 40 years up to an overall maximum of 45/60ths, or

(c) to the amount which could have been provided at normal retirement date increased either actuarially in respect of the period of deferment or in proportion to the increase in the Retail Prices Index during that period.

Controlling Directors

7.46 In respect of a controlling director with continued rights who defers the payment of benefits beyond normal retirement date no enhancement of pension under paragraph 7.45(b) or (c) may be given in respect of years of deferment before the attainment of age 70. If the director has taken a lump sum benefit at normal retirement date or later, the deferred pension may be increased during the period of deferment before attaining age 70 only in proportion to the increase in the Retail Prices Index during that period.

Early retirement

7.47 The maximum total benefits for a member with continued rights who retires (otherwise than on incapacity - see paragraph 6.2) before the normal retirement date are the greater of 1/60th of final remuneration for each year of service (up to 40 years) and a proportion of the maximum total benefits had the member completed his or her service to normal retirement date. This proportion is represented by the formula:

\[(N/NS) \times P\]

N is the number of actual years of service (up to 40 years)

NS is the number of years of potential service to normal retirement date (again up to 40 years)

P is the maximum pension approvable had the employee remained in service to normal
retirement date (see paragraphs 7.39 to 7.41) by reference to final remuneration calculated at the date of retirement.

Any restriction for retained benefits (see Part 16) must be made in arriving at P before applying the fraction N/NS.

Scheme rules may restrict the application of this formula to members whose earnings while a member of the scheme have exceeded £10,000 and who at the time of leaving pensionable service are 45 years of age or more. Where as a result of this restriction this formula does not apply, the maximum total benefits will be as set out in paragraphs 7.40 and 7.41 by reference to years of service to the date of retirement.

7.48 An early retirement benefit is normally an alternative to short service benefit under the preservation requirements. The relevant Department of Social Security legislation requires that alternatives to short service benefit should be at least equal in value on the date they become payable to the value of the short service benefit together with revaluation to normal retirement date where appropriate. If the preserved benefit is greater than the maximum under paragraph 7.46 no restriction can be applied and the preserved benefit may be paid (see also paragraph 7.8).

7.49 Where a scheme has equalised members’ normal retirement dates to comply with equal treatment law unequal benefits can still arise in respect of service for male and female members before the date of equalisation (where their respective normal retirement dates were different). Unequal benefits will only occur where benefits are calculated on a continued rights basis for early leavers and for early or late retirees (because tax approval limits pivot around the normal retirement date adopted by the scheme). Even though the length of pensionable service might be exactly the same, one sex could receive greater benefits than the other when retirement occurred either before or after a scheme normal retirement date. In some situations, members whose normal retirement dates have changed will receive better benefits as a result. In other situations they will be worse off than if their normal retirement date had remained unchanged, eg late retirement enhancement for women retiring after age 60 where the normal retirement date has been raised to 65. But calculations of benefits which attempt to accurately preserve rights accrued for periods of service during which different normal retirement dates applied can be complicated.

7.50 In recognition of the difficulties explained in paragraph 7.49 and in order to allow the maximum freedom for solutions to be provided, the following easements to our normal practice will apply where the normal retirement dates for males and females have been equalised, whether as a result of equal treatment law or following a corresponding scheme rule change:

(a) If, as a result of equalisation of male and female normal retirement dates under the scheme, a member’s benefits on retirement would be less than could have been paid had the normal retirement dates remained unequal, IR SPSS will not object to benefits being calculated and paid on the basis that the old unequalised normal retirement dates still applied for that member. (This easement does not give the member the right to take separate tranches of benefit at both the old and the new normal retirement date).

(b) In addition, because equal treatment law requires benefits to be levelled up for service between 17 May 1990 and the scheme rule change, benefits for a member retiring early on incapacity grounds during that period may be calculated by reference to service to the later of the male or female normal retirement date. Similarly, for death in service widow(er)’s, surviving civil partner’s dependant’s benefits based on the member’s potential incapacity pension (see paragraph 11.7).

(c) Where the application of the above easements would still result in the payment of unequal benefits for equal service, the benefits for a member of the disadvantaged sex may be calculated on the same basis as the advantaged sex even if normal Inland Revenue limits related to the old or the new normal retirement date would be exceeded for that member.
Payment of benefits under the terms of this paragraph can only be made if the scheme rules permit the payment of such benefits.

7.51 For the avoidance of doubt the easements detailed in paragraph 7.50:

(i) Only apply to continued rights members. No changes are required to tax approval limits under the Finance Act 1989 tax regime, as all aspects of that regime are non-discriminatory. Retirement benefit limits are subject to a straightforward 1/30th of final remuneration accrual formula on retirement at any time between age 50 and 75.

(ii) Apply to all members with continued rights, including those who joined after equalisation and those yet to join the equalised scheme. The easements are not limited to those who were members of the scheme when equalisation took place.

(iii) Apply equally to money purchase schemes where normal retirement dates are changed in order to provide equal treatment, notwithstanding that European Court of Justice’s decisions on equal treatment were made in the context of defined benefit schemes (since 1 January 1996, UK law has required equal treatment of members of money purchase schemes).

(iv) Allows benefit limits, for members within the scope of the easements, to be calculated relative to the current equalised normal retirement date, or either of the previous normal retirement dates (male or female). If the calculation produces unequal benefits for male and female members based on the same service and remuneration, then the higher level of benefits can be given to the disadvantaged sex even if normal Inland Revenue limits are exceeded.

(v) Apply also to the timing of benefit provision under the scheme. For example a male with continued rights could take benefits at the former female normal retirement date even if they have not reached the former male normal retirement date or the equalised normal retirement date.

7.52 The easements detailed in paragraphs 7.50 and 7.51 continue to apply if an employee’s benefits transfer from an equalised scheme to another scheme (the other scheme) in the following circumstances where:

(a) the equalised scheme is wound-up and replaced by a new scheme of the same employer;

(b) a new scheme of the same employer is set up because the employer has ceased to participate in an equalised centralised scheme;

(c) the employee becomes a member of another scheme by virtue of transferring from the current employer to an associated employer; or

(d) the employee becomes a member of a scheme of an employer who has acquired, been acquired by, merged with or taken over the whole or part of the business of the previous employer.

Payment of benefits under the terms of the easements can only be made if the rules of the other scheme permit the payment of such benefits. For the avoidance of doubt the easements do not apply to members with continued rights, who join the other scheme without having benefits transferred from the equalised scheme.

7.53 The easements described in paragraph 7.50 to 7.52 are made in the interests of simplicity and maximum flexibility. There is no compulsion on employers or trustees to adopt them, and they should be regarded as no more than setting an absolute maximum on the benefits calculation. It should not be inferred that benefits so calculated meet legal equalisation requirements, and it is for trustees to adopt a basis of calculation within the set parameters which satisfies those requirements. Employers or trustees of schemes which promise benefits up to existing Inland Revenue limits, but who do not wish to pay benefits in excess of those necessary to achieve
equality should consider whether their rules need amendment to limit their liability. Nothing in this paragraph and paragraphs 7.49 to 7.52 affects overriding requirements in the Pension Schemes Act 1993 or the Pensions Act 1995.

7.54 Where members with *continued rights* or those who joined the scheme prior to 1 October 1991 are given continued life cover under the scheme after retirement (other than on early retirement on grounds of *incapacity* or where the benefit does not exceed £2,500 in which case the terms of paragraph 7.37 apply) such cover is a retirement benefit and its value must be taken into account for the purpose of determining whether benefits are within approvable limits as follows:

(a) the single premium that would have to be paid to secure the life cover extending into retirement at the date of the employee's retirement is treated as a lump sum retirement benefit. This single premium cost must be taken into account in arriving at the maximum approvable lump sum retirement benefit payable to the employee under the scheme, and in any event must not exceed the maximum approvable lump sum retirement benefit payable to the employee under the scheme.

(b) For the purposes of ensuring that total benefits are within limits, the amount of pension that the single premium could secure under the scheme rules should be used in the case of members with *continued rights*. For members without *continued rights*, the pension equivalent is one-twelfth of the single premium in accordance with paragraph 7.2.

Where retirement takes place on or after the *normal retirement date* it should be assumed that the cover will continue for not less than three years unless the cover is in fact restricted to a lesser period. Where a member with *continued rights* remains in the employer's service after having taken benefits at or after *normal retirement date*, continued life cover should not extend beyond the actual date of retirement.

7.55 Continued life cover providing a lump sum death benefit which does not exceed £2,500 need not be taken into account for limits purposes. Where death in service life cover is renewed on its anniversary for a period of one year in the normal expectation of continued employment but prior to the end of that period the employee retires, the cover may be allowed to continue until the expiration of the period of one year. In these circumstances the cover which continues after retirement will not be regarded as a retirement benefit and so will not require to be taken into account for limits purposes.

7.56 The death benefits payable from life cover under paragraph 7.54 must be distributed in one of the ways described in paragraph 11.12; but where the benefits do not exceed £2,500 they may instead be distributed in accordance with paragraph 11.5. The cover may be provided under a group life policy held by the scheme *administrator* provided that it does not extend beyond *normal retirement date*. Cover after that date may not be provided out of exempt funds if other than term life policies are used - it may be provided either from a separate policy which does not qualify for pension business treatment under section 431(B)(2) (though it will be an exempt policy under section 266(10)(b)) or funded by direct payment by the employer to the *administrator* when the occasion arises (in which case the rules must specify the employer's liability to make such contributions to the scheme).

7.57 For members with *continued rights* the divisor in paragraph 7.2 for determining the pension value of lump sums is not mandatory. The relationship between lump sum and pension may instead be calculated on an approved basis appropriate to the particular scheme which (subject to variations of age) should be consistent for all members with *continued rights* in a scheme or schemes which have a substantial common membership. Where, however, there are differences of benefit levels as between categories of employee, separate commutation factors for each category may be adopted.

7.58 Commutation factors fall within two broad categories depending on whether or not they take account of the value of any entitlement to cost of living post-retirement increases on the pension. Factors which do take account of such increases are commonly referred to as "enhanced" and are
not appropriate to a scheme giving no such entitlement (but see paragraph 7.62 below in relation to schemes which provide for regular reviews and an expectation of resultant increases).

7.59 For schemes not using enhanced factors, commutation factors in the range 10.2 - 11.0 at age 60 and 9.0 - 9.8 at age 65 may be used for members of either sex (the appropriate point within the range being determined taking account of the ratio of male to female members of the scheme. This ratio should take account of service/benefit experience of male/female members and not simply their numbers.). Values for other ages within the acceptable range for normal retirement may be calculated by adding or subtracting 0.02 per month of age difference. The factors are acceptable whether pensions are guaranteed for 5 or 10 years or not guaranteed at all, irrespective of whether payments are in advance or in arrear and regardless of the frequency of payments. Where a scheme proposes to adopt commutation factors outside the ranges mentioned above the specific approval of IR SPSS must be sought.

7.60 It is not possible to produce a table of enhanced factors that will be common to all schemes because schemes have different levels of post-retirement increases. Tables for individual schemes should be based on an assumption of an overall gross interest yield of not less than 8% per annum. Where schemes provide for post-retirement increases at a rate exceeding 5% per annum (but restricted by reference to the Retail Prices Index) the factors should be based on the assumption that the yield will exceed the rate of pension increase by at least 3%. Where non-gender specific enhanced commutation factors (unisex) are adopted and it is not desired to use the divisor in paragraph 7.2, they should be based on assumptions that would be acceptable for male members.

7.61 When submitting a table of commutation factors to IR SPSS for agreement, the assumptions of yield and mortality should be quoted.

7.62 If the rules of a scheme provide for pensions to be reviewed regularly and increased (within the limit of the rise in the cost of living) at the discretion of the employer or administrator if funds permit, enhanced commutation factors may be used provided that a certificate by an actuary is furnished stating the anticipated percentage rate of future increases on the basis of the current annual contributions without taking into account any future special contributions which the employer might make.

7.63 A scheme may provide for individual calculations by a qualified actuary for every commutation. These must be consistent with other calculations made for the same individual and for other purposes of the scheme having regard to changing financial conditions.
Part 8. Lump Sum Benefits

General

8.1 This Part sets out the maximum lump sum retirement benefits that may be provided under an approved scheme. As with total benefits (see Part 7) the basic level of lump sum benefits which are approvable is calculated by reference to an employee's length of service with his or her employer (see paragraphs 7.13 - 7.24) and his or her final remuneration. Larger lump sum benefits may be possible, limited by reference to a multiple of total pension benefits.

8.2 Lump sum retirement benefits must normally be paid only once and at the time of retirement (except for members with continued rights – see paragraph 8.34) when the employee’s pension becomes payable.

However, there certain occasions when a second lump sum may be paid, including the following:

- the member's benefits include a guaranteed minimum pension (GMP) and, if the member were to exercise a commutation option, it would not be possible to establish with certainty whether sufficient funds will be available to meet the liability to pay the GMP at the date it becomes payable. In these circumstances, to meet contracting-out requirements, the scheme rules may require the scheme trustees to deny or restrict the option to commute. If so, the lump sum or a further lump sum can be taken at the date the GMP becomes payable. See also paragraph 7.29.

- the member's final remuneration cannot be precisely established at the relevant date because the tax liability has not been determined on all the constituent elements of the member's remuneration for all the years in question. See NB 2 to the glossary definition of final remuneration for the conditions for this exception.

- the scheme is in the process of winding-up and the trustees cannot establish precisely the value of the assets and liabilities in the scheme for all the years in question.

- following a court ruling, a court orders the scheme to recalculate benefits. “Court” here includes an Employment Tribunal and the Pensions Ombudsman.

- re-instatement of rights within an occupational pension scheme following personal pension misselling where the individual concerned retired before redress could be paid. The compensation received by the scheme can be used to provide additional pension and lump sum benefits within Inland Revenue limits.

- an employee has taken benefits from an occupational pension scheme but is subsequently provided with backdated membership relating to part-time service (following the decision in the Preston case). This exception applies where an employer is providing additional benefits from an occupational pension scheme whether or not this is as the result of a ruling from an Employment Tribunal.

An additional taxable lump sum may be paid where:

- a pension in payment is commuted on grounds of triviality (see paragraphs 8.14 and 14.8);

- backdated increases are awarded to a pension in payment and the arrears of pension are paid in a lump sum.

8.2A With effect from 20th December 2002, where a lump sum payment to a member was miscalculated due to a genuine error on the part of the trustees/administrator and the miscalculation falls within the circumstances set out below, a further payment made solely to correct the original miscalculation will not constitute a second lump sum. Instead this will be
treated as part of the original lump sum payment. In these circumstances the further payment will enjoy the same tax treatment as if it had been paid as part of the original lump sum.

The circumstances are:

- the miscalculation occurred as a result of a genuine and demonstrable error. This includes arithmetical mistakes and the failure to take into account an objective factor in calculating the lump sum (e.g. overlooking another scheme of the employer or forgetting about AVCs). It does not cover a change of mind on the part of the member (see also the third bullet below regarding this);
- there can be only one such re-calculation for each member;
- the re-calculation must be made on exactly the same basis as it should have been made on the date of the first payment. In particular no alteration to the basis of calculation should be made for any change in circumstances or change in intention of the member since the date of payment of the first lump sum;
- if the member was a controlling director of the company which is an employer in relation to the scheme, written authority to make the further payment should be obtained from APSS Pension Compliance, PO Box 62, Castle Meadow Road, Nottingham NG2 1BG before the payment is made.

Note: This practice relates solely to innocent miscalculations of the lump sum and should not be applied in any other circumstance. Tax geared penalties may be chargeable if it is applied in any other circumstance. If the result of the miscalculation is that the original tax free lump sum was excessive then the excess will be taxable under section 600.

8.3 Commutation must not be permitted to allow retirement benefits arising from a member's Additional Voluntary Contributions to be taken in lump sum form. Pensions arising from voluntary contributions (including Free standing Additional Voluntary Contributions) may nevertheless figure in the calculation of the lump sum provided they are not themselves commuted. The restriction on commutation does not apply to contributions under arrangements entered into by the employee before 8 April 1987.

8.4 If scheme rules provide for a pension and a separate lump sum rather than a commutable pension, Additional Voluntary Contributions may directly produce lump sum benefits where at the outset a contract is entered into to purchase a number of added years, which will produce a precise level of pension and lump sum benefit.

**Maximum Lump Sum Benefits**

8.5 The maximum lump sum benefit payable without taking account of the level of total benefits being provided for the employee (but see paragraph 8.9 in relation to controlling directors) is 3/80ths of final remuneration for each year of service (up to 40 years). A member for whom no pension is provided cannot be given a lump sum greater than 3/80ths of final remuneration for each year of service (up to 40 years). For the purpose of this paragraph, service may include potential service to normal retirement date after early retirement on grounds of incapacity (see paragraph 6.2).

8.6 Where in an approved scheme providing lump sum retirement benefits only which do not exceed 3/80ths of final remuneration for each year of service, a member's benefit entitlement is permanently reduced following a pension sharing order and the member does not fall within the administrative easement described in paragraph 7.7, the maximum lump sum benefit is:

- an amount determined in accordance with the scheme rules, but
- reduced by the amount of the lump sum allocated to the pension credit member.
For the purpose of this reduction, the amount of the lump sum allocated to the pension credit member at the date of divorce should be increased between that date and the date that the member takes his or her lump sum retirement benefit. The increase in that period should be in accordance with the statutory Revaluation Order in force at the date the member takes his or her lump sum retirement benefit.

8.7 Lump sum benefits greater than 3/80ths of final remuneration for each year of service may be given, up to an amount equal to 2.25 times the initial annual rate of pension to be paid i.e. before commutation and any allocation to provide benefits for a widow, widower, surviving civil partner and/or any dependants in accordance with paragraph 12.5. The initial rate of pension here in the context of paragraph 7.33 means the greater amount paid up to state pension age but in the context of paragraph 9.6 means the pension paid after the option has been exercised. Where scheme rules provide for a pension and a separate lump sum rather than a commutable pension, the maximum is an amount equal to 3 times the initial annual rate of the separate pension (but see paragraph 8.9 in relation to controlling directors).

8.8 The limits in paragraphs 8.5 and 8.7 do not apply where a member's benefit entitlement in a scheme is permanently reduced following a pension sharing order and the member does not fall within the administrative easement described in paragraph 7.7. In these circumstances the maximum lump sum benefit is:

- where the lump sum is obtained by commutation of pension, 2.25 times the initial annual rate of pension as in paragraph 8.7 above after reduction to take account of the pension debit.
- where scheme rules provide for a pension and a separate lump sum rather than a commutable pension, 3 times the initial annual rate of the separate pension after reduction to take account of the pension debit.

(But see paragraph 8.9 in relation to controlling directors).

8.9 When applying the limits in paragraphs 8.5 - 8.7 to lump sum benefits for a controlling director it is necessary to treat as provided by the current employer any lump sum benefits received or receivable from retirement annuity contracts or personal pension schemes (including any pension debits derived from these sources) arising from premiums or contributions paid in respect of relevant earnings from that employer.

Other Schemes

8.10 Paragraphs 7.25 - 7.27 are relevant to the calculation of maximum approvable lump sum benefits. If, in circumstances where paragraph 7.27 applies in relation to paragraph 7.25 and the first benefits paid are, or include, a lump sum, any deferred benefits may only be in lump sum form to the extent permissible under paragraphs 8.5 - 8.7. Where the lump sum is calculated on the basis of 3/80ths of initial remuneration for each year of service (up to 40 years), the deferred lump sum may be increased in line with the rise in the Retail Prices Index.

Department of Social Security (DSS) Requirements

8.11 In general the preservation requirements of the relevant DSS pensions legislation do not directly apply to the provision by schemes of retirement benefits in lump sum form because those requirements relate to the overall quantum rather than the form of benefits. However, in a scheme providing lump sum retirement benefits only or a separate lump sum, such lump sums are subject to the preservation requirements.

Commutation of Trivial Pensions

8.12 Commutation of trivial pensions is permitted to save life offices and fund managers the expense of recurring small payments. If the aggregate of total benefits payable to the employee...
under all schemes providing benefits in respect of the employment does not exceed the value of a
pension of £260 per annum the pensions, including any arising from the payment of voluntary
contributions (including Free standing additional voluntary contributions) may be commuted. For
this purpose, the aggregate of total benefits does not include a pension debit but where a pension
credit member is an employee, must include a pension credit (see paragraph 6A.20). If
commutation (under paragraphs 8.5 - 8.9 of part of a greater pension than £260 leaves a residual
trivial pension this may not then be commuted on grounds of triviality.

8.13 Payments in commutation of trivial pensions may give rise to tax charges on the scheme
administrator under section 599 (see paragraph 17.27). The scheme rules may allow the
administrator to recover this liability out of the commutation payment to the member.

8.14 Commutation of a trivial pension should normally take place at the time the pension becomes
payable. Trivial pensions which are not yet payable may be commuted if the scheme is winding-up.
The current value of the aggregate benefits should be used to determine whether the pension
is trivial. A pension already in payment may be commuted for triviality in the following
circumstances:

(a) on the occasion of an increase in the measure of a trivial pension if the pension in
payment is trivial under the new measure but not under the old;

(b) at state pension age where the guaranteed minimum pension has been revalued in line
with earnings and total pension then proves to be £260 per annum or less.

(c) on the occasion of a change in scheme rules to allow commutation on triviality grounds.
Any such change of rules must be consistent with the conditions in paragraph 8.12 and the
member's agreement to the commutation of their pension under the change of scheme rules
must have been obtained.

8.15 A pension secured by an annuity contract or policy bought in the name of the employee or
assigned to the employee on winding-up or after leaving service, may not be commuted on
grounds of triviality unless arrangements satisfactory to the Inland Revenue have been made by
the life office concerned for payment out of the policy proceeds of any tax due under section 599.
This principle applies also where pension credit rights for a pension credit member are secured
under an annuity contract or policy (see Part 6A).

8.16 The rules for commutation of trivial pensions set out above apply also to pensions for widows,
widowers, surviving civil partners or dependants. The occasions on which such commutation may
take place are extended to include the time at which the member's or pension credit member's
own pension is commuted on grounds of triviality. Widows', widowers', surviving civil partners' or
dependants' pensions which are commuted on grounds of triviality are not subject to a tax charge
under section 599. Widows', widowers', surviving civil partners' or dependants' pensions are not
commutable in any other circumstances (see also paragraph 8.21).

8.17 An approved scheme may permit a member who is in exceptional circumstances of serious ill-
health to commute the whole of his or her own pension (other than GMP and / or "Section 9(2B)
Rights and, where the member is married or in a civil partnership, at least half of any Protected
Rights) at the time it becomes payable. But for a controlling director the prior agreement of IR
SPSS is required (see paragraph 8.22). An approved scheme may also permit pension credit
member's pension credit rights to be fully commuted, if, when they become payable under
paragraph 6A.2 or earlier under paragraph 6A.3, the pension credit member is in exceptional
circumstances of serious ill-health. The prior agreement of IR SPSS is required where the pension
credit member is also a controlling director of an employer in relation to the scheme holding the
pension credit.

If the pension credit member is under age 50 at the time of full commutation on the grounds of
exceptional circumstances of serious ill-health, an appropriate age 50 annuity rate can be used to
determine the amount of pension that could have been provided for the pension credit member
from the pension credit benefits. The deductible lump sum for the purpose of the tax charge under
section 599 of the *Taxes Act* can be calculated by reference to the amount of pension that would have been payable using the appropriate age 50 annuity rate.

8.18 The term "exceptional circumstances of serious ill-health" is to be interpreted strictly and narrowly. It is not intended to refer to the kind of ill-health which prevents somebody from working but to cases where the expectation of life is unquestionably very short i.e. less than 1 year. Commutation on these grounds should not take place unless the administrator is satisfied by adequate medical evidence that this is the case and that the expectation of life is measured in months rather than years and so short that a pension is not a reasonable provision.

8.19 Full commutation in these circumstances gives rise to a charge to tax under section 599 (see paragraph 17.27).

8.20 An employee leaving service in mid-career in such serious ill-health may receive a commutation payment immediately, on the footing that he or she is retiring on *incapacity* grounds. An employee who has left service with an entitlement to a deferred pension and who becomes seriously ill before the pension commencement date may be permitted to commute the pension immediately. If the deferred pension is secured by an annuity contract in the name of or assigned to the employee, it may not be commuted on these grounds unless arrangements have been made for the payment of any tax due under section 599 (cf. paragraph 8.15). This latter principle applies also where *pension credit* rights for an *ex spouse* or *former civil partner* are secured under an annuity contract or policy.

8.21 Full commutation of widows', widowers', *surviving civil partners* or *dependants*' pensions on grounds of exceptional circumstances of serious ill-health is not permissible.

8.22 In the case of a *controlling director* regulation 9 of the Information Powers Regulations requires the administrator to give 14 days prior notice of the intention to fully commute benefits in circumstances of serious ill-health. Copies of documents relating to the decision of the administrator of the scheme to permit full commutation of benefits to lump sum form on retirement on grounds of serious ill-health, including copies of medical reports and other documents in the possession or under the control of the prescribed person containing details of the medical evidence which formed the basis of that decision, should be furnished. Provided all the information required is furnished by the prescribed time the onus will be on *IR SPSS* to say before the notification period has expired whether or not the proposal is acceptable. It is implicit in the Regulations that if nothing is heard to the contrary within 14 days the administrator is entitled to assume that the proposals are satisfactory, provided that they are consistent with the scheme rules and *IR SPSS* requirements in the first place. Notifications should be sent to *IR SPSS*, Compliance Audit Section. It is acceptable in the first instance for this information to be sent by fax (0115 974 1480). The original documents should then be sent by post in the normal way.

**Continued Rights**

8.23 As with total benefits the maximum lump sum which can be provided for a member with *continued rights* depends not only on his or her length of service and *final remuneration* on retirement but also on whether he or she is retiring at, before or after *normal retirement date*. Paragraphs 8.24 - 8.32 deal with lump sum benefits payable at *normal retirement date* separately for the two categories of *continued rights*. Paragraphs 8.33 - 8.40 set out for both categories how those requirements are qualified by early or late retirement.

8.24 The maximum lump sum benefit payable at *normal retirement date* to members with *continued rights* without taking account of *retained benefits* is 3/80ths of *final remuneration* for each year of service (up to 40 years).

8.25 For members with *pre 17 March 1987 continued rights* lump sum benefits greater than 3/80ths of *final remuneration* for each year of service may be given on retirement at *normal retirement date* in accordance with the table set out below provided that the aggregate of the value of non-pension retirement benefits in respect of service with the current employer and any *retained
benefits does not exceed 1.5 times final remuneration (see however proviso (iv) of that definition).

Table

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<tr>
<th>Years of service to normal retirement date</th>
<th>80ths of final remuneration</th>
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<td>1 to 8 years</td>
<td>3 for each year</td>
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<td>108</td>
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<td>20 or more years</td>
<td>120</td>
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Fractions of a year may be interpolated into the scale in accordance with the Occupational Pension Schemes (Maximum Rate Lump Sum) Regulations 1987 (SI 1987 No 1513).

Continued Rights

8.26 The limits in paragraphs 8.24 and 8.25 do not apply where a member's benefit entitlement in a scheme is permanently reduced following a pension sharing order and the member does not fall within the administrative easement described in paragraph 7.7. In these circumstances the maximum lump sum benefit is:

- where the lump sum is obtained by commutation of pension, the greater of:
  - 2.25 times the initial annual rate of pension as in paragraph 8.6 above after reduction to take account of the pension debit, or
  - an amount determined in accordance with the scheme rules as if there had been no pension share, but then reduced by 2.25 times the amount of pension from the pension debit calculated at the member's normal retirement date in accordance with paragraph 16.56.

- where scheme rules provide for a pension and a separate lump sum rather than a commutable pension, the greater of:
  - 3 times the initial annual rate of the separate pension after reduction to take account of the pension debit, or
an amount determined in accordance with the scheme rules as if there had been no pension share, but then reduced by 3 times the amount of pension from the pension debit calculated at the member's normal retirement date in accordance with paragraph 16.56.

8.27 For members with pre 1 June 1989 continued rights where benefits are granted at a rate of 1/60th of final remuneration for each year of service (up to 40 years) or less, the maximum lump sum available by commutation is 3/80ths of final remuneration for each year of service (up to 40 years). Where benefits are granted at a rate of 1/30th of Final remuneration for each year of service (up to 20 years) lump sum benefits will be granted in accordance with the table in paragraph 8.25 above.

8.28 Where benefits are granted at a rate of between 1/60th and 1/30th of final remuneration for each year of service the maximum lump sum available by commutation will be 3/80ths of final remuneration for each year of service plus a percentage of the difference between 3/80ths of final remuneration and the maximum under the table in paragraph 8.25. The maximum lump sum can be calculated by the formula:

\[
\left( \frac{(A - B)}{(C - B)} \right) \times (D - E) + E
\]

where:

A is the scheme pension payable (excluding any pension payable from transfers; see paragraphs 10.31-10.33) expressed in monetary terms, before any reduction to take account of commutation or allocation for widows' widowers' surviving civil partners' dependants' benefits and in the circumstances set out in paragraph 7.33 is the initial amount of pension payable up to state pension age.

B is a pension equivalent to 1/60th of "relevant annual remuneration" for each year of service (up to 40 years) before any deductions as at A above. "Relevant annual remuneration" means final remuneration or, if the scheme provides for benefits to be calculated on some other remuneration, that other remuneration.

C is a pension equivalent to 1/30th of "relevant annual remuneration" for each year of service, (up to 20 years) before any deductions as at A above.

D is a sum equivalent to the number of 80ths of "relevant annual remuneration" appropriate for the total years of service as shown in paragraph 8.25.

E is a sum equivalent to 3/80ths of "relevant annual remuneration" for each year of service (up to 40 years).

In calculating the maximum permissible lump sum in respect of a pre 1 June 1989 continued rights member the value of any retained benefits in non-pension form may be ignored.

8.29 For members with pre 1 June 1989 continued rights of schemes which provide separate lump sums the formula in paragraph 8.28 should be amended by substituting 1/80th for 1/60th in B and 1/40th for 1/30th in C.

8.30 When calculating lump sum benefits for members with pre 1 June 1989 continued rights, final remuneration or relevant annual remuneration should not exceed £100,000 (or such other figure as may be prescribed by the Treasury) - see proviso (vi) to the definition of final remuneration in the glossary.

Where such a member's lump sum is calculated by reference to the formula in paragraph 8.28, final remuneration or relevant annual remuneration used in D and E of the formula must be limited accordingly.
8.31 The limits in paragraphs 8.27 - 8.29 do not apply where a member's benefit entitlement in a scheme is permanently reduced following a pension sharing order and the member does not fall within the administrative easement described in paragraph 7.7. In these circumstances the maximum lump sum benefit is an amount calculated in accordance with paragraph 8.8.

8.32 The requirements of paragraph 8.9 do not apply to a controlling director entitled to continued rights. For such a director with pre 17 March 1987 continued rights any lump sum benefits payable from the relevant personal pension scheme or retirement annuity contracts are to be taken into account as retained benefits. For such a director with pre 1 June 1989 continued rights, any retained benefits in non-pension form may be ignored (see paragraph 8.28 above).

8.33 The requirement of paragraph 8.2 that lump sum benefits should be paid when the member's pension comes into payment does not apply to members with continued rights. Such a member has the option to take his or her lump sum without commencing his or her pension, at any time from the normal retirement date to the date of actual retirement (see paragraph 7.44). Alternatively the member may take his or her pension and defer the payment of the lump sum. After taking all or part of the benefits no further benefits can accrue for service after the date on which those benefits are taken though any deferred lump sum may be increased by an amount representing interest in respect of the period of deferment. The rate of interest should be reasonable i.e. commensurate with the return on the scheme investments.

8.34 Where the payment of all benefits is deferred beyond normal retirement date the lump sum may be enhanced as follows:

(a) to take account of the full service to and final remuneration at the actual date of retirement as if that date was the normal retirement date, or

(b) by the addition of a further 3/80ths of final remuneration (calculated at the date of actual retirement) for each extra year of service both after normal retirement date and in excess of 40 years up to an overall maximum of 135/80ths, or

(c) to the amount which could have been provided at normal retirement date increased by an amount representing interest at a rate commensurate with the return on the scheme’s investments in respect of the period of deferment.

8.35 Where a member's benefit entitlement in a scheme is permanently reduced following a pension sharing order and the member does not fall within the administrative easement described in paragraph 7.7, the maximum approvable lump sum benefit under paragraphs 8.33 and 8.34 must be suitably restricted (i.e. under paragraph 8.8, 8.26 or 8.31 as appropriate) at the relevant date to take account of the pension debit (see paragraph 16.56).

8.36 In respect of a controlling director with continued rights who defers payment of benefits beyond normal retirement date no enhancement of lump sum under paragraph 8.34 (b) or (c) may be given in respect of years of deferment before the attainment of age 70. If such a director has taken the pension benefit at normal retirement date or later, the deferred lump sum may be increased during the period of deferment in proportion to the increase in the Retail Prices Index during that period.

8.37 The maximum approvable lump sum benefit for a member with pre 17 March 1987 continued rights who retires (otherwise than on incapacity - see paragraph 6.2) before the normal retirement date is the greater of 3/80ths of final remuneration for each year of service (up to 40 years) and a proportion of the maximum approvable lump sum benefit had the member completed his or her service to normal retirement date. This proportion is represented by the formula:
Where

\[ \frac{N}{NS} \times LS \]

N and NS have the same meaning as in paragraph 7.47.

LS is: the maximum lump sum approvable had the employee remained in service to normal retirement date (see paragraph 8.25) by reference to final remuneration calculated at the date of retirement. Any restriction for retained benefits (see Part 16) must be made in arriving at LS before applying the fraction N/NS.

8.38 The maximum approvable lump sum benefit for a member with pre 1 June 1989 continued rights who retires (otherwise than on incapacity - see paragraph 6.2) before normal retirement date is the greater of 3/80ths of final remuneration for each year of service (up to 40 years) and an amount calculated in accordance with paragraph 8.28 above. Where total benefits are granted at a rate of 1/30th of final remuneration for each year of service (up to 20 years) or where \( \frac{A - B}{C - B} \) in the formula in paragraph 8.28 is equal to or exceeds 1, the maximum approvable lump sum is calculated by reference to the table in paragraph 8.25 to determine LS and the fraction N/NS (as above) is then applied to the result.

8.39 The limits in paragraphs 8.37 and 8.38 do not apply where a member's benefit entitlement in a scheme is permanently reduced following a pension sharing order and the member does not fall within the administrative easement described in paragraph 7.7. In these circumstances the maximum approvable lump sum benefit is an amount calculated under paragraph 8.8, 8.26 or 8.31 as appropriate but substituting the date of early retirement for normal retirement date.

8.40 A person who is entitled to continued rights and is a member of more than one scheme providing benefits in relation to service with the employer may on leaving service decide, subject to scheme rules, to take an immediate early retirement benefit from one and defer the payment of other benefits. In these circumstances, if the maximum lump sum is not taken from the first scheme, the balance may be taken from the others when the benefits come into payment (see also paragraph 7.27).
Part 9. Increases of Pensions in Payment

General

9.1 A pension in course of payment may be increased up to the level of the maximum (residual) pension at retirement i.e. after reducing the maximum approvable pension by the annuity value of the pension foregone (if any) in exchange for a lump sum benefit or the provision of an allocated pension for a contingent beneficiary. It may also be further increased to take account of increases in the cost of living but should not exceed the maximum residual pension at retirement increased on a year-on-year basis by the greater of 3% or the increase in the Retail Prices Index in the year in question. Alternatively a pension below the maximum at retirement may be increased by a greater annual amount provided the increased pension remains within the limit in this paragraph.

9.2 Subject to paragraph 8.33 and the Notes to the definition of final remuneration (i.e. the final remuneration after the provisos), increases of benefit after retirement must be in the form of non-commutable pension. Schemes which provide increases of benefit in lump sum form will not be approved.

9.3 The same principles apply to pensions for widows, widowers, surviving civil partners and dependants.

Advance Provision for Increases

9.4 Scheme rules may provide in advance for increases in pensions to counteract the effects of inflation. This provision may take the form of a commitment to raise pensions in step with the maximum increase described in paragraph 9.1 above but if this is considered impracticable, other acceptable formulae include:

(a) fixed increases of not more than 3% per annum compound, whether or not the increase in the Retail Prices Index reaches that level, or

(b) provision for regular review of pensions in payment and for increases (not exceeding the rise in the Retail Prices Index since the pension came into payment or since the last increase) at the employer's or administrator's discretion, or

(c) Limited Price Indexation as required by sections 51/54 of the Pensions Act 1995, that is, increases reflecting the rise in the Retail Prices Index for the appropriate period subject to a maximum percentage of 5% per annum. (Although the Pensions Act provisions take effect from 6 April 1997, such increases need not be confined to pensions accrued after that date.)

Where there is scope, i.e. where the residual pension at retirement is below the Inland Revenue maximum, fixed percentage increases in excess of 3% per annum compound may be provided but must be capped by the limit in paragraph 9.1.

Increases on any of the above bases may be funded in advance to the extent that the liability can be actuarially justified. Assumptions of the rate of inflation must be reasonable in the light of long term trends in the cost of living.

Increases Without Prior Provision or Commitment

9.5 If there is no special provision in the rules, surpluses in the scheme or special contributions by the employer may be used to increase benefits within the limits set out in paragraph 9.1 subject to that action being lawful. It might be justified on the authority of an existing power of augmentation but failing that the rules could be suitably amended or the increases provided from a special supplementary arrangement or arrangements (e.g. "Hancock" annuities). As such increases do not arise from a commitment they cannot be funded in advance.
Employee's Option

9.6 An alternative method of protecting pensions from inflation is an option for employees to exchange pension without (or with a lesser degree of) indexation for a smaller initial pension with (a greater degree of) indexation which is of equal actuarial value.

Pensions Act 1995

9.7 The Pensions Act 1995 came into force on 6 April 1997. Sections 37, 76 and 77 introduce new rules and consolidate existing legislation where payments to employers from surplus or excess assets are to be made. The sections lay down the minimum level of indexation required to comply with the Act. In each section pensions for future pensionable service and past pensionable service must be increased in line with the statutory requirements for revaluation and indexation of pensions. Paragraphs 9.4 - 9.6 and paragraphs 13.18 - 13.42 should be read accordingly.

Continued Rights

9.8 Members with continued rights who have commuted part of their pension at a value which does not take into account any future increases (see paragraphs 7.57 - 7.59) may be provided with post retirement increases on the commuted pension as well as the pension in payment but not on pension surrendered to provide widow's, widower's, surviving civil partner's or dependant's pension. If the scheme has adopted the 12:1 basis mentioned in paragraph 7.2 (which is available for employees with continued rights on a concessionary basis) it must be regarded for this purpose as an enhanced commutation factor for all members of the scheme and, therefore, post-retirement increases may only be given on the pension in payment.
General

10.1 The term "leaving pensionable service" covers all circumstances of leaving pensionable service, not giving rise to the immediate payment of relevant benefits, whether or not the employee remains in the employer's service.

10.2 Benefits on leaving pensionable service may be provided in any of the following ways:

(a) by the provision of a deferred pension and/or deferred lump sum retirement benefit from the scheme itself,

(b) by the payment of a transfer value to either a scheme of a subsequent employer or a personal pension scheme,

(c) by the provision of a deferred annuity and/or deferred lump sum retirement benefit from a life office or friendly society.

In certain circumstances it is possible for an employee to receive a refund of his or her own contributions to the scheme (see paragraphs 10.52 - 10.54) instead of all or part of the above benefits. This is only possible in respect of benefits to which the preservation requirements of the relevant Department of Social Security (DSS) pensions legislation do not apply. A short summary of these requirements is set out in paragraphs 10.3 - 10.7 - it is not intended as a definitive statement of these requirements (for fuller details see Joint Office Memorandum No 78).

Preservation of Occupational Pension Rights

10.3 In general terms the preservation requirements apply to all benefits where the member has completed 2 years' qualifying service on termination of pensionable service.

10.4 The principal requirement of preservation is that a member must, on leaving pensionable service with 2 years' qualifying service, be entitled to short service benefit (SSB). This should normally be calculated on the same basis as the benefits to which the member would have become entitled had he or she remained in pensionable service until normal pension age (in most circumstances this term equates to normal retirement date). Where the calculation produces a short service benefit (before statutory revaluation if appropriate) greater than the maximum leaving service benefit that the Inland Revenue would normally allow, the SSB will take precedence (but see paragraph 10.13).

10.5 Schemes providing defined benefits (as opposed to money purchase benefits) are required to revalue the GMP by one of the permitted alternatives and that part of the SSB (in excess of the GMP) in accordance with the relevant DSS pensions legislation by 5 per cent per annum or, if less, the percentage increase in the Retail Prices Index in respect of the period from the date of leaving pensionable service to the normal pension age. Schemes which revalue deferred benefits fully in line with the Retail Prices Index are deemed to comply with this requirement.

10.6 Under DSS pensions legislation a member leaving pensionable service who is entitled to preserved benefits has a right, if the revaluation condition is satisfied, to require the cash equivalent of his or her revalued benefits to be applied as a transfer value to secure benefits under:

(a) an approved scheme of a subsequent employer, or

(b) an approved deferred annuity contract with a life office purchased in the member's name (buying-out), or
Where a member opts for a cash equivalent as an alternative to SSB, the cash equivalent should be calculated having regard to the relevant limitations set out in paragraphs 10.9 to 10.13 (see also paragraph 10.26).

10.7 Under the preservation legislation scheme rules may provide for other alternatives to SSB e.g. an amount smaller than, equal to or larger than that required to constitute SSB to come into payment either earlier or later than the normal pension age. Such benefits should generally be of at least equal actuarial value to the revalued SSB payable at normal pension age. These alternatives are subject to the requirements of Part 6.

Payment of Deferred Benefits

10.8 Benefits deferred within an approved scheme may come into payment at any time between the attainment of age 50 (or earlier on the grounds of incapacity) and the attainment of age 75, subject to:

(i) the member having left the employment to which the benefits relate, and

(ii) DSS requirements.

This age range is further restricted:

(a) for an employee with continued rights under the scheme, to preclude the deferment of benefits beyond the later of normal retirement date under the scheme in which the benefits are secured, the normal retirement date under the last employer's scheme and the cessation of all employment,

(b) for an employee subject to an unusually low normal retirement date, to meet any restrictions applied in accordance with paragraph 6.7,

(c) as necessary to meet contracting-out requirements.

If the date in (a) is later than the normal retirement date in the scheme providing the deferred benefit an actuarial increase may be given as explained in paragraphs 7.43 and 7.44.

Maximum Deferred Benefits

10.9 The maximum benefits an approved scheme may provide for a member who has left the employer's service is a deferred pension (including the pension equivalent of any deferred lump sum benefits) of the greater of 1/60th of final remuneration for each year of service (up to 40 years) and the lesser of:

(a) 1/30th of final remuneration for each year of service (up to 20 years) and

(b) 2/3rds of final remuneration less any retained benefits

(a) and (b) are subject to the qualifications in paragraphs 7.5 and 7.6 (see also paragraph 7.10 in relation to controlling directors).

Where the member has a pension debit in relation to the scheme and does not fall within the administrative easement described in paragraph 7.7, the maximum benefits calculated in accordance with the requirements of this paragraph must be reduced by the pension debit (see paragraph 16.56).

The limit in this paragraph applies also to a member without continued rights who leaves pensionable service on or after normal retirement date but remains in the employment (final
remuneration and service should be calculated only in respect of the period of pensionable service). In these circumstances any augmentation above this limit is subject to the requirement set out in paragraph 10.11.

10.10 The maximum benefits an approved scheme may provide for a member who has left pensionable service before normal retirement date but remains in the employment or who has continued rights is a deferred pension (including the pension equivalent of any deferred lump sum benefits) of the greater of 1/60th of final remuneration for each year of service (up to 40 years) or an amount calculated using the formula N/NS x P where:

N is the number of years of service up to the termination of pensionable service (up to 40 years).

NS is the number of years of potential service to normal retirement date (again up to 40 years).

P is the maximum pension approvable had the employee remained in service to normal retirement date (see paragraphs 7.2 - 7.10 and 7.40 - 7.42) by reference to final remuneration calculated at the date of termination of pensionable service.

NB Any restriction for:

- retained benefits (see Parts 7 and 16), and
- pension debits, where the member does not fall within the administrative easement described in paragraph 7.7 (see Part 7 and paragraph 16.56),

must be made in arriving at P before applying the fraction N/NS.

Scheme rules may restrict the application of this formula to members whose earnings while a member of the scheme have exceeded £10,000 and who, at the time of leaving pensionable service are 45 years of age or more. Where as a result of this restriction, this formula does not apply, the maximum total benefits will be as set out in paragraph 10.9 or, in the case of a member who has continued rights, paragraphs 7.40 and 7.41 by reference to years of service to the date of leaving service.

The limit in both this paragraph and paragraph 10.9 is subject to the qualification in the final sentence of paragraph 10.4.

10.11 Deferred benefits, which are restricted under paragraph 10.10 because the member, who is not entitled to continued rights, remains in service, may be augmented when the member subsequently retires or leaves service. The augmented benefits must not, when aggregated with benefits from approved personal pension schemes (other than minimum contributions only schemes) or retirement annuity contracts based on relevant earnings from the employer during the period of deferment, exceed the limit set out in paragraph 10.9 by reference to service and final remuneration at the date of retirement or leaving service as the case may be.

10.12 Benefits calculated as in paragraphs 10.9 or 10.10 may be increased during the period of deferment:

(a) at a fixed rate not exceeding 5% per annum compound, or

(b) by a greater percentage but restricted so as not to exceed the increase in the Retail Prices Index during the period of deferment.

Any GMP must be revalued in accordance with the Pension Schemes Act 1993.
10.13 The maximum benefits an approved money purchase scheme may provide at normal retirement date for a member (whether or not entitled to continued rights) who has left pensionable service prior to that date, is a deferred pension (including the pension equivalent of any deferred lump sum benefits) of the greater of:

(a) 1/60th of final remuneration for each year of service (up to 40 years) increased in accordance with paragraph 10.12, and

(b) the total benefit the member could have expected to receive at normal retirement date calculated on the same basis as applies for incapacity (see paragraph 6.2) together with any statutory revaluation increases required by the relevant DSS pensions legislation.

NB A power of augmentation cannot be used to increase a member's benefit up to this limit: an increase in benefit up to the limits set out in paragraphs 7.4 and 7.47 is, however, permissible.

Where the member has a pension debit in relation to the scheme and does not fall within the administrative easement described in paragraph 7.7, the maximum benefits calculated in accordance with the requirements of this paragraph must be reduced by the pension debit (see paragraph 16.56).

10.14 A member who has left pensionable service while remaining in the employer's service may be permitted to rejoin the scheme whether it is a defined benefit scheme or a money purchase scheme. If the member does so, service in the intervening period may be taken into account for the calculation of benefits. But any benefits (including, where the member does not fall within the administrative easement described in paragraph 7.7, any pension debits) from approved personal pension schemes (other than minimum contributions only schemes) and retirement annuity contracts based on relevant earnings from the employer during that period must be treated for limits purposes as though they were benefits provided by the employer. If service in the intervening period is not taken into account for the calculation of benefits, then any benefits (including, where the member does not fall within the administrative easement described in paragraph 7.7, any pension debits) from approved personal pension schemes (other than minimum contributions only schemes) and retirement annuity contracts based on relevant earnings from the employer during that period should, in the case of a non-controlled director, be treated in accordance with paragraphs 7.10 and 8.9 and in the case of any other member in accordance with the definition of retained benefits.

Deferred Lump Sum Benefits

10.15 The maximum lump sum benefit which may be paid out of deferred benefits without taking account of the level of the total benefits being provided for the member (but see paragraphs 8.6 and 8.8 in relation to members with a pension debit who do not fall within the administrative easement described in paragraph 7.7 and paragraph 8.9 in relation to controlling directors) is an amount equal to 3/80ths of final remuneration for each year of service (up to 40 years) to the date of termination of pensionable service. Where the lump sum is granted on this basis, the amount so determined may be enhanced to the same proportionate extent as the Retail Prices Index has increased during the period of deferment.

10.16 A greater lump sum may be provided by commutation of pension of an amount equal to 2.25 times the initial annual rate of pension to be paid, determined in the same manner as set out in paragraph 8.7 (but see paragraph 8.8 in respect of members with a pension debit who do not fall within the administrative easement described in paragraph 7.7 and paragraph 10.17 in respect of members with continued rights). Where scheme rules provide for a pension and a separate lump sum rather than a commutable pension, the maximum is an amount equal to 3 times the initial annual rate of the separate pension (but see paragraph 8.8 in respect of members with a pension debit who do not fall within the administrative easement described in paragraph 7.7).

10.17 For a member with pre 17 March 1987 continued rights a lump sum in excess of 3/80ths of
final remuneration for each year of service may be given calculated on the formula \( N \div NS \times LS \) where:

- \( N \) and \( NS \) are as described in paragraph 10.10.
- \( LS \) is determined in the same way as described in paragraph 8.37 substituting the date of termination of pensionable service for the date of retirement.
- Any restriction for retained benefits (see Parts 8 and 16) must be made in arriving at \( LS \) before applying the fraction \( N \div NS \).

For a member with **pre 1 June 1989 continued rights** a lump sum in excess of 3/80ths of final remuneration for each year of service may be given calculated in accordance with paragraph 8.28. Where total benefits are granted at a rate of 1/30th of final remuneration for each year of service (up to 20 years) or where \( [A-B] \div [C-B] \) in the formula in paragraph 8.28 is equal to or exceeds 1, the maximum approvable lump sum is calculated by reference to the table in paragraph 8.25 to determine \( LS \) and the fraction \( N \div NS \) (as above) is then applied to the result.

Where the benefit entitlement in respect of a **continued rights** member in a scheme is permanently reduced following a pension sharing order and the member does not fall within the administrative easement described in paragraph 7.7, the maximum approvable lump sum is calculated in accordance with paragraph 8.26 for a **pre 17 March 1987 continued rights** member and paragraph 8.8 for a **pre 1 June 1989 continued rights** member. In both cases, the date of termination of pensionable service is substituted for the date of retirement.

10.18 Lump sum benefits calculated under paragraph 10.17 may be increased:

1. in the period between the date of leaving pensionable service and normal retirement date in accordance with the rise in the Retail Prices Index, and
2. in the period between normal retirement date and the date the lump sum benefit is paid by the addition of interest as in paragraph 8.33.

**Death Before Payment of Deferred Benefits**

10.19 A withdrawing employee who retains an entitlement to deferred benefits from a scheme may also be given a right to benefits from the scheme if he or she dies before the deferred benefits become payable. The benefits payable in these circumstances should comply with the requirements of Part 11 for benefits payable on death in service. Lump sum benefits should be based on the employee's final remuneration at the date of withdrawal from the scheme, and widows', widowers', surviving civil partners' and dependants' pensions should be calculated on the basis described in paragraph 11.7.

10.20 The benefits payable under paragraph 10.19 may be provided from the scheme, from a bought-out annuity contract or from a transfer value. They cannot be provided from the scheme if the deferred benefits have been bought-out or transferred. Where deferred benefits have been transferred they will become subject to the rules appropriate to the vehicle into which they are received. Where the transfer is to another approved occupational scheme, or one seeking approval, the effect is to limit the total lump sum payable from the main scheme fund and transfer value combined to the maximum permitted by the rules of the receiving scheme, by reference to remuneration in the new employment. If for instance the rules of that scheme limit the lump sum death benefit to twice final remuneration, that is the maximum that may be paid from the whole of the fund including the transfer value.

Any money remaining in the transferred fund after payment of the lump sum may be used without limitation to provide pension for any eligible widow, widower, surviving civil partner and/or dependants. If no such beneficiaries exist, the remainder of the transfer value will be treated as surplus.
Transfer Payments

10.21 Both legislation and Inland Revenue discretionary practice permit transfers between approved and tax advantaged pension arrangements. It is the intention that, as far as possible, transfers should be able to take place with the minimum of restriction. The actual payment of the transfer between tax advantaged arrangements must generally be made between schemes directly and not through an independent broker unless an independent broker is acting as the appointed scheme administrator, e.g. within a self-invested personal pension scheme. But as an exception, if an independent broker is formally acting on behalf of the appointed scheme administrator, for example providing scheme services, including the operation of the scheme trustees’ bank account, then the payment may be made via them.

Normally a transfer payment should represent the whole of a member's benefits under the transferring scheme, but partial transfer payments coupled with retention in the transferring scheme of certain residual benefits are permissible where

- GMP and/or “Section 9(2B)” Rights or Protected Rights are retained in the transferring scheme and the balance of the member's benefits in excess of the contracted-out rights are transferred out. This would occur where PSA 1993 prevents the receiving scheme from accepting the contracted-out benefits rights GMP etc; or the receiving scheme is unwilling to accept such benefit rights because of consequential revaluation difficulties

- pension credit rights are transferred but not employee benefit rights (or vice versa) where the member has both pension credit and employee benefit rights in the same scheme – see paragraph 6A.28. Paragraphs 6A.21 to 6A.27 give more details about the transfer of pension credit rights generally.

- a two-stage transfer payment is made on winding up in the circumstances described in paragraph 10.41a. Or, in other circumstances as described in paragraph 10.41g.

10.22 Subject to the exceptions below, schemes and arrangements must not permit transfers to be made out of the scheme/arrangement in the following situations:

(a) once the normal retirement date has been reached except where the member left pensionable service

- prior to normal retirement date and has deferred the receipt of benefits from the scheme in accordance with paragraph 10.8, or

- on or after normal retirement date but continued in the service of the employer and the payment of all main scheme benefits are deferred (see paragraph 7.32 and, in respect of members with continued rights, paragraph 7.44) – all main scheme benefits in all schemes of the employer must be deferred otherwise the payment of any main scheme benefit in any scheme of the employer will preclude the transfer of benefits from any other scheme of the same employer where main scheme benefits are not in payment and arrangements for the transfer must be made before the member leaves the service of the employer

(b) after pension and/or lump sum benefits have come into payment in the scheme/arrangement from which the transfer is proposed except

- where additional voluntary contributions benefits are in payment prior to the commencement of main scheme benefits in accordance with the arrangements described in Part II of Appendix XII.

Transfers on or after an unusually low normal retirement date can take place only if the special
conditions attached to the agreement of that low normal retirement date (see paragraph 6.7) allow for the payment of benefits to be deferred beyond that date. For example, a transfer would not be possible if an agreed low normal retirement date is subject to benefits being paid at that date regardless of the circumstances of the employee whereas a transfer could take place if it is possible to defer payment where the employee continues in the service of the employer after the low normal retirement date. Where the normal retirement date is age 45 or less, a transfer is conditional on the receiving scheme paying benefits from the transfer payment no later than would have been the case under the transferring scheme (see paragraph 16.21).

Where a transfer can be made from a scheme/arrangement it can be paid into a scheme/arrangement in which the member has benefits in payment, provided the receiving scheme/arrangement is not a personal pension scheme. If the member has already taken a lump sum benefit in the receiving scheme/arrangement, no further lump sum benefits can be paid in respect of the transfer payment.

The prohibitions on transfers do not apply when an employer's pension arrangements are restructured. In these circumstances each transferred member's benefits under the successor scheme should be in the same form and of not lesser amount than was formerly payable under the transferring scheme and if the member has already taken a lump sum benefit in the transferring scheme/arrangement, no further lump sum benefits can be paid in respect of the transfer payment. Where normal retirement date has been reached in the transferring scheme it cannot be altered in the successor scheme. Even where arrangements are restructured, in the situations described at (a) and (b) it is not permissible to transfer into a personal pension scheme.

The prohibitions on transfers outlined above do not apply where the final part of a two-stage transfer payment is made upon winding-up (see paragraphs 10.42-10.48 for the terms and conditions of such payments).
10.23 Subject to the exceptions and conditions described in paragraphs 10.24 and 10.25 transfers may be made freely between all of the following tax advantaged arrangements:

(a) schemes approved under Chapter I Part XIV including *Free standing Additional Voluntary Contribution Schemes*,

(b) approved *personal pension schemes*

(c) *relevant statutory schemes*,

(d) annuity contracts to which section 431(B)(2)(d) or (e) applies,

(e) funds to which section 608 applies, and

(f) approved *retirement annuity contracts*.

10.24 The exceptions to freedom to transfer referred to in paragraph 10.23 are as follows:-

(a) Until 06/04/2003 the prior written consent of *IR SPSS* must be obtained before making any transfer payment which meets both the following conditions

- the transfer is to or from a small self-administered scheme (as defined in paragraph 20.1) from or to any of the tax advantaged arrangements referred to in paragraph 10.23, and
- the market value of the transfer either on its own, or when added together with the value of any transfer made to/ received by the same scheme for the same member within the previous 364 days equals or exceeds £250,000.

Form PS7050 should be used for this purpose (see Appendix II).

However, this requirement does not apply where the transfer consists only of the transfer/assignment of a death in service only term life insurance policy.

(b) Transfers are not permitted either way between *personal pension schemes* and schemes seeking approval under Chapter I Part XIV.

(c) A *personal pension scheme* may not make a transfer to an approved scheme or a *relevant statutory scheme* unless the individual is already accruing benefits under the receiving scheme as a result of service as an employee before the transfer payment is made on his or her behalf.

(d) A *free-standing additional voluntary contribution scheme* may only accept a transfer from another free-standing additional voluntary contribution scheme, an approved *personal pension scheme* or a separate additional voluntary contribution scheme of the employer (see part 14 of the separate FSAVCs Guidance Notes, IR12 Supplement).

(e) A buy-out contract to which section 431(B)(2)(d) or (e) applies may only accept a transfer in the form of a single premium from an approved scheme or a *relevant statutory scheme* at the time of inception. A transfer may be made from a buy-out contract to a new buy-out contract provided the conditions in paragraphs 6.12, 10.45 and 10.47(c) are complied with.

(f) A fund to which section 608 applies is a frozen scheme which is entitled to certain exemptions provided that it accepts no further contributions. It is not permitted to accept transfers.

(g) A *retirement annuity contract* is not permitted to accept transfers except from another retirement annuity contract. They may transfer to approved schemes, approved *personal*
pension schemes and relevant statutory schemes.

(h) A scheme seeking approval may never accept a transfer from a personal pension scheme and may not accept a transfer value from any other source unless, exceptionally, a genuine need to make such a transfer can be demonstrated to the satisfaction of, and agreed in writing by, IR SPSS. Subject to paragraph 10.25, a scheme seeking approval may make a transfer to an approved scheme, a relevant statutory scheme or a buy-out contract.

(i) A scheme that has received conditional approval as per paragraph 2.14 requires the prior written consent of IR SPSS to receive a transfer whilst the scheme has still not fulfilled its approval condition. Once a scheme has met its approval condition this transfer restriction will be lifted.

(j) None of the tax advantaged arrangements listed in paragraph 10.23 above can make transfers to, or accept transfers from a scheme in a category other than those listed (but see paragraphs 10.25 and 10.39 - 10.40).

See also paragraphs 16.17 and 16.18 in relation to transfers to personal pension schemes.

Transfers from schemes seeking approval

10.25 A scheme seeking approval may make a transfer to an approved scheme, a relevant statutory scheme or a buy-out contract. The first transfer from a scheme where an application for approval has been made but has not yet been granted must receive prior written authority from IR SPSS. Once such clearance has been given, it may be regarded as blanket approval for subsequent transfers from the scheme provided it is not a small self-administered scheme. No separate application for transfer clearance need be made where the documents of the receiving scheme expressly name the transferring scheme as one from which transfers may be accepted provided they do not involve small self-administered schemes. But the transfer may not go ahead until:

(i) expressly authorised in writing by IR SPSS, or

(ii) the recipient scheme has been formally approved.

All block transfers, however, must continue to be separately reported to IR SPSS in accordance with paragraph 10.36.

Amount of transfer value

10.26 Subject to the exceptions set out below, the value of any transfer must be limited to the amount which is sufficient to provide the maximum benefit on the basis that the member had left pensionable service at the date of taking the transfer (or, where the member had already left service prior to that date, the maximum at that date plus any appropriate increases in respect of the intervening period) (see also paragraph 10.6). If a pension debit exists against the benefits to be transferred and the member did not fall within the administrative easement described in paragraph 7.7, details of the amount of pension debit must, except where the receiving scheme is a simplified defined contribution scheme, also accompany the transfer payment to ensure that the necessary restrictions on the member’s benefits are maintained in the receiving scheme (see paragraph 16.56).

Subject to the above, transfer values paid in the following circumstances are unrestricted:

(i) from simplified defined contribution schemes;

(ii) from Free standing additional voluntary contribution schemes;

(iii) to a scheme of the same employer, other than a simplified defined contribution scheme; or

(iv) to a scheme of a different employer where continuous service has been granted.
10.27 Benefits from a transfer value received by an approved occupational pension scheme other than from a scheme of the same or an associated employer may be given in addition to any benefits in respect of service with the current employer i.e. the transfer benefits need not be subject to the scheme's limits rule. These benefits may be paid in lump sum form only to the extent described in paragraph 10.31 below. The transfer benefits, including where necessary, the value of any pension debit (see paragraph 10.26), will fall to be treated as retained benefits for the purpose of the scheme's limits rule except in the case of a lump sum death in service benefit derived from a transfer payment which is treated as an aggregable benefit for the purposes of the receiving scheme - see paragraph 10.20.

10.28 Alternatively transfer benefits may be calculated on the basis of added years. Under this system the transfer value is converted into a benefit expressed as the product of a number of years of notional service and the scheme benefit accrual rate (e.g. a pension of 1/50th of final remuneration for each added year of service) or the benefit can be expressed as a percentage of final remuneration. The total scheme benefit (including the transfer benefit and, where paragraph 10.26 applies, the amount of the pension debit) may exceed two thirds of final remuneration only if the accrual rate is 1/60th of final remuneration for each year of service or less or has been restricted to that level in respect of the years of service with the current employer. Lump sum benefits calculated on this basis must also be subject to the maximum described in paragraph 10.31 but no certificate from the transferring scheme is required (but see paragraph 10.35).

10.29 Where transfer payments are calculated on the basis of paragraph 10.28 and a transfer is made from a scheme where the member was not subject to the permitted maximum to a scheme where the member's benefits are to be calculated by reference to the permitted maximum, final remuneration for the purpose of calculating the appropriate number of added years to be given, should be estimated without regard to the permitted maximum.
Transfer benefit Example

10.29a An employee with 15 years prospective service to normal retirement date changes employment and a cash transfer value of £146,075 is paid to the new employer's scheme (which provides pension for future service at an accrual rate of 1/30th for each year of service). The employee has no other retained benefits.

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Transfer payment</td>
<td>£146,075</td>
</tr>
<tr>
<td>Plus interest for 15 years</td>
<td>£350,545</td>
</tr>
<tr>
<td>Total amount</td>
<td>£496,620</td>
</tr>
</tbody>
</table>

Total amount provides an annuity of £55,180 (converted at an annuity rate of 9:1).

Annual remuneration on entry to new employer's scheme = £100,000 (permitted maximum £82,200 at point of entry). Estimated final remuneration = £275,903 (viz. current remuneration is rolled up at 7% per annum compound in accordance with the principle set out in paragraph 13.9 without any regard to the permitted maximum).

Annuity of £55,180 is equivalent to 6/30ths of £275,903, therefore the scheme credits the member with 6 added years of service. It is recognised that this is not the only approach which may reasonably be adopted to quantify the additional benefits.

At the member's normal retirement date the permitted maximum has risen to £141,600 (final remuneration is taken as having risen to the original estimate of £275,903 in order to keep the example simple). Since the member has no other retained benefits the maximum approvable aggregate pension is calculated as the lesser of:

(a) $\frac{15}{30} \times £141,600 = £70,800$ and

(b) $\frac{2}{3} \times £141,600 - \frac{6}{30} \times £275,903 ( £55,180) = £39,220$,

plus, in either case, $\frac{6}{30} \times £275,903 = £55,180$. So in this particular example the maximum approvable aggregate pension is £94,400 (viz. £39,220 + £55,180).

If on the other hand, in the example above, the employee had retained benefits of say £15,000, the scheme benefit would be subject to a minimum of $\frac{15}{60} \times £141,600 = £35,400$ plus $\frac{6}{30} \times £275,903 ( £55,180)$ giving an aggregate minimum scheme benefit of £90,580.
More About Transfer Payments

10.30 Where a transfer payment is received from a scheme providing benefits in respect of an associated employment, or from any other scheme where IR SPSS would agree to continuous service (see paragraphs 7.15 - 7.19), or have specifically so agreed, service with the 2 employers may be aggregated provided that the transfer benefits are also aggregated with those from the current employment for the purposes of the scheme’s limits rule. If the scheme that receives the transfer is not a simplified defined contribution scheme and a pension debit accompanies the transfer payment (see paragraph 10.26), the value of that pension debit (see paragraph 16.56) must also be taken into account for the purpose of the scheme’s limits rules.

10.31 An approved scheme may pay transfer benefits (except those subject to a NIL certificate) in lump sum form but the maximum approvable lump sum benefit payable by the receiving scheme, from the transfer payment, must not exceed 2.25 or 3 times (as appropriate to the pattern of benefits) the initial annual rate of pension (determined in accordance with paragraph 8.7 or 8.8 as appropriate) payable from the transfer payment. This maximum is to apply to all lump sum transfer benefits where the employee in respect of whom the transfer is made is not entitled to continued rights in the receiving scheme (except those falling under paragraph 10.32(c) whose maximum will be subject to the amount stated on the lump sum certificate). In the case of the added years transfer example in paragraph 10.29, the members maximum approvable lump sum is calculated as 2.25 times the initial annual rate of pension (inclusive of that derived from the added years credit) i.e. 2.25 x £94,400 = £212,400. Where a transfer payment in respect of a continued rights member is applied in the receiving scheme in the form of added years, the lump sum from the transfer payment should be given on the basis of 3/80ths x final remuneration in the final remuneration in the receiving scheme for each added year given (subject to paragraph 10.35) or, if greater, the amount of the lump sum specified in a certificate, which may then be enhanced in proportion to the increase in the Retail Prices Index since the date of transfer.

10.32 The receiving scheme must obtain a lump sum certificate from the transferring scheme (unless the transferring scheme is a personal pension scheme) in respect of the member where

a) a transfer payment comes (whether directly or indirectly) from a source which does not permit a lump sum to be taken (see paragraph 10.35), or

b) the member in respect of whom the transfer is made has continued rights in the receiving scheme, or

c) a transfer payment is received from an approved scheme with a normal retirement date of age 45 or earlier where benefits are restricted in part to non-commutable pension because a maximum lump sum retirement benefit is provided from another source, for example as is the case for English league professional footballers.

The amount certified in respect of a continued rights member may be enhanced in proportion to the increase in the Retail Prices Index since the date of transfer. If a pension debit exists against the benefits to be transferred (see paragraph 10.26), the amount of the certified lump sum must be appropriately reduced to take account of the pension debit (see paragraph 10.34).

10.33 Where a transfer in respect of a member with continued rights in the receiving scheme comes from a personal pension scheme, the maximum lump sum retirement benefit payable out of the transfer benefits is 25% of the value of the accumulated transfer payment at the time of commutation excluding the value of any Protected Rights and any amounts subject to a NIL certificate. Where such a member is instead given added years in the receiving scheme, the lump sum from the transfer payment should be given on the basis of 3/80ths x final remuneration in the receiving scheme for each added year given (subject to paragraph 10.35). Where in respect of
such a member the transfer is from a retirement annuity contract the maximum is determined by a certificate to be provided by the transferring life office.

**NB** No transfer benefits are to be included in A of the formula set out in paragraph 8.28.

10.34 Where a lump sum certificate is required for a member

- not entitled to continued rights in the transferring scheme
- in respect of a transfer from
  - one scheme to another scheme, or
  - a scheme to a personal pension scheme

the lump sum should be calculated as follows:

The greater of:

(a) 3/80ths of final remuneration for each year of service (up to 40 years), and

(b) in a money purchase scheme, 2.25 times the amount of pension determined by:

   (i) establishing the member's actuarial interest in the scheme - this should exclude any amounts which have been allocated towards the provision of widows', widowers', surviving civil partners' or dependants' own right benefits,

   (ii) projecting this amount forward to the member's normal retirement date in the transferring scheme at a rate of 3% per annum compound, and finally

   (iii) calculating the amount of pension that the fund at (ii) will purchase using an annuity rate of £83.33 per £1,000, or

(c) in a defined benefit scheme, 2.25 times the member's accrued pension (by reference to final remuneration and service as at the date of leaving pensionable service)

Where a member's benefit entitlement in the transferring scheme is permanently reduced following a pension sharing order and the member does not fall within the administrative easement described in paragraph 7.7, the lump sum should be calculated as in (b) or (c) above. In each case the member's pension will have been determined after reduction to take into account the pension debit.

The amount so calculated may be increased by reference to the rise in the Retail Prices Index for the period between the cessation of pensionable service and the date of transfer.

Where a lump sum certificate is required for a member

- entitled to continued rights in the transferring scheme
- in respect of a transfer from
  - one scheme to another scheme, or
  - a scheme to a personal pension scheme

the lump sum should be calculated on the basis set out in paragraph 8.37 or 8.38 as appropriate.

Where a member's benefit entitlement in the transferring scheme is permanently reduced following a pension sharing order and the member does not fall within the administrative easement
described in paragraph 7.7, the lump sum is calculated in accordance with paragraphs 8.7, 8.24 or 8.28 as appropriate but substituting the date of termination of pensionable service for the date of retirement.

Where a lump sum certificate is required in respect of a member

- who is transferring to another scheme or personal pension scheme
- at or after normal retirement date

the certified figure should correspond with the maximum approvable lump sum benefit that could have been paid to the member at the date of the transfer had the member been paid benefits from the scheme instead of making the transfer (see paragraphs 8.5, 8.7 – 8.9, 8.24 – 8.32 and 8.34 – 8.39 as appropriate). In the case of a member without continued rights whose lump sum from a money purchase scheme would have been 2.25 times the initial pension payable, the initial pension is determined by

(i) establishing the member's actuarial interest in the scheme - this should exclude any amounts which have been allocated towards the provision of widows', widowers', surviving civil partners' or dependants' own right benefits, and

(ii) calculating the amount of pension that the fund at (i) will purchase using an annuity rate of £83.33 per £1,000.

The annuity figure established at (ii) immediately above is multiplied by 2.25. The resulting figure is the amount that is certified for the purpose of the lump sum certificate.

Where a lump certificate is required for an individual

- whose deferred benefits are held in a buy-out contract
- in respect of a transfer from the buy-out contract or assigned policy to another scheme or personal pension scheme

the lump sum should be calculated as follows.

1. Where the buy-out contract expresses the maximum lump sum that could have been paid from the buy-out contract in monetary terms – that monetary amount (the monetary amount may be increased in accordance with the rise in the Retail Prices Index for the period between the purchase of the buy-out contract and the date of the transfer). See paragraph 10.45(c) for more details about lump sums having a monetary limit and the effects that a pension sharing order might have that limit.

2. Where the lump sum payable from the buy-out contract is expressed

- as the result of 2.25 times the initial amount of the contract holder's annuity, and
- the buy-out contract has details of what was the policy holder's normal retirement date in the scheme that purchased the buy-out contract (or, in the case of a transfer from a contract that is a replacement for an earlier contract or contracts, the scheme that purchased the original buy-out contract), and
- the contract holder has not reached the normal retirement date of the scheme that purchased the original contract

the lump sum should be calculated as 2.25 times the amount of annuity determined by:

(i) establishing the value of the buy-out contract at the time of the transfer - this should exclude any amounts which have been allocated towards the provision of
widows', widowers’, surviving civil partners, or dependants’ own right benefits and any surplus funds after testing for Inland Revenue limits,

(ii) projecting this amount forward to what was the contract holder’s normal retirement date in the scheme that purchased the buy-out contract (or, in the case of a transfer from a contract that is a replacement for an earlier contract or contracts, the scheme that purchased the original buy-out contract) at a rate of 3% per annum compound, and finally

(iii) calculating the amount of pension that the fund at (ii) will purchase using an annuity rate of £83.33 per £1,000.

The annuity figure established at (iii) immediately above is multiplied by 2.25. The resulting figure is the amount that is certified for the purpose of the lump sum certificate.

3. Where the lump sum payable from the buy-out contract is expressed

- as the result of 2.25 times the initial amount of the contract holder’s annuity, and

- the buy-out contract has no details of what was the policy holder’s normal retirement date in the scheme that purchased the buy-out contract (or, in the case of a transfer from a contract that is a replacement for an earlier contract or contracts, the scheme that purchased the original buy-out contract), or

- the contract holder is at or has past the normal retirement date of the scheme that purchased the original contract

the lump sum should be calculated as 2.25 times the amount of annuity determined by:

(i) establishing the value of the buy-out contract at the time of the transfer - this should exclude any amounts which have been allocated towards the provision of widows’, widowers’, surviving civil partners, or dependants’ own right benefits and any surplus funds after testing for Inland Revenue limits, and

(ii) calculating the amount of pension that the fund at (i) will purchase using an annuity rate of £83.33 per £1,000.

The annuity figure established at (ii) immediately above is multiplied by 2.25. The resulting figure is the amount that is certified for the purpose of the lump sum certificate.

See paragraph 10.45(c) for more details about lump sums expressed as 2.25 times the amount of the contract holder’s annuity and the effects that a pension sharing order might have that limit.

Where a lump certificate is required for an individual

- whose deferred benefits are held in an assigned policy

- in respect of a transfer from the buy-out contract or assigned policy to another scheme or personal pension scheme

The lump sum should be calculated on the same basis that applies for buy-out contracts described above.

10.35 Where a transfer is received, which consists in whole or in part of a payment from one or more of the following:

(i) an approved scheme (including a Free standing Additional Voluntary Contribution Scheme) the benefits of which are funded solely by employee’s voluntary contributions, where that contract commenced after 7 April 1987, or
(ii) a fund to which section 608 applies, or

(iii) an approved scheme with a normal retirement date of age 45 or earlier where benefits are wholly in non-commutable pension form because a lump sum retirement benefit is provided from another source, for example, as is the case for individual English league football club schemes for professional footballers

(iv) an approved scheme, the benefits being pension credit rights deriving from a member’s benefit rights from which a tax-free lump sum retirement benefit was taken before the pension sharing order – see paragraphs 6A.5 and 6A.26

then a NIL certificate will be received in respect of the non-commutable source.

The impact of the NIL certificate will be as follows:

(i) Where the payment is used to secure added years credit then no part of the added years credit in respect of the NIL certificated amount may be used to form part of the basis for granting lump sum benefit in the receiving scheme.

(ii) Where the payment is used to secure benefits on a money purchase basis then no part of the NIL certificated amount plus the investment growth thereon can be used to form part of the basis for granting lump sum benefit in the receiving scheme.

Block transfers

10.36 When groups of employees enter a new scheme of the employer on the re-organisation of that employer’s pension arrangements or following mergers, re-organisation or take-over of companies or change of ownership of businesses, IR SPSS should be consulted in advance about the treatment of any transfers of assets or payments from one scheme to another. Also see paragraph 10.41a about two-stage transfers.

Particulars should be provided on a form PS 295 (see Appendix II).

Assignment of individual arrangement to a new employer

10.37 It may be possible for an individual arrangement for an employee to be assigned to a new employer prepared to assume the former employer’s responsibilities. Such an arrangement constitutes a new retirement benefits scheme which must be referred to IR SPSS for approval.

Public Sector Transfer Club

10.38 Most schemes in the public sector participate in a transfer system which facilitates transfers between participating schemes and specifies the basis of such transfers. Exempt approved schemes outside the public sector may participate in the system in certain circumstances. This is not a matter for the Inland Revenue and any enquiries should be addressed to the Cabinet Office, Civil Service Pensions, 8th floor, Grosvenor House, Basing View, Basingstoke, Hants. RG21 4HG.

Overseas schemes

10.39 Generally, transfers to overseas schemes from approved schemes and from buy-out policies are permitted only where a number of requirements are met. Appendix VI sets out those requirements and outlines the procedures for making such transfers. The administrator/trustees of the transferring scheme, or the insurance company if the transfer is from a buy-out policy, must ensure that the relevant conditions in Appendix VI have been satisfied before making a transfer.

10.40 Transfers may not be accepted from overseas schemes or schemes to which section 615 applies except with the specific authority of IR SPSS. Before authorising such a transfer from an overseas scheme, IR SPSS will need to be satisfied that the transferring member had been employed for a significant period (normally not less than 2 years) in the overseas employment to which the transfer benefits relate. The transfer should be unconditional and made direct between the schemes. The overseas scheme may be an employer’s scheme or of the personal pension scheme type.

10.41 A transfer payment to an approved scheme must produce benefits in accordance with the
rules of that scheme. The amount paid to the member in the form of a lump sum retirement benefit must not exceed as a multiple 2.25 times or 3 times (as appropriate to the pattern of benefits) the initial amount of the pension produced from the transfer payment (i.e. as in paragraph 10.31 above). The payment of lump sums to any greater extent as certified by the transferring scheme is not approvable.

**Two-stage transfer payments**

10.41a A transfer payment should normally represent the whole of a member's benefits under the transferring scheme - see paragraph 10.21. However, in certain circumstances, where the transferring scheme is in the process of winding-up it is possible for a transfer payment to be made in two stages. Those circumstances are where

- a) it is not possible at the time of the transfer payment to provide the whole of the member's entitlement due to uncertainties about the values of the assets and liabilities of the scheme, and
- b) it is essential that a transfer payment is made before the winding-up process is completed, and
- c) there is a suitable enabling provision in the scheme rules.

Two-stage transfer payments should not be regarded as an optional alternative to a single payment where such a payment can be made. There are provisions in the Pension Schemes Act 1993 and the Pensions Act 1995 for scheme trustees to apply to the Occupational Pensions Regulatory Authority (Opra) for authority to defer payment of a transfer value until such time as they have sufficient information to enable them to calculate a full, correct payment, and then make one payment. Two-stage transfer payments should not be made as a matter of course but should be made only in exceptional circumstances.

Where a two-stage transfer payment is appropriate the transferring scheme must tell the trustees/providers of the receiving pension arrangement(s) that it is not possible to make a single payment. It will be for the receiving trustees/providers to decide whether or not to accept the two-stage transfer payment.

Paragraphs 10.41a - 10.41d apply equally to block transfers, provided the provisions in paragraph 10.36 are adhered to.

10.41b The two-stage transfer payment should comprise:

(i) an initial transfer payment which should, where appropriate, include all of a member's contracted-out benefits and be of an amount advised by the actuary that:-

(A) can be paid without fear of overpayment having regard to the priority accorded to the various classes of beneficiaries under the scheme's winding-up rule, and

(b) subject to the need to avoid trivial residues (see paragraph 10.44) is as close as possible to the best estimate of the likely final aggregate value of the two payments, and

(ii) a final transfer payment when the assets and liabilities of the scheme have been determined and the winding-up process is being completed.

If, exceptionally, an initial transfer payment is found to be in excess of the limits on benefits, the transferring scheme should provide **IR SPSS** with full details.

10.41c The transferring scheme should ensure that:-

- the individual and the trustees/providers of the receiving pension arrangement(s) are told that the initial transfer payment does not represent the whole of the individual's
rights under the transferring scheme,

- so as to avoid small amounts being stranded, the receiving pension arrangement(s) will not object to accepting a small final transfer payment. (Paragraph 14.8 will not apply to any trivial residue remaining after an initial transfer payment has been made).

- taking account of both payments, the benefit limits applicable at the time the individual left pensionable service are not exceeded and

- it holds a statement from the individual to the effect that he/she will notify the transferring scheme if any part of the benefits represented by the initial transfer payment commence to be paid to him/her (see paragraph 10.41e).

### Destination of final transfer payment

10.41d An initial transfer payment and final transfer payment should normally be made to the same destination or, if the initial transfer payment were fragmented, to the same destinations and in the same proportions as the initial transfer payment. However, subject to the exceptions in paragraphs 10.41e and 10.41f, the final transfer payment need not be transferred to the same pension arrangement(s) as received the initial transfer payment if that would lead to practical difficulties. For example, if

- at the time the final transfer payment is made the individual is no longer a member of the scheme which accepted the initial transfer payment but is a member of a subsequent scheme, there will be no objection to the first accepting scheme being bypassed and the final transfer payment being made directly to that subsequent scheme, or

- the initial transfer payment was fragmented on a proportionate basis and the final transfer payment is less than £10,000, the final transfer payment need not be transferred on the same proportional basis - instead it can be transferred to one of the pension arrangements which accepted part of the initial transfer payment.

### Retirement before final transfer payment is made

10.41e Where, before the final transfer payment is made, the individual draws any benefits from that part of the initial transfer payment derived from employer contributions and/or basic or contractual contributions, the transferring scheme must arrange for the final transfer payment to be made as soon as possible to the pension arrangement(s) from which the benefits are being paid. Where the initial transfer payment was to a personal pension scheme, the final part of the transfer payment may go ahead even though benefits are already in payment from the personal pension scheme; the prohibition on transfers to personal pension schemes once benefits are in payment (see paragraph 10.22) does not apply in these circumstances.

In all instances, any further pension and any further lump sum emerging from the final transfer payment must be paid as soon as possible. In the case of an individual who does not have continued rights and whose lump sum retirement benefit from the initial transfer payment is calculated on the basis set out in paragraph 8.7, no further lump sum payment will be possible where the final payment is made after the end of the first year in which the pension from the initial transfer payment has been in payment.

The timing of the final transfer payment can take its intended course if the only benefits paid from the initial transfer payment derive from additional voluntary contributions as part of an income drawdown arrangement (see Part II of Appendix XII) under the receiving scheme.

Where any part of the initial transfer payment subsequently becomes subject to an annuity purchase deferral or income drawdown arrangement (see Appendix XII) in the receiving pension arrangement, there is no objection to the appropriate part of the final transfer payment being transferred into that pension arrangement.

### Death before final transfer payment is made

10.41f In the event of an individual's death before the final transfer payment is made, the final
transfer payment(s) should be made as soon as possible to the pension arrangement(s) which hold(s) the initial transfer payment at that time so that the death benefits emerging from the final transfer payment can be dealt with in accordance with the conditions/rules of that/those arrangement(s) and paid as soon as possible. Where the initial transfer payment was split on a proportionate basis, the final transfer payment should be dealt with in accordance with paragraph 10.41d.

**Supplementary transfer payments**

10.41g There may be circumstances when, a two-stage transfer payment not having been contemplated, after a member's rights have been transferred or bought-out, it is considered that a supplementary transfer payment could be made. There will be no objection to such payments where:

- a scheme receives a further payment from the Occupational Pensions Regulatory Authority (Opra) or the Department for Work and Pensions (formerly Department of Social Security), or
- a scheme receives a payment made by a decision of a court, tribunal, commissioner, an arbitrator or (in Scotland) arbiter, or
- an error is discovered in the calculation of the original transfer payment, or
- a scheme improves deferred benefits retrospectively.

The provisions in paragraph 10.41d should be followed as regards the destination of a supplementary transfer payment.

If an individual retires/dies before a supplementary transfer payment is made, the provisions in paragraphs 10.41e-10.41f should be applied as appropriate.

**Buy Out Policies**

10.42 Under Department for Work and Pensions pensions legislation members who are entitled to preserved benefits and whose pensionable service ends on or after 1 January 1986, have a right to the cash equivalent of their scheme benefits and the option for that cash equivalent to be used to purchase deferred annuities. The deferred annuity contracts must satisfy Inland Revenue requirements as set out at sections 591(2)(g) and 431B(2)(d) and (e) and described in paragraphs 10.44-46. It is not necessary to seek prior approval from the IR SPSS (see paragraph 10.51). This option is subject to the requirement that the annuity contracts satisfy Inland Revenue requirements. Prior to 1 July 1994, this normally meant that the contracts had to be in a form approved for the purposes of sections 431(4)(d) and 591(2)(g). Approval under the latter section enabled the contracts to be used for this purpose while the former section provided for pension business treatment of the investments underlying the contracts. With effect from 1 July 1994 both the aforementioned sections were amended by sections 107 and 143 of the Finance Act 1994 so that such contracts no longer require approval. The cash equivalent of pension credit rights that have yet to come into payment may also be used to purchase a deferred annuity (see paragraph 10.51).

10.43 As an alternative to the purchase of buy-out policies, any individual policy or policies held for the provision of an employee's benefits under the scheme can be assigned to the employee. On assignment the policies must be endorsed so that they comply with the requirements of paragraphs 10.45 and 10.46 below. These endorsements will not affect the status of the policies as corresponding for the purposes of section 431(4)(b).

10.44 With effect from 1 July 1994, the primary requirement of an acceptable buy-out contract is that it must provide only those relevant benefits which could be provided directly by a hypothetical approved scheme i.e. the benefits must be approvable in form and amount. To be approvable in form, the benefits must fall within the Inland Revenue's published criteria for approval of a scheme.
To be approvable in amount, the benefits must be within the limits permissible under the particular regime appropriate to the member concerned, i.e. whether the member has pre 17 March 1987 continued rights, pre 1 June 1989 continued rights, or is subject to the Finance Act 1989 requirements. In addition the contract should be made with the administrator of an approved scheme or a scheme being considered for approval or a relevant statutory scheme either alone or together with the individual to whom the benefits relate. It should be a single premium contract with no provision for the payment of further premiums. However, where a two-stage transfer is taking place (see paragraphs 10.41a - 10.41f) and the contract is set up to receive any part of the initial transfer payment, the contract provisions may, if it was considered necessary, be amended to take account of the receipt of any part of the final transfer payment.

10.45 The contract should contain provisions which:

(a) Require that the benefits cannot be assigned, except to meet a pension sharing order.

(b) Require that the contract cannot be assigned or surrendered except for the purpose of transferring the value (see paragraph 10.21 et seq.), to allow the exercise of an open market option (see paragraph 6.12) or to meet a pension sharing order.

(c) Show the maximum extent to which benefits may be taken in lump sum form either by way of commutation or on death. The maximum lump sum by commutation must be expressed in monetary terms where the member is entitled to continued rights in the scheme purchasing the buy-out policy. But where the member is not entitled to continued rights in the purchasing scheme, the maximum may be expressed as the greater of 3/80ths of final remuneration for each year of service (up to 40 years), the result to be expressed in monetary terms, and 2.25 times the initial annual amount of the contract holder's annuity (determined in accordance with paragraph 8.7). Where the member's benefits in the purchasing scheme are subject to a pension sharing order and the member does not fall within the administrative easement described in paragraph 7.7, any monetary amount in the case of a pre 17 March 1987 continued rights member, should be reduced to take account of the pension debit (see paragraph 10.17). For members with pre 1 June 1989 continued rights and members without continued rights, the maximum lump sum is an amount equal to 2.25 times the initial annual amount of the contract holder's annuity (determined in accordance with paragraph 8.7). If the purchased buy-out policy itself is subsequently subject to a pension sharing order, any monetary amount of lump sum to be paid must be reduced by an amount of 2.25 x the pension debit (see paragraph 16.54). Where the maximum lump sum is expressed in monetary terms the contract may provide for the increase of that amount in accordance with paragraph 10.18. Such an increase is not permissible in relation to the maximum lump sum expressed as a multiple of the pension payable.

(d) Show the latest date on which the member's benefits may commence where the contract is made with the administrator of a scheme with a normal retirement date of age 45 or less.

10.46 The contract should also contain a monetary limit (expressed in terms of pension) on the individual's retirement benefits if:

(a) it contains a general provision allowing a choice of any form of Relevant Benefit to be provided within the relevant maximum approvable for or in respect of the individual, or

(b) the contract proceeds consist of a single lump sum to secure both the individual's benefits and reversionary pension(s) for the individual's widow, widower, surviving civil partner or dependant's, or

(c) the contract secures from the outset a separate reversionary widow's, widower's, surviving civil partner's or dependant's pension the value of which, on the death of the beneficiary before the individual's pension commences, will be applied to secure additional benefits for the individual.
10.47 The contract may provide for:

(a) Benefits to come into payment at any time between the attainment of age 50 (or earlier on grounds of *incapacity*) and the attainment of age 75. Where, however, a member’s rights under the scheme are represented by two or more buy-out policies, those policies must require that like benefits under all such policies are to come into payment simultaneously. When the insurer issues a buy-out policy it should ascertain whether that policy represents the entirety of the member’s benefits from the scheme concerned, or whether other buy-out policies have been purchased (and if so from which insurers). When the member claims his or her retirement benefits, the insurer should check with the others that they too are bringing the like benefits into payment.

(b) Full commutation on grounds of triviality or exceptional circumstances of serious ill-health provided that the contract also requires the insurer to account to the Inland Revenue for any tax liability arising thereon.

(c) The contract to be assigned or surrendered to comply with a *pension sharing order* or provide a transfer value to a new buy-out contract, or a *personal pension scheme*, (together, where appropriate, with a certificate under regulation 6(3) of the Personal Pension Schemes (Transfer Payments) Regulations 1988 (SI 1988 No 1014) or the Personal Pension Schemes (Transfer Payments) Regulations 2001 (SI 2001 No 119) and any lump sum certificate for the purpose of the same Regulations – the amount certified in the lump sum certificate must take account of the effects of the *pension debit* where applicable (see paragraph 10.45(c)) or an approved scheme, or subject to paragraph 10.24(h), a scheme being considered for approval, or a *relevant statutory scheme* of which the individual has become a member. The amount of the transfer payment must conform with the requirements in paragraph 10.26 (including, where appropriate, the passing on to the receiving scheme details of any *pension debit*) and the contract must specify that the payment is to be made direct to the scheme, or, in the case of a new buy-out contract, the provider concerned (see also paragraph 10.24(c)). If the benefits include a GMP which the receiving scheme is unable or unwilling to accept, the excess of total proceeds over those necessary to secure the GMP may be transferred.

(d) An open market option provided that the transfer must be made direct to the other insurer and that the new contract includes the same restrictions on commutation and further assignment as the old one. The new policy should also meet the requirements necessary for discharge of the scheme trustee’s liability (see Joint Office Memorandum No 77 paragraph 84).

(e) Lump sum death benefits payable under the contract to be subject to discretionary trusts. Such trusts may be effective from the outset of the contract or may be introduced at a date later than that on which the contract was taken out.

(f) A facility to defer the purchase of an annuity and in the meantime pay pensions by income drawdown (see Appendix XII).

(g) A second lump sum may be paid in the circumstances set out in paragraph 8.2 and where there has been a personal pensions misselling within the former Securities & Investment Board review and benefits are already in payment.

(h) A lump sum may be recalculated and a further payment made (where appropriate) in the circumstances set out in paragraph 8.2A.

10.48 Paragraphs 10.45 and 10.46 explain what limitations on benefits are to be included in a buy-out contract. Where limits are required on the amount rather than the form of benefits it is possible for surpluses to arise. Should a surplus arise after providing the individual’s maximum benefits it
may be used to provide or augment other approvable benefits within Inland Revenue maxima. Ideally the contract should reduce the possibility of a surplus by indicating how any monies not needed for the main benefits should be dealt with. In the absence of such a provision, however, excess monies may be used to provide post retirement increases on the pensions payable. Any remaining surplus after all possible augmentation should be returned to the employer (NOT to the scheme trustees) or be retained by the insurer as a windfall profit. Contracts should provide for the insurer to deduct and account to the Inland Revenue for any tax liability under section 601.

10.49 The following pointers may be helpful when drafting buy-out contracts:

(a) The main object of the contract should be the provision of an annuity for, or in respect of, the individual.

(b) The contract should be self-contained. All provisions should be complete without reference to the scheme rules. (Contract providers may wish to incorporate within the terms of the contract a particular vesting date that coincides with the contract holder’s normal retirement date in the purchasing scheme for the purpose of any subsequent transfer – see paragraph 10.34.)

(c) Pension scheme rules must contain limits which apply to the aggregate of an individual's benefits from all schemes relating to service with the employer. The contract should similarly apply the required limits (see paragraphs 10.45 and 10.46) to aggregate benefits but, alternatively the monetary expression of such limits may be an amount which represents the balance of the overall limit after taking account of benefits from other relevant sources.

(d) Retirement benefits provided under the policy may come into payment at any time between the attainment by the individual of age 50 (or earlier on grounds of incapacity) and the attainment of age 75. Where a member's rights under the scheme are represented by two or more buy-out policies, those policies must require that like benefits under all such policies are to come into payment simultaneously.

10.50 Where the buy-out contract provides for transfers to subsequent schemes (whether an employer's scheme or of the personal pension scheme type), the insurance company will be required to give a general undertaking to the Inland Revenue in the following terms:

(a) that it will ascertain from the trustees or administrator of the receiving scheme, or in the case of a personal pension scheme the provider, the section of the Taxes act under which it is approved or being considered for approval and will pay transfer values only to a scheme approved, or being considered for approval, under the Taxes act;

(b) that it will, in the case of a continued rights member, or where part or all of the transfer value is not available in lump sum form (see paragraph 10.35), or in the case of a transfer to a simplified defined contribution scheme (see paragraphs 16.20 and 22.21), or in the case of a transfer to a personal pension scheme in the circumstances described in paragraph 16.17, give the trustees or administrator of the receiving scheme, or in the case of a personal pension scheme the provider, a certificate stating the maximum amount which can be taken in lump sum form (also see paragraph 10.47(c) where the member’s benefits are subject to a pension debit); and

(c) that it will provide details of the amount represented by the individual's own contributions, and of any restrictions on the return of such contributions to that individual.

Alternatively, this obligation may be accepted by the insurance company by including suitable conditions in all its buy-out contracts.

10.51 Whilst it will be a condition of scheme approval or continued approval that the trustees satisfy themselves before purchase that a particular buy-out contract provides only suitable benefits, it will be sufficient to obtain from the insurance company a warranty that the benefits
satisfy the statutory requirements. Insurance companies who wish to know beforehand that their policies will satisfy the Inland Revenue's requirements, may submit them to IR SPSS's Standard Documents Section for examination.

**Refunds of Contributions**

10.52 Since the full implementation from 6 April 1980 of the preservation requirements of the relevant DSS pensions legislation, the Inland Revenue place no separate restrictions on refunds of contributions. But a refund disqualifies the member from taking any other benefit from the scheme in respect of the period for which the refunded contributions were paid apart from a GMP or benefits from Protected Rights as required by the contracting-out legislation (see however paragraphs 7.23 and 17.26).

10.53 Refunds of contributions are only possible where the member has completed less than 2 years' qualifying service. However, the effect of DSS pensions legislation is such that, where a scheme has accepted a transfer value from a personal pension scheme or a retirement annuity contract and the benefits have arisen from employed rather than self-employed earnings, the member has a preserved benefit in the scheme even though he/she may not complete the 2 years' qualifying service. In these circumstances, the contributions to the personal pension scheme, the retirement annuity contract and the scheme may not be refunded to the member. Interest at a reasonable rate may be added to a refund of contributions. In this respect the rate of return achieved on the scheme assets or the bonuses paid on the initial sum assured will normally be regarded as acceptable. Such interest will be regarded as an element in the calculation of the refund and not as true interest for tax purposes.

10.54 Subject to the preservation and, where appropriate, the contracting-out requirements, rules may permit an employee who has elected for, or is otherwise entitled to deferred benefits, to change his or her mind later and exercise an option for a refund of contributions (subject to paragraph 10.52) provided that he or she does so before receiving any benefit under any scheme relating to the same employer.

**Mis Selling of Personal Pensions**

10.55 The Securities and Investments Board (SIB), now within the Financial Services Authority, announced on 25 October 1994 details of redress for people suffering material loss as a result of bad investment advice which led them to forego retirement benefits scheme membership, in favour of retirement annuity contracts, personal pension schemes or buy-out policies. The relevant transactions are those based on advice given between 29 April 1988 (the date on which the main provisions of the Financial Services Act 1986 came into force) and 30 June 1994 inclusive. (New regulatory safeguards took effect on 1 July 1994). The SIB review also required that redress for mis-selling be provided in “execution-only” cases. This would arise where the investor requested a transaction and no advice or judgement on the part of the firm selling the pensions vehicle was expected or given. The investor may however have been prompted to request the transaction after reading misleading advertising or sales literature which could be regarded as bad investment advice.

The aim of the accepted remedies in the SIB review guidelines was to put people in a financial position equivalent to, or as close as possible to, that in which they would have been had the bad investment advice not been given.

10.56 Redress should in the majority of cases take the form of the reinstatement of individuals in their original retirement benefits schemes. It has also been agreed that compensation in the form of a cash lump sum paid to the individual would in general be inappropriate because it is normally not possible to convert pension rights into a cash lump sum before retirement. The general recommendation is therefore that compensation should be paid to the pension vehicle securing the individual's, or, where appropriate a widow's, widower's, surviving civil partner's or dependant's, benefits, for example, an retirement benefits scheme or personal pension scheme. The personal pension scheme does not have to be the original personal pension scheme that was mis-sold or, in
the case of someone who has retired, the vehicle under which the annuity/pension is being paid. Redress in the form of cash in hand, should be paid only where the individual has already retired (or died) and catching-up payments are needed to match what he or she would already have received from the retirement benefits scheme, or, exceptionally, where it is impractical for redress to be achieved by the provision of retirement benefits.

10.57 Section 148 Finance Act 1996 exempts from income tax and capital gains tax compensation paid to individuals or to pension vehicles as a consequence of a review carried out under the SIB review process. The exemption will also apply to lump sums received in cash by individuals as a result of, for example, Court awards, and to interest forming part of a compensation payment for the period up to the earliest date on which the amount of compensation is determined whether by agreement or by a decision of a Court. The Inland Revenue will not therefore seek to divide a payment into capital and interest: the entire sum will be exempt from tax. But interest which accrues after the date of determination (for example, because the compensator delays making the capital sum payment) will be clearly identifiable and will be fully taxable under the normal rules applicable to the payment of interest. The exemption under section 148 would also arise where redress is provided in "execution-only" cases (see paragraph 10.55).

10.58 Where an individual was persuaded by bad investment advice to join a personal pension scheme rather than join his/her employer's retirement benefits scheme, the desired remedy is that firstly, if possible, the individual should be allowed to join, i.e., be instated in the retirement benefits scheme for future service with the employer. Secondly, the parties concerned should try to restore the retirement benefits scheme rights that the individual would have had for past service.

The preferred form of redress for loss of past service rights is normally reinstatement in the retirement benefits scheme. In this situation, the appropriate level of personal pension funds would be returned to the retirement benefits scheme as described in paragraph 10.61 below and the payment would be made to the retirement benefits scheme of any compensation amount required. The return of the funds to the retirement benefits scheme is not treated as a transfer payment.

10.59 Where the individual was already a member of the employer's retirement benefits scheme but was persuaded to "opt-out" and join a personal pension scheme, the objective is the same. Where the original rights in the retirement benefits scheme were transferred to the personal pension scheme, the return of funds from the personal pension scheme to the retirement benefits scheme will automatically include that original transfer (plus income from investments and deposits). In cases where the original rights in the retirement benefits scheme remained with that scheme as a deferred benefit, the return of funds from the personal pension scheme will be added to the deferred benefit.

10.60 There will be individuals who were (or would have been) required to contribute to their retirement benefits schemes at a rate of say, 5% or salary but who, when they became members of personal pension schemes, were able to pay contributions at the rate of, for example, 20%. In the event of reinstatement or instatement, sums representing any such "excess" contributions should to the maximum extent possible (see paragraph 10.61 below) be placed in the receiving retirement benefits scheme's additional voluntary contributions facility or a Free standing Additional Voluntary Contribution Scheme.

10.61 Where the individual is to be reinstated/instated in the retirement benefits scheme and a personal pension scheme fund is to be returned to the retirement benefits scheme, the return payment should, wherever possible, be made before any compensation payment is paid to the retirement benefits scheme. If, as a consequence of this process, the payment of the whole of the compensation to the retirement benefits scheme would result in the overfunding of the individual's benefits, the "excess" compensation may be paid to the individual as indicated in paragraph 10.56. The examples that follow illustrate how a payment from a PPS should be dealt with. (In all cases it is assumed that compensation to make up for "lost" employer contributions will be subsumed in the main fund of the retirement benefits scheme).

- Reinstatement/instatement in a contributory retirement benefits scheme
Sufficient monies to restore the compulsory employee contributions that would have been made during the reinstated period of membership (plus income "build-up") should be subsumed into the retirement benefits scheme main fund.

Any balance, to the extent that total employee contributions do not exceed the aggregate of 15% of the relevant earnings for each tax year separately (or part year) of reinstated membership of the retirement benefits scheme (plus income from investments and deposits), should be placed in the additional voluntary contributions facility.

Any amount remaining should be placed with the main fund of the retirement benefits scheme and the benefits emerging from that amount treated for the purposes of maximum Inland Revenue limits as though they were benefits provided by the employer.

**- Reinstatement/instatement in a non-contributory retirement benefits scheme**

Firstly, payment as at the second bullet point above should be placed in the additional voluntary contributions facility.

Any amount remaining should be dealt with as at the third bullet point above,

10.62 If, as a condition of reinstatement, the retirement benefits scheme will not accept any part of the "excess" contributions, and though in principle an individual should have retirement benefits scheme benefits only or personal pension scheme benefits only in respect of the same period of service, the "excess" should be retained in the individual's personal pension scheme in paid-up form. The benefits emerging from the personal pension scheme should be treated as retained benefits for the purposes of maximum Inland Revenue limits on the retirement benefits scheme benefits.

10.63 In the examples given above, income from investments and deposits should be calculated by having regard to the actual returns achieved by the scheme's main fund or additional voluntary contributions facility or other suitable indicators, for example, bank base rates.

10.64 If the personal pension scheme funds transferred into the retirement benefits scheme are insufficient to make up for the compulsory employee contributions (plus income from investments and deposits) that would have been made (see paragraph 10.61, third bullet point above), the individual may be required or permitted by the employer to make further contributions for past years. In such a case, the normal rules for tax relief on employee contributions to an retirement benefits scheme apply (see paragraphs 4.2 – 4.3). There is no objection to the payment of back contributions by instalments over future years' service in order to keep the amount paid in any one year of assessment within the 15% tax relief limit.

10.65 If an individual's contributions in any one year of assessment would nevertheless exceed 15% of remuneration, the Board of Inland Revenue will, under their discretionary powers in the case of schemes approved on or after 27 July 1989, not object to the payment of an excess. In the case of schemes approved before 27 July 1989 the Retirement benefits schemes (Continuation of Rights of Members of Approved Schemes) (Amendment) Regulations will disapply the override which currently limits contributions to 15%. In neither case will tax relief be allowable on contributions in excess of 15%.

10.66 In the case of an individual who retired before any redress could be paid and who is retrospectively reinstated in the retirement benefits scheme concerned, there will be no objection to the compensation payment being paid to that retirement benefits scheme and used to provide further benefits (both pension and lump sum) within Inland Revenue limits. Nor will there be any objection to the individual being allowed to make up a shortfall by payment of the appropriate amount (without tax relief on that amount) to that scheme. If the individual retired in the same tax year as that in which the contribution shortfall is paid, tax relief on payments up to 15% of remuneration for the part tax year will be available.
10.67 While an individual remains in the *personal pension scheme* pending reinstatement in the *retirement benefits scheme*, there is no objection to contributions continuing to be made to the *personal pension scheme* under normal rules.
Interpretation

11.1 For the purposes of this Part provisos (i), (ii), (iii) and (vi) of the definition of final remuneration do not apply. However, the term may be defined, subject to the permitted maximum, in the following additional ways:

(a) where there are no fluctuating emoluments, as the annual rate of basic salary or wages being received immediately before death;

(b) as basic salary or wages as in (a) above plus the average of fluctuating emoluments during the 3 years (or the whole period of the employment if less) up to the date of death;

(c) as the total earnings (fixed plus fluctuating) paid during any selected period of 12 months ending not earlier than 36 months before the date of death.

Earnings or emoluments included in (b) and (c) for any year other than the 12 months prior to death may be increased in proportion to the increase in the Retail Prices Index from the last day of that year up to the date of death.

Lump Sum Benefits

11.2 On death in service before any retirement benefits have been paid, a lump sum benefit from all sources set out in paragraph 7.25 may be provided not exceeding:

(a) £5,000, or, if greater,

(b) four times the deceased employee’s final remuneration less any retained benefits.

For members whose earnings for the first year's employment following entry to the scheme do not exceed 1/4 of the permitted maximum and who are not, and have not been controlling directors, (see paragraph 7.5) retained benefits may be ignored.

11.3 Alternatively if the current employer provides a lump sum which cannot exceed twice final remuneration (this limit relates to the aggregate lump sum under all schemes of the employer including any additional voluntary contribution scheme(s), retained benefits need not be taken into account except in the case of a lump sum benefit derived from a transfer payment which is treated as an aggregable benefit for the purpose of the receiving scheme (see paragraph 10.20). It is not permissible to apply this alternative in respect of individual members of a scheme which otherwise provides lump sum death benefits on the paragraph 11.2 basis.

NB In relation to paragraphs 11.2 and 11.3 where scheme rules give an entitlement to death benefits calculated using a multiple of annual remuneration, in the case of an employee without continued rights, that annual remuneration must be restricted in the rules of the permitted maximum. Before the date benefits crystallise, i.e. the date of death, they may be augmented, if the scheme rules already allow, and provided they do not exceed the limits on benefits set out in paragraph 11.2 and 11.3 as appropriate. However, it is not permissible to establish a scheme to provide lump sum death in service benefits for a controlling director (or a director who is a member of a family which owns more than 50% of the company's shares), nor to pay contributions to provide any such benefits through an existing approved scheme, on or after his or her death.

The limits in paragraphs 11.2 and 11.3 are unaffected by a pension sharing order and so no account need be taken of any lump sum death benefit payable on the death of a pension credit member before pension credit rights come into payment.

11.4 A refund of the employee’s own contributions (other than those made specifically for the provision of death in service benefits) with or without interest, may be paid in addition to the lump
sum payable under paragraphs 11.2 and 11.3 above. Where interest is added it must be reasonable and in this respect the principle set out in paragraph 10.53 applies. Such interest is regarded as an element in the calculation of the refund and is not true interest for tax purposes.

11.5 The lump sum may be paid to the employee's legal personal representatives or a nominated beneficiary, or distributed at the discretion of the trustees/administrator: it is not necessary to limit nomination or distribution to dependants. The money may continue to be held under the rules of the pension scheme for a period not exceeding 2 years if this is necessary for the trustees/administrator to determine who is to benefit, and interest may be credited provided the lump sum thus payable (excluding refunded contributions and interest thereon) does not exceed the limit in whichever is appropriate of paragraphs 11.2 and 11.3. The money should be paid over promptly to the beneficiaries (or to a trust for their benefit) once they have been selected, or transferred to an account outside the scheme if they have not been selected after 2 years. The principles explained in this paragraph apply also to lump sum death benefits payable on the death of a pension credit member in accordance with paragraph 6A.9.

11.6 If approval is sought for a scheme providing a lump sum death benefit for a director who holds a life appointment (and for whom the provision of retirement benefits is therefore not appropriate), discretionary distribution will be permissible if death occurs before the director's 75th birthday. The scheme rules must however preclude discretionary distribution if death occurs on or after that date, with the beneficiaries being restricted to the legal personal representatives or the surviving spouse or civil partner as in paragraph 11.12.

Widows', Widowers', Surviving Civil Partners' And Dependents' Pensions

11.7 An approved scheme may also provide a pension for a widow, widower, surviving civil partner or dependant, of an amount not exceeding two thirds of the maximum pension (calculated by reference to final remuneration as extended by paragraph 11.1) that could have been approved for the employee if the employee had had no retained benefits and had retired on incapacity grounds (see paragraph 6.2) on the date of his or her death. Maximum pension in this context includes the pension equivalent of any separate lump sum retirement benefit which would have been payable. Where the administrative easement described in paragraph 7.7 does not apply, a pension sharing order in relation to the deceased member's benefit will have the effect of reducing the maximum pension payable to the widow, widower, surviving civil partner or dependants of the deceased member. This is because the deceased member's maximum approvable pension is reduced by the amount of the pension debit (see paragraph 16.54).

11.8 Where the category of widow, widower, surviving civil partner and dependants includes more than one person, separate pensions may be provided for each. No individual pension may be greater than the limit specified in the preceding paragraph. Where more than one is to be paid the total must not exceed the full amount of the incapacity pension that could have been provided for the employee on the basis described in that paragraph. Subject to these limits, the benefits may be shared in any proportions desired.

11.9 Widows', widowers', surviving civil partners' and dependants' pensions should normally come into payment immediately on the death of the employee or on the death of the pension credit member as the case may be (see paragraph 6A.10 and 6A.11). A widow's or widower's or surviving civil partner's pension, however, may be deferred at the widow's or widower's or surviving civil partner's request until she or he reaches retirement age and if so it may be increased actuarially in respect of the period of deferment. A pension for a child must cease when the child ceases to be a dependant. A pension payable to other dependants or to a widow or widower or surviving civil partner may continue for life irrespective of any later change in the beneficiary's circumstances. If desired, however, a widow's or widower's or surviving civil partner's pension may cease on remarriage or forming a civil partnership or cohabitation.

Death in Service After Normal Retirement Date

11.10 A member who remains in service after normal retirement date may, on death while in such
service, have benefits provided on the basis of death in service generally (paragraphs 11.2 - 11.5 and 11.7 - 11.9). Where, however, such service continues beyond attainment of age 75, then on the member's death in service subsequent to attainment of that age, benefits may only be paid in accordance with Part 12. (But see paragraph 11.11 in relation to members with continued rights).

Continued Rights

11.11 A member with continued rights may, on death in service after normal retirement date, be given benefits on either the basis appropriate to death in service generally or on the basis which would have applied had he or she retired on the day before his or her death. Where a scheme provides for a lump sum death in service benefit to be given to a member who dies in service having taken his or her pension and/or lump sum at or after normal retirement date (see paragraphs 7.44 and 8.33), this continued life cover becomes a retirement benefit. In this situation, however, there is no objection to life cover up to the time of actual retirement being provided through term life policies held by the scheme administrator but the benefit from such cover must be distributed in accordance with paragraph 11.12. For the purposes of any restriction of the lump sum retirement benefit taken at or after normal retirement date the life cover should be valued using the same basis and assumption as set out in paragraph 7.54. Even where the life cover is treated as a retirement benefit in accordance with this paragraph, any pension or lump sum under a guarantee (see paragraphs 12.9 - 12.11) may be paid in addition.

Controlling Directors

11.12 Where a controlling director with continued rights remains in service until or beyond his or her 75th birthday, discretionary distribution of any lump sum death in service benefit payable if death occurs on or after that date will not be approvable. This restriction does not apply to any lump sum payment in respect of a guarantee of a pension already in payment (see paragraph 12.10). The acceptable alternatives to discretionary distribution where that is precluded are:

(a) payment automatically to the legal personal representatives, or

(b) payment to the surviving spouse or civil partner, or, in the absence of any surviving spouse or civil partner, to the legal personal representatives.

For the purpose of this paragraph the term controlling director is to be interpreted as though the attainment of age 75 is the date of retirement.
Part 12. Benefits on Death After Retirement

Lump Sum Benefits

12.1 No lump sum benefits may be paid if death occurs after retirement except:

(a) any payments due under a guarantee attaching to the pension (see paragraph 12.9 and Appendix XII), and/or

(b) any sum payable under permitted continued life cover (see paragraphs 7.37 and 7.54 - 7.56).

Where a member of a contracted-out money purchase scheme dies after retirement but before state pension age and there is no qualifying widow, widower or surviving civil partner, there is no objection to the payment of the Protected Rights benefits where appropriate as a lump sum to a nominated beneficiary or to the member's estate. Such a payment is not treated as a lump sum retirement benefit.

Widows', Widowers', Surviving Civil Partners' And Dependents' Own Right Pensions

12.2 An approved scheme may provide a pension for a widow, widower, surviving civil partner or dependant of an amount not exceeding 2/3rds of the maximum pension that could have been approved for the employee on his or her retirement if he or she had had no retained benefits, increased in proportion to the subsequent rise in the retail price index. Maximum pension in this context is the maximum total benefit in accordance with Part 7 (which amount will remain the same whether lump sum benefits are provided separately or by commutation). So where the administrative easement described in paragraph 7.7 does not apply, a pension sharing order in relation to the deceased member's benefit will have the effect of reducing the maximum pension payable to the widow, widower, surviving civil partner or dependants of the deceased member. This is because the deceased member's maximum total benefit is reduced by the amount of the pension debit (see paragraph 16.54).

12.3 Where the category of widow, widower, surviving civil partner and dependants includes more than one person, separate pensions may be provided for each. No individual pension may be greater than the limit specified in the preceding paragraph. Where more than one is to be paid the total must not exceed the full amount of the maximum employee's pension on the basis described in that paragraph. Subject to these limits, the benefits may be shared in any proportions desired.

12.4 Widows', widowers', surviving civil partners' and dependants' pensions may commence on the employee's death or on the pension credit member's death as the case may be (see paragraphs 6A.15 and 6A.16) (but see paragraph 12.9 where the employee's or pension credit member's pension is guaranteed for over 5 years) and may continue for life irrespective of any later change in the beneficiary's circumstances. If desired, however, a widow's or widower's or surviving civil partner's pension may cease on re-marriage or forming a civil partnership or cohabitation. A pension for a child must cease when the child ceases to be a dependant. A widow's, widower's, surviving civil partner's or dependant's pension must not be guaranteed for a minimum number of years except to the extent that the contracting-out legislation permits such a pension bought with the member's Protected Rights Fund to be guaranteed for up to 5 years.

Allocated Widows', Widowers', Surviving Civil Partners' And Dependents' Pensions

12.5 Subject to any contracting-out requirements, an employee or pension credit member may, at the point of drawing benefits, surrender (or allocate) part of his or her own pension to provide a pension for his or her widow, widower, surviving civil partner or a dependant to commence on the death of the employee or pension credit member. The amount of the pension may not exceed the reduced pension that the employee or pension credit member retains. An allocated pension may be arranged in this way even though a separate own right widow's, widower's, surviving civil partner's or dependant's pension is provided and without being taken into account the purposes of
the limits set out in paragraphs 12.2 and 12.3. For the purpose of calculation, the reduced pension retained by the employee or pension credit member can include the pension equivalent of any lump sum retirement benefit whether provided separately or by commutation.

12.6 An employee or pension credit member may similarly provide allocated pensions for more than one individual in this class provided that the total of these pensions does not exceed the pension the employee or pension credit member retains.

12.7 Where the allocated pension is provided by surrender of a pension which is guaranteed for no more than 5 years the allocated pension may also be guaranteed for the same period after the commencement of the member's or pension credit member's own pension and paragraph 12.10 may apply.

12.8 If required, an approved scheme may provide for the allocation to be made by the employee (or pension credit member) after the payment of pension (or pension credit benefits) has commenced e.g. because of subsequent marriage or forming a civil partnership.

Guarantees

12.9 An approved scheme may provide for the pension payable to a retired employee or to a pension credit member to continue for a period up to 10 years despite the pensioner's death within that period. If the guarantee exceeds 5 years, however, own right pensions for the widow, widower or surviving civil partner or dependants may not begin until the end of the guarantee period. For this reason it may not be possible to provide a guarantee in excess of 5 years from a scheme contracted-out under the relevant Department of Social Security pensions legislation unless that part of the guaranteed pension equal to the widow's or widower's or surviving civil partner's pension is paid to her/him as of right, with a corresponding reduction in the amount of the guaranteed pension available for distribution in accordance with paragraph 12.11.

12.10 If the guarantee period does not exceed 5 years, instead of the pension continuing after the pensioner's death, an immediate lump sum may be paid. The lump sum must not exceed the total of the instalments falling due after the pensioner's death. For this purpose the value of those instalments may include any cost of living increases which are quantified by the rules: any restriction of those increases by reference to the Retail Prices Index may be ignored.

12.11 Lump sums payable under paragraph 12.10, or pensions continuing after the member's or pension credit member's death, may be paid at the discretion of the trustees/administrator in the same way as lump sums on death in service except that a pension which is not taken in lump sum form in accordance with paragraph 12.10 must retain its nature as a pension i.e. it may be split into a number of pensions each payable to an individual. These pensions must not be paid to such bodies as charities, societies or clubs.

12.12 The requirement (in paragraph 11.5) that the money representing lump sums should be transferred to a separate account outside the scheme if 2 years have passed and the beneficiaries have still not been selected will not apply in the case of members who retired early or left service with a deferred pension.
General

13.1 The tax advantages of exempt approved schemes are controlled only indirectly by the imposition of limits on benefits. It is equally important that the amount of money held in exempt funds is reasonable in relation to the benefits to be provided. The basic requirements of funding are that money should not be held except to provide benefits which the scheme has a commitment to pay and that the amount of money held should not be more than sufficient to pay those benefits when they would normally become payable i.e. in relation to retirement benefits, at the normal retirement date. It is not, therefore, permissible for an employer to fund in advance for the extra actuarial costs of a benefit which comes into payment before the normal retirement date. Any enhancement of early retirement benefits must be provided by way of augmentation at the time of such retirement (but see paragraph 13.2). This paragraph does not prevent an employer funding in advance for early retirements on the grounds of incapacity on the basis of scheme experience of the numbers and ages of members retiring in these circumstances.

13.2 The restriction on early retirement funding by the employer in paragraph 13.1 does not preclude an employee who intends to retire early from paying Additional Voluntary Contributions (subject to the normal restrictions - see paragraph 4.4) to fund the extra costs of early retirement. This applies to all members of all schemes.

13.3 The Taxes Act, Regulations and Inland Revenue discretionary practice include provisions to prevent overfunding and, when surpluses occur, for the elimination of those surpluses. The guidance in this Part is intended to be read in conjunction with sections 601 and 602, Schedule 22 and Regulations made thereunder. There are three statutory instruments which are relevant viz. the Pension Scheme Surpluses (Valuation) Regulations 1987 (SI 1987 No 412) referred to in this Part as the "Valuation Regulations", the Pension Scheme Surpluses (Valuation)(Amendment) Regulations 1989 (SI 1989 No 2290) and the Pension Scheme Surpluses (Administration) Regulations 1987 (SI 1987 No 352) the latter being referred to in this Part as the "Administration Regulations".

13.4 Whether a scheme falls within the scope of the Valuation Regulations or the discretionary practice depends upon the nature of the scheme. Regulation 3 of the Valuation Regulations as amended specifies that they apply to:

(a) self-administered schemes having not less than 12 members, and

(b) insured schemes, the policies in respect of which do not provide that levels of contributions require to take account of surpluses except those which provide only for lump sum benefits for members on death before normal retirement date.

They do not apply to simplified defined contribution schemes (see Part 22) which are wholly outside the scope of both the Regulations and this Part.

13.5 The requirements of the three statutory instruments outlined in paragraph 13.3 should be regarded as applying to all schemes. This means that where a scheme is not subject to the requirements set out in these "Regulations" then our discretionary practice will apply unless otherwise indicated. For convenience paragraphs 13.6 - 13.12 have been divided to show the position under the headings of Defined Benefits Schemes and Money Purchase Schemes.

Defined Benefits Schemes

13.6 The legislation has the effect of placing a ceiling on funding - calculated using prescribed methods and assumptions - by requiring valuations on that basis to be prepared at intervals not exceeding 3 years 6 months (or 5 years in the case of certain public service schemes - see regulation 9 of the Valuation Regulations). Alternatively, the administrator may produce to the
Inland Revenue a certificate on form PS162 (a specimen is included in Appendix II) in relation to the scheme's funding determined on the prescribed basis. The Valuation Regulations also provide for the elimination of surpluses.

13.7 The exclusion from the scope of the Valuation Regulations of schemes insured with policies which regulate contributions to take account of surpluses follows the long standing practice for setting aside the normal requirement that defined benefits schemes should provide 5 yearly actuarial valuations to the Inland Revenue. This exception from that practice remains in force for such schemes to which the Valuation Regulations do not apply. In these circumstances the policy should provide for the policy benefits (or assets) and the scheme liabilities to be reviewed at intervals not exceeding 5 years using methods and assumptions not materially different from those prescribed in the Valuation Regulations. Any surplus so disclosed should be eliminated by the adjustment of premiums.

**Money Purchase Schemes**

13.8 A scheme providing money purchase benefits may be self-administered or insured through group or individual earmarked policies. In a scheme using earmarked policies, each sum or annuity assured is earmarked to provide benefits for or in respect of the individual member. The policy proceeds may be more than sufficient to provide the benefits due and the excess may be dealt with in any of the ways described in paragraph 13.20. In other schemes, the members' benefits are calculated by reference to the performance of assets notionally attributed to them in a common pool. The assets must be held in a common trust fund from which the members' entitlement to benefits will be provided at the appropriate times and they must not be earmarked for individuals to the extent that a member could identify an entitlement to any specific assets. Any surplus arising in respect of an individual member must be retained within the scheme as part of the common fund. The Valuation Regulations do not distinguish between schemes which provide defined benefits or those funded on a money purchase basis. Therefore money purchase schemes may be subject to the Valuation Regulations if they fall within the definitions in paragraph 13.4. However, schemes providing benefits under earmarked policies are deemed to fall outside category (b) on the basis that the "corresponding" policy and the scheme rules are interdependent. Otherwise, whatever the method of funding, the principles set out in the following paragraphs are relevant.

13.9 The funding of fully insured money purchase schemes or arrangements must comply with the ABI Funding Guidelines (ABI 1996 Method as amended 31 March 1998 and 21 December 2001) following agreement between the Inland Revenue and the Association of British Insurers. A copy of the 1994 Guidelines is reproduced in Appendix VIII. The funding of small self-administered schemes must comply with the Maximum Permissible Funding Rates For Small Self-Administered Schemes (SSAS 1996 Method) following agreement between the Inland Revenue and the Association of Pensioner Trustees. A copy of the SSAS 1996 Guidance Notes is reproduced in Appendix IX. Under these bases contributions must be calculated as an annual percentage of salary rather than on a level annual basis. Until the three-year period immediately prior to normal retirement date calculations may be based on either current remuneration or final remuneration provided that whatever choice is made for a particular member is retained for that individual. Level annual contributions remain acceptable provided they do not produce funding levels above those acceptable under the new bases. Special contributions to insured money purchase schemes/arrangements and small self-administered schemes should not be made to fund benefits in advance of the maximum justifiable by reference to service to date.

13.10 The principal assumptions to be used for calculating contributions to the type of schemes or arrangements described in paragraph 13.9 are broadly based on those set out in the Valuation Regulations (see paragraph 13.3). They are:

(a) a rate of investment return of 8.5% per annum;

(b) a rate of general earnings increases of 6.9% per annum;

(c) a maximum rate of increases to pensions in payment of 5.3% per annum (unless
index linking is guaranteed in which case the principle in regulation 5(2)(C)(iv) of the Valuation Regulations applies); and

(d) post-retirement mortality based on the PA (90) ultimate table, rated down two years.

In addition for these schemes/arrangements:

(e) the permitted maximum (see paragraph 13.18), should be assumed to increase at the rate of 5.3% per annum.

13.11 For schemes and arrangements other than those described in paragraph 13.9, it is permissible to fund on the basis of an assumed salary progression which allows for career advancement as well as cost of living pay increases but does not exceed 8.5% per annum compound (but see also paragraph 13.18). Contributions to secure benefits calculated by reference to such an assumption may be calculated on a level annual contribution basis or as a percentage of salary. Other assumptions used for calculating contributions should conform with the following:

(i) The pre-retirement return on invested funds should be assumed to be at least 1% over the rate of salary escalation.

(ii) Post-retirement net yield should not be less than 3% per annum where cost of living increases in excess of 5% per annum are provided. Otherwise a gross yield of at least 8% per annum should be assumed.

(iii) Mortality assumptions should be in line with the PA 90 tables rated down by no more than one year, or the a (90) tables unadjusted.

(iv) The Valuation Regulations (see paragraph 13.3) do not prescribe an actuarial assumption to be used in respect of limited price indexation (LPI). Nonetheless, in the light of advice from the Government Actuary's Department, the IR SPSS will regard as acceptable a net investment yield of 4% per annum.

13.12 Schemes providing benefits on a money purchase basis should normally fund by reference to either:

(a) specifically targeted benefits that it is intended to provide for or in respect of the member - such targets, usually expressed in terms of a fraction of final remuneration, serve a dual purpose by both facilitating control of the scheme's funding while providing for the member a meaningful (although not guaranteed) estimate of his or her expectations of benefit from the scheme (section 590(2)(b)) or, alternatively,

(b) where the only constant is the rate of contributions, an amount of benefit (within Inland Revenue limits) that those contributions, if continued to normal retirement date, are likely to secure. In these circumstances it is necessary for both funding and information purposes to calculate the amount that is likely to be available at normal retirement date to provide benefits together with an illustration of the benefits that might be provided from such amount. For members' information, this should again be expressed in a meaningful form.

Review of Funding

13.13 The rules of a self-administered scheme both providing money purchase benefits and outside the scope of the Valuation Regulations should require the funding position to be reviewed and, if necessary, adjusted at intervals of no longer than 5 years. For fully insured money purchase schemes/arrangements, contribution re-assessment should take place at 3 yearly intervals in accordance with the Guidance Notes referred to in paragraph 13.9.

13.14 Unless a scheme uses tailored insurance policies or is of sufficient size to bear its own actuarial risks, funding for death benefits may be difficult to reconcile with that for retirement
benefits. Term life insurance is therefore often used in relation to the excess of death benefit liability over the current funding level for retirement benefits. In these circumstances, where contributions are calculated separately for each member (viz. individual arrangements, earmarked schemes and small self-administered schemes), the insurance should be calculated annually so as to produce as nearly as possible the balance of benefits payable under the rules in the event of the employee's death in the coming year. For this purpose it may normally be assumed that in the case of a male employee he is married to a wife 3 years younger than himself, and in the case of a female employee, that she is married to a husband 3 years older than herself. Subject to this paragraph, in the case of a scheme or arrangement as described in paragraph 13.9, contributions up to the levels set out in (a) and (b) below may be paid for death in service benefits without regard to the contributions being paid for post-retirement benefits:

(a) a contribution of up to 5% of the maximum future contribution rate to secure death in service lump sum benefits up to the maximum permitted (see paragraphs 11.2 and 11.3) taking into account the value of the retirement benefits fund; and

(b) a further contribution of up to 5% of the maximum future contribution rate to secure a spouse's pension, or a dependant's pension for a named dependant(s) of an unmarried member, on death in service up to the maximum permitted (see paragraph 11.7).

Contributions in excess of the amounts in (a) and (b) may be paid (provided the benefit is within the maximum permitted) but the excess must be offset against the maximum contribution for retirement benefits.

13.15 Conversely certain traditional forms of insurance, if used to fund all of a scheme's liabilities on retirement, death etc, may provide excessive funds on the early death of the employee. Thus, in general, insurance policies used for this purpose should be specially tailored to the scheme's needs and to meet the correspondence requirement of section 431(B)(2) if premiums are to be referred to the insurer's pension business.

Multiples of salary

13.16 Some life offices market schemes where the term life sum assured necessary to secure death in service benefits consisting of both a lump sum and a widow's/widower's pension is calculated as a multiple of the employee's salary varying according to the current age of the spouse. This is acceptable if the multiples are calculated assuming a positive net yield of at least 3% in respect of the period of payment of the widow's/widower's pension. Other assumptions should be within the guidelines set out in paragraph 13.10.

13.17 In schemes where contributions are calculated separately (i.e. as in paragraph 13.14 above) or where the membership is insufficient for reasonably accurate funding on the basis of group experience, funding for a reversionary pension for a widow, widower, surviving civil partner or dependant is permissible only in respect of an employee who currently has a spouse, civil partner or dependant prospectively entitled to benefit.

Actuarial Assumptions

LPI and the Permitted Maximum

13.18 To a large extent the Valuation Regulations prescribe the actuarial assumptions to be used in funding computations. They are, however, silent concerning limited price indexation (LPI) and they do not comment on the effect of the permitted maximum on future salary progression. In relation to LPI a net investment yield of 4% per annum will be regarded as acceptable and the permitted maximum should be assumed, subject to a ceiling of 3% lower than the assumed investment return, to increase in line with the Retail Prices Index.

Surpluses

Statutory basis

13.19 When a surplus under the statutory valuation basis of more than 5% of the scheme's liabilities is identified, administrators of schemes to which the Valuation Regulations apply are
required to make proposals to the Inland Revenue for the elimination of at least the excess of that surplus over 5%. Such proposals should be made on a form PS 290 - a specimen is included in Appendix II. These proposals are required to be made within 6 months of the date that the valuation report or certificate was signed. Failure to take satisfactory action to eliminate a surplus may, in a self-administered scheme, result in the scheme suffering a restriction in the tax reliefs it enjoys as a result of being granted exempt approval (see paragraph 17.10).

13.20 A surplus may be eliminated by any one or more of the following methods:

(a) by providing new benefits or improving existing benefits under the scheme;

(b) by suspension or reduction of contributions by either or both the employer and the members. The suspension or reduction should not be for a period in excess of 5 years unless a longer period is appropriate under the special provisions of regulation 11 of the Valuation Regulations; and

(c) by making payments to the employer (but see paragraph 9.7 about the impact of the Pensions Act 1995 on a scheme’s ability to do this).

**NB: No payment should be made to an employer without the prior written agreement of IR SPSS.**

13.21 Proposals to bring a surplus within the 5% margin should be effective within:

(a) 6 months where the method is either of those described in paragraph 13.20 (a) and (c);

(b) the period of up to 5 years over which contributions are suspended or reduced where the method is that described in paragraph 13.20(b);

(c) such other period as is specified in regulation 11 of the Valuation Regulations in the case of a scheme falling within that regulation.

13.22 The periods referred to in paragraph 13.21 above begin 30 days after the date on which the Board gives the scheme’s administrator their written agreement. If a payment is to be made to the employer, the effect of this, when combined with any other methods to be adopted, should be to reduce the actuarial value of the fund when calculated on the prescribed basis, to 105% of the liabilities exactly. Where a surplus is used to improve benefits, the 5% additional margin should be calculated by reference to the value of the liabilities as increased by the cost of the benefit improvements.

13.23 Where a contribution holiday or reduction over, say, 2 years is adopted in conjunction with other methods to reduce a surplus, the position at the end of the 2 years has to be estimated, taking into account new entrants and the cost of benefit improvements up to the end of that period, including additional service accrued in respect of existing staff and new entrants. If all three methods of reducing a surplus are adopted, it will be necessary for the actuary to take into account:

(i) the cost of benefit improvements relating to past service and service up to the end of the 2 years in respect of existing staff and new entrants plus the additional 5% margin, and

(ii) the value of the contribution holiday or reduction in contributions over that period in respect of the total expected payroll.

The maximum permitted payment to an employer would be the present value of an amount sufficient to reduce the actuarial value of the assets required to be held at the end of the 2 year period to cover 105% of the expected liabilities on that date, taking into account (i) and (ii) above.

13.24 Regulation 12 of the Valuation Regulations provides that, unless it is winding-up and not to
be replaced, a scheme which is not normally subject to the Valuation Regulations may nevertheless come within their scope where it is the intention to make a payment to the employer from a surplus. Where excess policy proceeds arise under an insured earmarked scheme, IR SPSS interpret this situation as being within the exception to regulation 12 and so not within the scope of the Valuation Regulations.

Excess policy proceeds may arise, for example, in the following circumstances:

(a) when the use of the life office's own immediate annuity rates or the exercise of the open market option permits the benefit to be bought for less than the policy proceeds;

(b) on leaving pensionable service, when the member elects to take a refund of his or her own contributions;

(c) on retirement or earlier withdrawal, when the employee's final remuneration is lower than was anticipated;

(d) on death during service where no widow, widower, surviving civil partner or dependant exists for whom a pension is needed, or where the ages of such persons result in the cost of the desired pensions falling short of the policy proceeds;

(e) where the scheme provides for post-retirement increases and the pension increases which have been funded are greater than those justified by the increase in the cost of living.

13.25 Approved schemes which, taking account of paragraph 13.24, remain outside the scope of the Valuation Regulations should provide for surpluses to be eliminated by:

(a) augmenting benefits within approvable limits, and/or

(b) set off against the employer's existing liability to pay further contributions to the scheme, and/or

(c) payment to the employer.

Failure to take satisfactory action to eliminate a surplus may result in the scheme having its tax approved status withdrawn (see Part 19).

NB: Except in the circumstances outlined in paragraph 13.28 no payment may be made to an employer without the prior written agreement of IR SPSS.

13.26 Section 601 imposes a 35% tax charge on payments to an employer from the funds of an exempt approved scheme except where:

(a) the employer is a charity or otherwise exempt from income tax or corporation tax, or

(b) the payments fall within certain categories prescribed by the Administration Regulations (regulation 4) (see paragraph 17.39), or

(c) the payment is a repayment of contributions paid in error (see paragraph 5.17).

In practice assessments will not be raised where the total tax payable would be £100 or less. The tax is due on the date that the payment is made to the employer and interest may be charged if the remittance is not made within 14 days of the due date.

13.27 The Administration Regulations contain the detailed rules relating to the assessment and collection of section 601 tax and the procedures can be summarised as follows:

(a) IR SPSS will normally agree a payment to the employer either as a gross amount directly
available for payment or in terms of actuarial value i.e. such an amount as will reduce the actuarial value of a scheme to a given level as at the relevant valuation date.

(b) In the latter case, it is for the scheme to decide which assets are to be liquidated to achieve the desired actuarial result and to notify IR SPSS of the amount available for payment to the employer.

(c) Once the precise amount of the payment has been notified IR SPSS will give instructions in relation to both the payment and the tax liability. The administrator will be issued with a payslip and a return form PFS1 (a specimen of this form is included in Appendix II).

(d) The scheme administrator is responsible for the deduction and payment of the tax (see also paragraph 17.38). The administrator should send the tax payment with the payslip and completed form PFS1 to the Inland Revenue, Finance Division (Worthing), Cashiers Section, Room D42 South Block, Worthing BN12 4XH.

Concessional arrangements for payment to employer

13.28 Concessional arrangements are in force for the payment from a surplus to an employer in certain circumstances without notifying IR SPSS. These arrangements relate to schemes which use individual insurance policies, each earmarked to provide the benefits of a named individual member, where the life office concerned has given an undertaking only to operate the concession in accordance with the conditions outlined in this paragraph and in paragraph 13.29. The life office will be provided with a supply of payslips and forms PFS2 (a special return to be used in this type of case). These will enable it, without reference to IR SPSS, to make payments net of tax to the employer provided that:

(a) the gross amount of the total refund is less than £30,000, and

(b) the administrator has indicated agreement by the completion of both a form PFS2 and a payslip.

The life office must then send both items with the remittance of tax to the Inland Revenue, Finance Division (Worthing) (address as in paragraph 13.27(d)).

13.29 The concession set out in paragraph 13.28 is not available for any scheme which has not yet been granted Exempt Approval nor would it operate where for any reason the payment might not be charged to tax under section 601. Nor is the concession appropriate where the whole scheme is terminating or where one of the employers is ceasing to participate or where there is an unredeemed loan to an employer secured on the policies of the scheme.

The Inland Revenue retains the right to ask for further information about any case and to withdraw the concession if there is evidence that it has been misapplied.

Winding-up

13.30 The treatment of a surplus on winding-up depends on whether or not the scheme is being replaced by another scheme. In this context a "replacement scheme" is any scheme (other than a personal pension scheme) used within 5 years of the winding-up date to provide further retirement benefits for members of the wound-up scheme in respect of service which could be accepted as aggregable with that to which the original scheme applied. Schemes providing only death in service benefits will not be regarded as replacement schemes but the Inland Revenue will not exercise its discretion to approve any subsequent amendment thereto to introduce other benefits. The Inland Revenue may also request additional specific amendments that prohibit certain types of future benefits or members from joining on any other basis.

Scheme being replaced

13.31 If a scheme is being replaced and a payment to the employer is proposed, it must be valued on a continuing basis using the prescribed guidelines. Only if, and to the extent that there is, a surplus in excess of 5% of liabilities on that basis may a payment be made to the employer. Failure to observe this requirement will normally prejudice approval of the replacement scheme.
13.32 If no payment to the employer is proposed the Valuation Regulations do not require a valuation on the prescribed basis unless a valuation is made at the termination date.

**New replacement scheme**

13.33 Where a scheme is wound-up and the members are transferred into a newly established replacement scheme not only will paragraphs 13.31 or 13.32 apply, as appropriate but, whether or not the replacement scheme is subject to the Valuation Regulations, **IR SPSS** may require an actuarial valuation to be submitted as at the commencement date taking account of the transfer of members and any assets from the terminating scheme.

**Existing replacement scheme**

13.34 Similarly where a replacement scheme is an already existing scheme **IR SPSS** may require an actuarial valuation to be submitted as at the date of transfer.

**No replacement scheme**

13.35 If the scheme is not being replaced the prescribed valuation assumptions are not relevant. **IR SPSS** will be prepared to dispense with an actuarial valuation report on the prescribed basis if winding-up is completed within two years of the as at date of the actuarial valuation report. If completion of winding-up is delayed beyond this period then any request by the trustees for the actuarial valuation report to not be submitted will be considered on its merits. Information regarding the schemes funding prepared on a discontinuance basis may be required in lieu of an actuarial valuation report on the prescribed basis. If a scheme in the process of winding-up is subsequently revived then an actuarial valuation report on the prescribed basis will be required in accordance with the Valuation Regulations.

A surplus over liabilities calculated on a discontinuance basis may be paid to the employer. **Again the prior written agreement of IR SPSS to the payment is required.**

When notifying **IR SPSS** of a proposed refund it should be confirmed that there is to be no replacement scheme and a copy of the winding-up balance sheet should be submitted. If the winding-up arises on the sale of part of the employer's business to an unrelated purchaser, the name and address of the purchaser should be given together with confirmation that there is no connection between the vendor and the purchaser.

**Transfers of surplus**

13.36 Subject to the guidance in paragraphs 13.37 and 13.38 about pension scheme reconstructions, a movement of surplus funds in isolation (i.e. without a corresponding transfer of members and/or accrued liabilities) from one scheme to another is not acceptable.

**Scheme mergers and reconstructions**

13.37 An employer is free to merge or reconstruct schemes if desired. This may involve the termination of one or more schemes and the transfer of members and possibly assets from one scheme to another of the same employer, an **Associated Employer** or perhaps an unassociated employer. Where mergers or reconstructions involve block transfers, **IR SPSS** should be consulted in advance concerning any such transfer in accordance with paragraph 10.36. The Inland Revenue reserves the right to call for actuarial valuations if necessary on the prescribed basis.

**Transfer to scheme of unassociated employer**

13.38 Where the employees are transferred into a scheme of an unassociated employer, for example in a take-over situation or on the sale of part of the business, the approach will depend on whether active members of the terminated scheme are granted benefits in the receiving scheme by reference to the aggregate of their service before and after the change i.e. their service is treated as continuous for pension purposes.

If service is treated as continuous the receiving scheme is treated as a replacement scheme and paragraphs 13.31 - 13.34 will apply. Otherwise paragraph 13.35 will apply.

**Centralised schemes**

13.39 A centralised scheme for non-associated employers will be considered, for the purposes of this Part and the Valuation Regulations, to be a collection of separate schemes for individual
employers (although associated employers participating in such a scheme will be treated as one employer for this purpose). This will mean, for example, that where such schemes are self-administered, those participating employers with less than 12 members in the scheme will be excluded from the general scope of the Valuation Regulations or that the special provisions for schemes which have less than 30 members may be in point (regulation 11(4) of the Valuation Regulations).

Money purchase schemes

13.40 The Valuation Regulations do not distinguish between schemes which provide defined benefits and those funded on a money purchase basis. Where a money purchase scheme which falls within the scope of these Regulations applies funds for specified target benefits, the rules for calculating a surplus should be applied by reference to the target benefit levels. Target benefits should, for this purpose, be deemed to accrue uniformly over the relevant service. Where no target is specified it should be taken to be the maximum approvable within Inland Revenue limits.

Overseas scheme

13.41 An exempt approved scheme is within the provisions of section 601, 602 and Schedule 22 in respect of the whole of its assets and liabilities notwithstanding that some of its members may be overseas. A United Kingdom scheme which is treated as two or more separate schemes under section 611(3) will, however, be subject to these provisions only in respect of that part which has been treated as an exempt approved scheme.

13.42 An overseas scheme, to the extent that it is exempt approved (i.e. section 611(3) may be relevant), is subject to section 601, 602 and Schedule 22 through the person described in section 590(2)(c). Any charge to section 601 tax will be assessable on the employer whose United Kingdom undertaking employs the members.
Part 14. Discontinuance of Schemes

General

14.1 Neither tax legislation nor Inland Revenue practice requires an employer to set up a pension scheme, or, having done so, to enter into an open-ended commitment to continue to contribute. Subject to its contracts of employment with its employees, an employer is free to cease contributing at any time.

14.2 It is therefore necessary for the rules of an approved scheme to specify what is to happen if the employer's contributions cease. A scheme may be discontinued either by being made paid up (such a scheme is sometimes referred to as a frozen scheme) or by winding-up.

14.3 IR SPSS should be notified of a scheme’s discontinuance in routine cases after the event on form PS 199 - a specimen copy is included in Appendix II. However, it is necessary to inform IR SPSS at an earlier stage in any of the following circumstances:-

(a) if the scheme is not yet approved (see paragraph 14.11);
(b) if it is proposed to treat the scheme as abandoned (see paragraphs 14.14 and 14.15);
(c) if it is proposed to refund monies to the employer(s) (see paragraph 16.6);
(d) if a block transfer is to be made (see paragraph 10.36).

Paid up Schemes

14.4 A scheme is "paid up" when all contributions cease but the assets of the scheme continue to be held by the administrator to be applied in accordance with the rules. It is possible for a scheme to continue in paid up form despite the employer ceasing to exist, but this should not be done without the prior agreement of IR SPSS (also see paragraphs 20.84 – 20.86 in relation to small self-administered schemes). This agreement is unlikely if the scheme is in surplus or there is a prospect that a surplus will arise in the future. In any event a paid up scheme must eventually wind-up when no assets or beneficiaries remain.

Winding up

14.5 When a scheme is wound-up it ceases to exist and to achieve this both its assets and its liabilities must be disposed of. To the extent that the assets and liabilities match, this may be done by securing the benefits under individual buy-out contracts with insurers (see paragraphs 10.42 et seq.), or by transfer to other approved schemes or personal pension schemes (see paragraph 10.21 et seq.) or by assigning individual scheme policies to the members (see paragraph 10.43).

14.6 Except in the case of a money purchase scheme, an employer is required by DSS pensions legislation to make good any deficiency of assets needed to meet a scheme's liabilities on winding-up. The winding-up rule may specify an order of priorities between the various classes of beneficiaries on the winding-up of the scheme e.g. existing pensioners may be given preference over those with contingent interests and present employees although the Inland Revenue are not generally concerned with this aspect of the scheme rules.

14.7 In the event of a surplus the rules may provide for benefits to be augmented within approvable limits with active members being treated as having withdrawn from service on the date that the benefits were determined (see Part 10). Any remaining surplus should be dealt with in accordance with paragraph 13.31 or paragraph 13.35 (as qualified by paragraph 9.7) depending on whether or not there is a replacement scheme. Any part of a surplus which is attributable to Additional Voluntary Contributions paid by members should be dealt with in accordance with paragraph 4.7.

14.8 The scheme rules may provide for any trivial pensions to be fully commuted at the time of
winding-up (see paragraph 8.12 et seq.) and for refunds of contributions to employees with less than 2 years qualifying service (see paragraph 10.52 et seq.). Where no pensions are payable, trivial lump sums (i.e. in aggregate not exceeding £2,500) may be paid on winding-up. This does not apply to any trivial residue remaining after the initial part of a two-stage transfer payment has been made - see paragraph 10.41c.

14.9 Payments which give rise to tax liability should be reported to HM Inspector of Taxes dealing with the tax affairs of the scheme or, where this is not known, to IR SPSS who will forward it to the appropriate Tax District (see paragraph 16.6).

Partial Winding up

14.10 A scheme which provides for the participation of more than one employer (whether or not restricted to employers who are associated with a principal employer) should provide for that part of the scheme relating to any participating employer to be wound-up if that employer goes out of business or leaves the scheme for other reasons. The same considerations apply to a partial winding-up as to a total winding-up, i.e. paragraphs 14.3 and 14.5 - 14.9 apply (see also paragraph 21.6).

Discontinuance at Interim Stage – where application received before 6th April 2002

14.11 Where a scheme is discontinued at interim stage because, for example, the employer has ceased to trade or has gone into liquidation IR SPSS should be informed of the reason for the discontinuance and of how it is intended to deal with the scheme i.e. whether it is to be made paid up or whether it is to be wound-up. If it is to be made paid-up full definitive documents or a documentation certificate will be required before exempt approval may be given. If it is to be wound-up and the definitive documents have not been submitted to IR SPSS when the winding-up is proposed, the action to be taken will depend upon the type of scheme involved and how long it has been in existence. This paragraph only applies where the approval application was received by IR SPSS before 6th April 2002.

14.12 In the case of insured schemes which have been in existence for less than 2 years and have 100 or less members IR SPSS will normally be prepared to approve the scheme on the basis of a declaration (PS 160) - a specimen is included in Appendix II - signed by the trustees and the employer to the effect that:

(a) the scheme has been administered from its establishment in accordance with the terms of the interim trust deed and the initial announcement made to the members and in a manner consistent with the requirements for approval under Chapter I Part XIV as amended by section 75 and Schedule 6 Finance Act 1989, and

(b) has been administered in accordance with the requirements of regulation 5 of the Retirement Benefits Schemes (Restriction on Discretion to Approve) (Additional Voluntary Contributions) Regulations 1993 (SI 1993 No 3016) and where the scheme is the "leading scheme" in relation to a member, with the requirements of regulation 6 of those Regulations so far as they concern "main schemes" and,

(c) the scheme has been, or will be, wound-up in a manner consistent with such requirements.

Where such a declaration is impracticable because, for example, the employer is also the trustee and has gone into liquidation, IR SPSS will normally be prepared to accept a written assurance to the same effect from the life office. This paragraph only applies where the approval application was received by IR SPSS before 6th April 2002.

14.13 In the case of insured schemes which have more than 100 members and all self-administered schemes IR SPSS will normally expect to be provided with more formal documentation. However, full definitive documents are not usually required and Exempt Approval may be given after the execution of a short supplemental deed setting out the events which have
occurred. The deed should contain similar wording to that described in paragraph 14.12 above and enabling powers for dealing with the scheme assets and to cover any benefits already paid. This paragraph only applies where the approval application was received by IR SPSS before 6th April 2002.

**Abandonment - scheme not approved**

14.14 A scheme may normally be abandoned, with IR SPSS agreement, if

- it has not yet received exempt approval,
- it is fully insured,
- it has less than 100 members,
- the trustees are satisfied that the terms of the trust allow it, and
- none of the members has completed two years qualifying service.

Where a member has completed two years qualifying service - defined in section 71 Pension Schemes Act 1993 (PSA 93) - the member is entitled to preserved benefits within the terms of PSA93. As the member is entitled to short service benefit it is not possible to abandon the scheme.

To abandon the scheme the policies are surrendered and all premiums paid are refunded to the employer (and employee where they have contributed). Deductions may be made for life office expenses etc.

Abandoned schemes will not receive tax approval. Any tax reliefs granted provisionally will be withdrawn.

**Abandonment - scheme approved**

14.15 If an approved scheme that falls within paragraph 14.14 is to be abandoned it will be necessary for IR SPSS to formally cancel the approval of the scheme. However, where the correct approval procedure has taken place, and there is no change in the terms and conditions notified to IR SPSS when approval was granted, IR SPSS can not cancel the approval of the scheme. In these circumstances where a scheme is no longer required, it should be made paid up or wound up in accordance with the scheme trust deed and rules.

Where it is discovered that the conditions notified to IR SPSS on which approval was granted have changed IR SPSS will consider cancelling the approval of a scheme. An example may be that it is discovered that the members are self employed and taxed under Schedule D and hence not eligible ‘employees’ as defined in Section 612. In these circumstances the scheme trustees/administrator should apply to IR SPSS for the scheme approval to be formally cancelled stating the circumstances that have changed.
Interpretation

15.1 For the purposes of Part 15.2 to 15.5 inclusive, the term "overseas employer" means one who is not resident for tax purposes in the United Kingdom, with trading profits which are liable to United Kingdom tax only to the extent that they arise from a branch or an agency in this country.

Overseas Employer

15.2 An overseas employer's scheme can be approved in its entirety if it relates wholly to employees who are chargeable to UK tax under Case I or II of Schedule E. Such schemes must have an appropriate membership restriction in their rules. Form PS262A (draft rule amendment) can be used for this purpose.

15.3 Where membership of an overseas employer's scheme is not restricted in this way approval can be given to the element of the scheme which relates to employees who are chargeable to UK tax under Case I or II of Schedule E. The scheme will be granted split approval under section 611 (3). For the purposes of any claim for United Kingdom tax reliefs and exemptions a split approved scheme must either segregate its assets or calculate actuarially the proportions relating to the approved and unapproved elements of the scheme.

15.4 It is a condition of approval that where an administrator is resident overseas a person resident in the United Kingdom (the agent) should be appointed to act on his or her behalf. Form PS259 should be used for this purpose. The agent will be responsible for securing compliance with the administrator's duties under the tax approval rules. So, for example, all pensions payable under an approved scheme or the approved element of a scheme must be paid through the agent who will be responsible for the operation of PAYE. A pensioner resident abroad may qualify for the exemption described in paragraph 17.5. The provisions of sections 65 (2) or 196 will not apply to pensions from an approved scheme.

15.5 Schemes established by an overseas employer solely to provide benefits for employees who work abroad and who are not chargeable to UK tax under Case I or II of Schedule E cannot be approved.

Overseas Employees

15.6 Employees who are performing their duties abroad for a United Kingdom resident employer may be provided with benefits under an approved scheme - whether or not the employees are chargeable to UK tax under Case I or II of Schedule E (see paragraph 4.4 regarding contributions by the employee). Such employees must have a contract of employment with the UK resident employer. They must also receive remuneration from the employer (unless they are an officer or director of it, or manage its affairs).

15.7 An employee whose earnings are not chargeable to UK tax under Case I or II of Schedule E may be provided with benefits through an unapproved scheme without liability arising under section 595. The benefits need not therefore conform to the conditions for approval, but liability will arise under section 596A on benefits paid while he or she is resident in the United Kingdom. Liability under section 596A in respect of lump sum benefits may be mitigated if the criteria set out in Extra Statutory Concession A10 are satisfied. (The text of Extra Statutory Concession A10 is set out in a free booklet IR1 which is available from any Tax Enquiry Centre or Tax Office or from the Inland Revenue Information Centre, South West Wing, Bush House, Strand, London WC2B 4RD.)

Employee Permanently Transferred Abroad

15.8 An employee will cease to be eligible for membership of a wholly approved scheme, or of the approved element of a scheme granted split approval (see paragraph 15.3), if permanently
transferred to an employment with an overseas employer and his or her earnings cease to be chargeable to UK tax under Case I or II of Schedule E. No further benefits should then accrue under the wholly/split approved scheme. The benefits should be restricted to those based on service and remuneration while eligible for membership of the wholly/split approved scheme. The employee should be treated as having left pensionable service. In certain circumstances the accrued benefits may be transferred overseas (see paragraph 10.39).

**Employee Temporarily Working Abroad For an Overseas Resident Employer**

15.9 Unless the specific consent of IR SPSS has been obtained, an approved scheme may include employees whose duties are performed wholly abroad for an overseas employer only in the circumstances and subject to the conditions described in paragraphs 15.10 and 15.11. Such employees must have a contract of employment with the overseas resident employer. They must also receive remuneration from the employer (unless they are an officer or director of it, or manage its affairs).

15.10 The circumstances referred to in paragraph 15.9 are that:

(a) there is a definite expectation that the employee will come to the United Kingdom either to take up employment with an employer participating in the scheme (such an expectation should be evidenced in writing), or to retire, or

(b) the employee's earnings remain chargeable to UK tax under Case I or II of Schedule E because he or she only works overseas for periods which total less than 365 days in any year.

15.11 The conditions are that:

(i) the United Kingdom employer should continue to pay to the approved scheme any employer contributions due, but must be reimbursed by the overseas employer annually or more frequently for the costs, unless IR SPSS have specifically agreed otherwise, and

(ii) the prospective pension in respect of the service abroad should be calculated and funded by reference to the rate of remuneration appropriate for similar employment in the United Kingdom.

There is no requirement that an employee must have been sent abroad,

Having completed a period of service in the United Kingdom. An employee who is recruited to work initially for an overseas employer, may join an approved scheme without the need for a prior period of employment with a United Kingdom resident employer or the United Kingdom branch of an overseas employer in the circumstances described in paragraph 15.10 if the conditions specified in paragraph 15.11 are met.

In relation to the exception in (i) above, agreement will generally be given only where reimbursement is not possible because of exchange control difficulties or because the law of the overseas country prohibits transfers of assets to the United Kingdom. Reimbursement payments do not need to be made where the member's scheme is currently undergoing a contributions holiday.

15.12 An employee may continue to accrue benefits under an approved scheme while temporarily performing duties abroad even if he or she becomes a member of an overseas scheme. If the employee does so, however, it will not be possible to transfer the benefits of that other scheme into an approved scheme in the United Kingdom.

**Temporary Unpaid Absence Overseas**

15.13 An employee who is temporarily absent overseas and is not in paid employment (or self employment) during the period of absence, may remain in full membership of an approved scheme
if:

(a) there is a definite expectation of return to service with the employer which is evidenced in writing,

(b) he or she has provided the employer with a written undertaking not to do paid work whilst absent, and

(c) the period does not exceed 10 years.

15.14 Full membership must cease immediately if the employee commences paid work unless it is with the employer, with another participating in the scheme, or with an overseas employer on secondment. In the case of secondment, the conditions described in paragraphs 15.10 and 15.11 must apply, except that the maximum period of service abroad of 10 years specified in 15.11(iii) has to take account of the unpaid absence overseas as well as the overseas secondment.

**Corresponding Schemes**

15.15 An employee who is in receipt of "foreign emoluments" (i.e. broadly, a person who is not domiciled in the United Kingdom and is employed in the United Kingdom by an overseas employer) might choose to remain a member of an overseas scheme. If the overseas scheme is accepted by the Inland Revenue as "corresponding" to a United Kingdom approved scheme then the employee will be eligible for relief under section 192(3) on personal contributions to the overseas scheme. Also, under section 596(2)(b) he or she will not be liable to a charge to tax under section 595 in respect of any employer's contributions to the overseas scheme.

15.16 In order for an overseas scheme to be accepted as "corresponding" the following conditions must all be met. They are:

(a) the scheme should be established in a country where the employee was working or resident immediately before being sent to the United Kingdom, or in a country where the employer or an associated employer has an operating presence.

In exceptional circumstances an "international scheme" (i.e. a scheme exclusively for the benefit of employees working outside the country in which the scheme is established) may also be acceptable even where it does not meet the criterion above (see paragraph 15.17);

(b) the tax or supervisory authorities of the country in which the scheme is established should recognise it as a scheme for the provision of relevant benefits;

(c) the amount of the benefits should be reasonable (for example a pension should not normally exceed 70% of the final salary or the usual maximum allowed in the country in which the scheme is established);

(d) the primary purpose of the scheme should be the provision of relevant benefits which should normally be payable on retirement no earlier than age 50 (unless earlier payment dates are permitted in the country in which the scheme is established) or upon death;

(e) the contributions to the scheme by the employer and the employee should be reasonable in relation to the benefits to be paid. The level of contributions paid should conform to the actuarial standards of the country where the scheme is established, or in the absence of such standards to United Kingdom actuarial practice.

15.17 An "international scheme" will normally only be exempt from the location criterion set out in paragraph 15.16 (a) if:

i) it is legally impossible to establish a scheme for the foreign emoluments employee in the jurisdiction of location, or
ii) it is a scheme for a multi-national group to which all expatriate (or at least career expatriate) employees belong.

15.18 To obtain acceptance that an overseas scheme corresponds to a UK approved pension scheme for the purposes of 355 and 390 ITEPA 2003, a form PS3008 should be sent to IR SPSS

If the scheme is considered satisfactory for corresponding purposes, IR SPSS will formally notify the applicant and tax office(s) that the scheme has been accepted as a corresponding scheme under the provisions of sections 355 and 390 ITEPA 2003 A unique reference number in the SF74/series will be allocated to the scheme in question. That reference should be quoted when a claim for corresponding relief is made to a scheme member’s tax office. A PS3008(UA) or PS3008(UB) undertaking should be signed by the member and the scheme’s administrator where appropriate.

15.19 It may also be possible for a member of a "corresponding" scheme to be granted similar reliefs (to those referred to in paragraph 15.15) under a particular Double Taxation Agreement even where he or she is not in receipt of foreign emoluments.
Part 16. Administration of Schemes

Duties of Administrator

16.1 Chapter I Part XIV places specific duties on the administrator of a retirement benefits scheme. Where the administrator is the employer these include the requirement to notify the Inland Revenue (the employer's Inspector of Taxes) that a "top-up" scheme (viz. a scheme providing benefits in addition to those provided under an approved scheme(s)) has come into existence. It also specifies how to apply for approval and, if the scheme is approved, sets out requirements for the provision of information to the Inland Revenue. Such information includes providing IR SPSS, when asked, with certain details about the scheme for compliance audit purposes.

16.2 These duties are extended by Regulations (e.g. the Surplus Regulations - see Part 13) and by conditions prescribed by the Inland Revenue for the granting of approval under its discretionary powers. Most of these requirements are described in full elsewhere in these notes. The following paragraphs, however, provide both a summary of all these duties and a full description of those not dealt with elsewhere (e.g. in relation to Free standing Additional Voluntary Contribution Schemes).

16.3 Section 604 requires an application for approval to be made by the trustees (or scheme sponsor/s in the case of a non-trust scheme) in the prescribed form before the end of the first year of assessment for which approval is required (see Part 18).

16.4 The Information Powers Regulations (see paragraph 1.10) came into force on 1 January 1996. These Regulations were made under the powers contained in section 605 and they extend and modernise the Inland Revenue's authority to require submission of, or to inspect, information and underlying books, documents and other records relating to retirement benefits schemes. They also introduce minimum periods for which scheme records must be retained.

16.5 Part II of the Regulations details the items and events which must be submitted or notified to IR SPSS automatically at prescribed times. Failure to comply may lead to penalties under section 98 Taxes Management Act 1970. Some of these events were formerly required to be notified by virtue of undertakings signed by the administrator (SF 176(U) for schemes or SF 177(U) for individual arrangements) as a condition of approval. The most important items from the undertakings have been brought into these Regulations and the remainder have been dispensed with. The undertakings were therefore abolished in relation to events which occurred on or after 1 January 1996 and it is no longer necessary for them to accompany an application for approval on forms PS 176 and PS 177.

16.6 The administrator of an approved scheme or previously approved scheme is required by regulation 10 of the Information Powers Regulations to report certain payments, which give rise to tax liability on the part of the administrator or the employer, to the Inland Revenue on form 1(SF) not later than 30 days after the end of the year of assessment in which the event occurs. Such reports are required irrespective of whether the events have already been the subject of correspondence with IR SPSS. These payments are:

(a) a refund of a member's contributions (see paragraph 17.22),

(b) a repayment of surplus Additional Voluntary Contributions to a member (see paragraph 17.35),

(c) a payment in commutation of pension on grounds of triviality or serious ill-health (see paragraph 17.27), or

(d) any payment of surplus assets or excess policy proceeds to the employer (see however Part 13 regarding the need to obtain the prior written agreement of IR SPSS).
The completed form 1(SF) should be sent direct to HM Inspector of Taxes dealing with the tax affairs of the scheme or, where this is not known, it may be sent to IR SPSS who will forward it to the appropriate Tax District. Cheques in payment of tax liabilities should not be sent to IR SPSS. Any tax deductible by the scheme administrator for an employee is not reclaimable by the employee. For this reason a certificate of deduction of income tax, R185 should not be used when notifying the employee of the (net) payment.

16.7 Regulation 11 of the Information Powers Regulations covers the requirements equivalent to those in regulation 10, referred to above, for insurance companies to account direct to the Inland Revenue on form 2(SF) - a specimen is included in Appendix II, for any tax arising in cases of full commutation, refunds to employees and payments to employers, where a pension has been secured by the purchase of an individual annuity contract. This provision is necessary because the administrator of the scheme in which the benefits accrued has no continuing legal responsibility once they are bought-out.

16.8 The administrator is also responsible for providing information to IR SPSS within prescribed periods in respect of the following items and events:-

- (a) actuarial valuation reports on self-administered and certain insured schemes (see paragraph 16.14),
- (b) investment and borrowing transactions of small self-administered schemes (see paragraph 20.49 et seq.),
- (c) admission of a new employer in a scheme (see paragraphs 21.5 and 21.14(b)),
- (d) special contributions by employers (see paragraph 5.7),
- (e) membership of controlling directors in schemes (see paragraph 3.8),
- (f) proposals to pay controlling directors' benefits on retirement due to incapacity or serious ill-health (see paragraphs 6.3 or 8.22 respectively) and
- (g) certain transfer payments for individuals (see paragraphs 16.17 & 16.18).

16.9 Part III of the Information Powers Regulations gives the Board the authority to issue notices requiring particulars and documents relating to any aspect of scheme administration. Regulation 12 relates to approved schemes (including schemes previously approved) and relevant statutory schemes whereas regulation 13 mirrors regulation 12 where annuity contracts have been used to secure benefits which accrued under schemes.

16.10 Part IV of the Information Powers Regulations introduces a power allowing authorised officers of the Board to inspect all books, documents and other records relating to all monies going into and out of a scheme and all investments or other assets within a scheme. It also brings in a requirement that scheme records must be kept for six years from the end of the scheme year in which the act, event, transaction, payment etc occurred.

16.11 The automatic reporting requirements, the notice provisions and the inspection powers in Parts II, III and IV of the Information Powers Regulations are linked, via section 605(1A)(a) to (d), to the “Special returns etc” penalties contained in section 98 Taxes Management Act 1970. These provide for the imposition of an initial penalty of up to £300 and in the event of continuing failure to comply a daily penalty of up to £60. There is also a penalty of up to £3,000 if any person fraudulently or negligently gives incorrect information in connection with these requirements. A similar penalty will be imposed under section 605(1C) for failure to comply with the requirements to retain records.
16.12 It is a condition of approval that the administrator will advise IR SPSS at once if there is any alteration to the rules or other terms of the scheme. Unless the alteration is of a type which is specified in Regulations as not requiring the approval of the Board, it must be approved by IR SPSS otherwise the scheme’s approval will lapse from the date of the amendment. IR SPSS is prepared to consider proposed rule amendments in advance of their being put into effect if there is doubt over their acceptability (see also paragraph 18.14).

16.13 The administrator of a scheme to which the Pension Scheme Surpluses (Valuation) Regulations 1987 apply (see paragraph 13.3) is required to produce to the Inland Revenue either an actuarial valuation or a certificate on form PS 162 (a specimen is included in Appendix II) at prescribed intervals (see paragraph 13.6). Other defined benefits schemes are required to produce actuarial reports at intervals no longer than 5 years (but see paragraph 13.7). A small self-administered scheme is required to produce actuarial reports at 3 yearly intervals (see paragraph 13.6).

16.14 Under regulation 4 of the Information Powers Regulations actuarial valuation reports with effective dates on or after 1 January 1996 are required to be submitted to IR SPSS not later than two years from the effective date of the valuation in the case of large self-administered schemes and certain insured schemes as defined in paragraph 13.4(b) and not later than one year from the effective date of the valuation in the case of small self-administered schemes. Where a surplus certificate in a prescribed form is submitted in lieu, as described in paragraph 13.6, it will be regarded as satisfying the reporting requirement.

16.15 The administrator of an exempt approved scheme has a duty under the Pension Scheme Surpluses (Administration) Regulations 1987 to deduct from any payment to the employer any tax payable in respect of that payment under section 601 (see paragraph 13.27). The Regulations require the administrator to make a return in respect of the payment within 14 days and to pay the tax without an assessment being raised.

16.16 An administrator has a general duty to pay any amount of tax properly assessed upon him or her, e.g. in relation to repayment of a member’s contributions or commutation in special circumstances.

16.16a With effect from 6/4/2003 regulation 11A of the Information Powers Regulations requires certain transfers to be reported by

- the administrator of an approved scheme making a transfer. (This includes a scheme for which an approval application has been made but which has not yet received approval.);
- the administrator of a relevant statutory scheme making a transfer, or
- the insurance company in respect of a deferred annuity contract (a policy that does not provide immediate benefits) making a transfer.

Reports are required where the following 2 conditions are met:

**Condition 1**

The transfer is made to any scheme or arrangement other than

- a relevant statutory scheme, or
- a statutory scheme which is approved, or
- a compulsory purchase annuity contract providing immediate benefits.
**Condition 2**

The transfer either

- on its own, or
- when added together with any other transfer payment made in the previous 364 days from the same scheme for the same member

has a market value of £250,000 or more.

For the avoidance of doubt potentially reportable transfers include

- transfers of *pension credits*, and
- the assignment of a policy into the member's name where the policy does not immediately start paying benefits

The reporting requirement only refers to individual transfers. Bulk/block transfers should continue to be reported in accordance with paragraph 10.36.

Reports are required to be made within 28 days of the date of the transfer. Form number PS 7050 should be used to report the transfer.

16.16b With effect from 6/4/2003 regulation 11B of the Information Powers Regulations requires certain transfers to be reported by:

- the *administrator* of a scheme which is actually approved that receives a transfer (but not a statutory scheme that is approved), or
- the insurance company in respect of a deferred annuity contract (a policy that does not provide immediate benefits) receiving a transfer payment.

Reports are required where the following 2 conditions are met:

**Condition 1**

The transfer either

- on its own, or
- when added together with any other transfer payment received by the same scheme for the same member in the previous 364 days

has a market value of £250,000 or more.

**Condition 2**

The transfer is not one required to be reported under regulation 11A of the Information Powers Regulations.

For the avoidance of doubt potentially reportable transfers include:

- transfers of *pension credits*;
- the assignment of a policy into the member's name where the policy does not immediately start paying benefits.

The reporting requirement only refers to individual transfers. Bulk/block transfers should continue to be reported in accordance with paragraph 10.36.
Reports are required to be made within 28 days of the date of the transfer. Form number PS 7050 should be used to report the transfer.

16.16c Certain individual transfers still need prior clearance from IR SPSS (see paragraphs 10.24(h), 10.24(i), 10.25, 10.39 and 10.40). Such transfers may still fall within regulation 11A and 11B of the Information Regulations to be reported after the transfer has been made. Where

- the information given to IR SPSS to consider agreement to the transfer is as provided on form PS 7050 (the form may be used for this purpose), and
- the transfer actually proceeds within 1 month of IR SPSS agreement to the transfer, and
- the details provided to IR SPSS remain the same – a tolerance of +/- 5% in the value of the transfer is acceptable -

the reporting requirement under regulation 11A or 11B (as appropriate) will be regarded as having been met by the provision of the information to IR SPSS before the transfer is made.

16.17 The Personal Pension Scheme (Transfer Payments) Regulations 2001 (SI 2001 No 119) provide that benefits from a transfer value into a personal pension scheme from an approved scheme or a relevant statutory scheme may, in certain specified circumstances, be paid in lump sum form only to the extent certified by the administrator of the transferring scheme. The circumstances are where:

(a) the transferring member is, or has been at any time during the period of ten years prior to the date of the transfer payment, in relation to any employment to which the transfer payment or any part of it relates, a Controlling Director, or

(b) the transferring member

- was aged 45 or more on the date the transfer payment was made, and
- his or her annual remuneration is, or was, for any year of assessment falling (wholly or partly) during the period of six years prior to the transfer date, more than the allowable maximum (i.e. the equivalent for Personal Pension Schemes of the Permitted Maximum) for the year of assessment in which the transfer date falls.

A condition of approval of certain schemes with a normal retirement date of age of 45 or less where lump sum benefits are also provided under a separate scheme (but are aggregable for the purposes of Inland Revenue limits) is, on transfer to a personal pension scheme, the administrator will provide a certificate showing the amount of tax-free lump sum payable from the transfer payment. It is a further condition of approval of the personal pension scheme that the scheme personal pension scheme administrator complies with the certificate when benefits are paid from the personal pension scheme.

16.18 The Regulations referred to in paragraph 16.17 above also restrict the payment of lump sum benefits from a personal pension scheme

- where transfers originate from schemes where retirement benefits are restricted to the form of non-commutable pension (see paragraph 10.35), or
- where transfers consist of pension credit rights which are themselves non-commutable (see paragraph 6A.26).

In either of these circumstances, the transferring scheme should provide a certificate to the effect that the transfer value is not to be used to provide retirement benefits in lump sum form (viz. a Nil certificate). Where, as a result of an earlier transfer, a transfer payment includes an amount from
such a source, the certificate must specify how much of the transfer payment emanates from that source and is subject to that restriction. This requirement is relevant to transfer payments which arise from:

(i) an approved scheme (including a Free standing Additional Voluntary Contribution Scheme) the benefits of which are funded solely by employees' voluntary contributions where that contract commenced after 7 April 1987, or

(ii) a fund to which section 608 applies, or

(iii) an approved scheme with a normal retirement date of age 45 or earlier where benefits are wholly in non-commutable pension form because a lump sum retirement benefit is provided from another source, for example, as is the case for the individual English league football club schemes for professional footballers, or

(iv) a non-commutable pension rights credit.

16.19 It is a condition of approval or continuation of approval that an administrator making a transfer in any of the circumstances set out in 16.17 or 16.18 should provide the required certificate. An administrator of an approved scheme or relevant statutory scheme may also, in the case of an individual within paragraph 16.17(a) or (b), be asked to provide a certificate in relation to the amount of a proposed transfer payment to a personal pension scheme, in accordance with Regulation 8(3) of the Regulations referred to in paragraph 16.17 and Appendix XI. If able to do so, the administrator must comply with the request.

16.20 Where a transfer payment is made from one approved scheme to another (whatever its nature), it is not necessary for the administrator of the transferring scheme to give, or the Administrator of the receiving scheme to obtain, a lump sum certificate in respect of the transferring member unless:

(a) the transfer payment, either in whole or in part, may not be used to provide retirement benefits in lump sum form (see paragraph 10.35), or

(b) the transferring member is entitled to Continued Rights in the receiving scheme, or

(c) the receiving scheme is a simplified defined contribution scheme.

NB It is not necessary for a lump sum certificate to be given or obtained where a transfer takes place between schemes of the same employer or in the circumstances described in paragraph 10.30.

16.21 The requirements of paragraphs 16.17-16.20 apply equally to transfers from the following:

i) buy-out policies taken out on or after 6 April 2001,

ii) policies assigned to members (see paragraph 10.43) on or after 6 April 2001, and

iii) free standing additional voluntary contribution schemes.

Buy-out policies taken out before 6 April 2001 will remain subject to the concessionary practice existing at the date the buy-out policy was effected. For individuals who, in respect of any period of employment to which the proposed transfer, or any part of it, relates, were

- controlling directors at any time during the period of 10 years prior to the date on which the application is made to transfer from the section 32 contract, or

- earning in excess of the allowable maximum for any year during the period of 10 years prior to the date on which the application is made to transfer from the section 32 contract
• a transfer will only be possible if an old-style regulation 6(3) certificate (under SI 1988/1014)

• was either completed at the time the contract was taken out, or is now completed by the administrator of the original occupational scheme as at the date of the transfer to the section 32 policy, and

• is passed on to the scheme administrator of the receiving personal pension scheme with the transfer payment.

The concessionary practice for section 32 contracts may also be applied to policies assigned to the member on leaving service or on winding up.

It is also a condition of approval or continued approval of an approved scheme with a normal retirement date of age 45 or less that, on making a transfer to any other scheme (whether it is an employer's scheme or of the personal pension scheme type), the administrator will certify to the receiving scheme the latest date on which the member's transfer benefits may come into payment in accordance with the transferring scheme rules and it is also a condition of approval or continued approval that the receiving scheme complies in this respect.

16.22 If a transfer value is fragmented, e.g. part transferred to a personal pension scheme or a buy-out policy and part to the pension scheme of a new employer, the amount certified should also be split proportionately to the amount of each transfer payment to ensure that the total lump sums flowing from the transfer payment are consistent with the amount payable in that form from the scheme had the transfer not been made.

16.23 Where a lump sum certificate is required in respect of a member in accordance with paragraphs 16.17-16.20, the lump sum should be calculated in the manner set out in Part 10.

16.24 Where a member has received Additional Voluntary Contributions benefits prior to receipt of their employer funded benefits and a transfer payment is being made to a buy-out policy or another approved scheme (excluding any scheme where the transfer value will be a retained benefit) the Administrators or Life Offices (in respect of buy-out policies) will need to supply to the receiving scheme (or Life Office): -

• the details of the status of the member,

• a statement of the member’s annual earnings after age 50 and

• the aggregate amount of the Additional Voluntary Contributions pension drawn up to the date of the transfer.

The reasoning for this to ensure that the Additional Voluntary Contribution benefits are brought into account for the purposes of the maximum benefits limits checks at their “pension equivalent”. Further guidance in this respect can be found in Part III of Appendix XII.

16.25 An employee accruing benefits under an approved scheme has a right to contribute to a Free standing Additional Voluntary Contribution Scheme to secure further relevant benefits. These further benefits are subject to the usual Inland Revenue limits and must be aggregated with those provided under the approved scheme. The contributions paid to the Free standing Additional Voluntary Contribution Scheme will, if they exceed £2,400 in a year of assessment, need to be tested to ensure that they do not exceed an amount necessary to secure any headroom between the benefits under the approved scheme and the maximum approvable benefits.

16.26 The headroom check is carried out by the Free standing Additional Voluntary Contribution Scheme provider. The administrator of the approved scheme has, however, a statutory duty (under the disclosure requirements of the relevant DSS pensions legislation) to provide the member with sufficient information to enable the headroom check to be carried out.
16.27 So that the benefits from employers' schemes and Free standing Additional Voluntary Contribution Schemes are properly aggregated (and any over-provision correctly utilised) both sorts of scheme are required to liaise with each other and keep relevant records.

Employers' main schemes will receive notifications from Free standing Additional Voluntary Contribution Schemes to the effect that members of the former are contributing to the latter. They will also receive notifications from leading schemes (see paragraph 16.28) about benefits secured for main scheme members under Free standing Additional Voluntary Contribution Schemes. Main scheme administrators are required to keep a record of these notifications for a period of 6 years from the end of the tax year in which the relevant date (see paragraph 16.28) occurs. The notification(s) for a particular employee may be passed with a transfer to a new scheme in the circumstances described in paragraph 10.30.

Both Free standing Additional Voluntary Contribution Schemes and employers' main schemes must notify each other whenever there is a change in the name or address of the administrator. In addition, employers' main schemes must notify leading schemes about any Free standing Additional Voluntary Contribution Schemes known to be providing benefits additional to those provided by the main schemes.

16.28 The occasion for checking whether the payment of Additional Voluntary Contributions to a Free standing Additional Voluntary Contribution Scheme has produced a surplus is called the "relevant date". This term is defined in the Retirement Benefits Schemes (Restriction on Discretion to Approve) (Additional Voluntary Contributions) Regulations 1993(SI 1993 No 3016) as the earliest of the member's retirement, death or leaving pensionable service. If the member has also paid Additional Voluntary Contributions under the current employer's pension scheme(s) (other than to secured added years of service) then the scheme providing the member's basic benefits is regarded as the "leading scheme" and the administrator of that scheme is responsible for calculating any surplus and ensuring that:

(a) all non-surplus benefits are paid,

(b) the member is given a choice whether the value of any surplus benefits is repaid or is utilised to provide further benefits within normal approvable limits. If the member (or his or her personal representative), fails to exercise this choice within three months of being notified of the over-provision the member is deemed to have chosen repayment of the over-provision, and

(c) any remaining surplus is repaid.

Where a member has paid no Additional Voluntary Contributions under the employer's schemes, the leading scheme will be the Free standing Additional Voluntary Contribution Scheme from which a notification of membership in accordance with paragraph 16.27 was last received.

16.29 When the leading scheme is a Free standing Additional Voluntary Contribution Scheme, the administrator of the employer's main scheme is required to provide the leading scheme with a certificate showing details of:

(a) the initial amount of the member's pension (before commutation under Part 8 or allocation under paragraph 12.5) payable or prospectively payable under all schemes of the employer or to which the employer has contributed,

(b) the prospective spouse's or civil partner's pension (excluding pensions provided by allocation under paragraph 12.5) payable under all schemes of the employer or to which the employer has contributed,

(c) the rate of post-retirement increases of the pensions payable either guaranteed or, where not guaranteed, the average of the percentage by which pensions payable have been
increased in each of the three years preceding the relevant date,

(d) the maximum annual amount under the rules of the employer's scheme of the aggregate member's pension payable from all approved or relevant statutory schemes in respect of the member's service with the employer,

(e) the maximum annual amount under the rules of the employer's scheme of the prospective spouse's or civil partner's pension payable from all approved or relevant statutory schemes providing benefits in respect of the member's service with the employer,

(f) the identity of any other Free standing Additional Voluntary Contribution Schemes to which the member has contributed by reference to the employment, and

(g) the measure of final remuneration upon which the maxima in (d) and (e) and, where appropriate, (i) below were based.

If the relevant date is the date of the member's death, the details at (a) and (d) are not required but the certificate should instead give details of:

(h) the amount of the aggregate lump sum benefit (excluding refunds of contributions) payable from all approved or relevant statutory schemes of the employer or to which the employer has contributed, and

(i) the maximum amount under the rules of the employer's scheme of the lump sum benefit (excluding refunds of contributions) payable from all schemes providing benefits in respect of service with the employer.

At the same time as any certificate is given, each of the Free standing Additional Voluntary Contribution Schemes described at (f) should be notified that a relevant date has occurred and of the identity of the leading scheme.

The maxima under (d), (e) and (i) above may be calculated by reference to whichever of the following measures of final remuneration is chosen by the administrator of the employer's scheme:

(i) the measure of annual remuneration on which the benefits of the employer's scheme are calculated, or

(ii) the greatest measure of final remuneration permitted by the Inland Revenue, or

(iii) the average (subject, where appropriate, to the permitted maximum) of the annual remuneration from the relevant employment of the last three years of assessment from which tax was deducted under the PAYE system.

For the purpose of calculating maximum benefits on early retirement or on leaving pensionable service, benefits secured by the Additional Voluntary Contribution funds are not to be treated as money-purchase benefits. (The preservation legislation specifically allows any surplus Additional Voluntary Contribution element of the short service benefit to be repaid.)

Calculation of surplus

16.30 The leading scheme is responsible for obtaining details of the benefits under all Free standing Additional Voluntary Contribution Schemes and for calculating any surplus benefits in respect of the relevant types of benefit (e.g. member's pension, spouse's or civil partner's pension or lump sum death benefits as appropriate) payable out of the member's Additional Voluntary Contribution funds. There is no objection to a provision allowing members an option to change the form of the Additional Voluntary Contribution benefits payable. Such an option must be exercised before any surplus is repaid as it may necessitate re-calculation of the surplus. Surplus benefits are calculated using the formula A - B where:

A is the initial pension (as described in (a) or (b) of paragraph 16.29) or lump sum (as in (h) of paragraph 16.29) payable or prospectively payable in respect of service with
the employer (i.e. including any from Additional Voluntary Contribution schemes whether of the employer or Free standing), and

B is the maximum amount of the relevant form of benefit that may be paid under the rules of the employer's main scheme.

16.31 Where schemes provide separate pension and lump sum retirement benefits the references to pension before commutation are to be construed as the aggregate of the pension and the pension equivalent (see paragraphs 7.2 and 7.57) of the separate lump sum. Having calculated the surplus benefits it becomes possible to calculate the surplus Additional Voluntary Contributions which may be refunded to the member. The amount refundable is the lesser of:

(a) the value of the surplus benefits, and

(b) the accumulated value of the member's Additional Voluntary Contributions.

It is the duty of the leading scheme (having consulted the member) to instruct the various schemes involved as to what benefits are to be paid and the amount of the benefits, the value of which is to be refunded.

16.32 Where benefits are not payable at or from the relevant date, the surplus benefits may be calculated by reference to a current valuation of those benefits without making assumptions as to revaluation in the period of deferment. Money-purchase benefits may be valued as the amount of benefit which can be secured at the relevant date. Administrators may use more sophisticated valuations if they wish.

16.33 The authority of the leading scheme to control the payment of Additional Voluntary Contributions benefits and repayments of surplus flows from the provisions of the Regulations which preclude any such payment or repayment of Free standing Additional Voluntary Contribution Scheme benefits or funds without the authority of the leading scheme. The actual arrangements for the necessary exchange of information, determination of the member's wishes and the consequent authorities are not prescribed though the pensions industry operates under a voluntary code of practice.

16.34 Administrators of schemes have a duty to report repayments of surplus Additional Voluntary Contributions to the Inland Revenue under the Information Powers Regulations (see paragraph 16.6).

Retained Benefits

16.35 In addition to the specific duties placed on the administrator by tax legislation there is a general duty to administer the scheme in accordance with the terms of its trust deed and rules; approval is conditional upon the provisions included in those terms being complied with. Thus, amongst other things, the administrator has a duty to ensure that Inland Revenue limits on benefits are properly applied. Failure to comply with the terms of the trust deed and rules can result in the scheme's approval being withdrawn (see paragraph 19.2).

16.36 Paragraphs 7.4, 7.40 - 7.42, 7.47, 8.25, 8.28, 8.32, 8.37, 10.9, 10.10, and 10.17 all require benefits to be limited by reference to retained benefits. retained benefits may thus need to be valued:

(a) when a member's entitlement under the scheme is first determined on entry,

(b) if a member's entitlement is revised, and

(c) when a member's benefits crystallise on leaving pensionable service, or when they
become payable (subject to paragraphs 16.40 and 16.49 as appropriate).

In addition retained benefits may have to be valued at the date of assessment when determining the maximum funding rate permissible for fully insured money purchase schemes (see Appendix VIII paragraph 6A) and small self-administered schemes (see Appendix IX paragraph 7A).

16.37 The valuation of a Retained Benefit may not be straightforward if it comes into payment other than at the date that benefit entitlement vests under the current employer's scheme. The following paragraphs give guidance on acceptable methods of valuation and the circumstances in which a subsequent revision of that valuation will be necessary.

Benefits paid or in payment

16.38 Pensions already in payment, although they have an enhanced value by reason of earlier payment, may nevertheless be taken at their current amount (but see paragraph 16.44 if subject to revaluation). Similarly lump sum benefits already paid are taken at their actual amount and their pension equivalents calculated as if received (or to be received) concurrently with scheme benefits.

Benefits in payment under income drawdown (Personal Pension/Occupational Money Purchase Schemes)

16.39 It may be necessary to take into account as a Retained Benefit, a pension already in payment under a drawdown facility. Such a pension may arise from a personal pension scheme, an occupational money purchase scheme or a buy-out contract. In these circumstances the pension should be valued for Retained Benefit purposes

- where the pension is being paid from a Personal Pension Scheme, on the basis of the maximum amount which is currently capable of being withdrawn i.e. the 100% amount determined by the GAD Tables
- where the pension is an employer funded benefit being paid from an approved scheme or a buy-out contract, on the basis of the maximum amount which is currently capable of being withdrawn (see Part I of Appendix XII)
- where the pension is being paid from an AVC fund, on the basis of the pension equivalent determined when benefits from the employer first become due and payable (see Part III of Appendix XII).

Deferred benefits

16.40 Pensions which will not come into payment until after normal retirement date or the actual date of retirement or leaving pensionable service under the current employer's scheme should be taken into account on the basis of their actuarial equivalent (viz. the actual amount of benefit that could be secured or provided) at that date or, alternatively, brought into account once they begin to be paid. The latter alternative is not available to a member with pre 1 June 1989 continued rights or a member not entitled to continued rights whose lump sum retirement benefit is calculated by reference to the scheme pension payable (see paragraphs 8.7 and 8.28). Where the former basis is applied, the value of the Retained Benefit is:

a) where the valuation is at normal retirement date, the amount of pension benefit that could be secured or provided at that date,

b) where the valuation is occasioned by the member retiring or leaving pensionable service before normal retirement date, the actuarial amount of pension benefit that could be secured or provided at the date of early retirement or leaving pensionable service as the case may be.

In assessing the annuity equivalent of the Retained Benefit in a) and b) above the calculations should assume that the retained benefits will take the same form as the benefits payable under the current employer's scheme in terms of own right spouses'/civil partners'/dependants pension, post-retirement increases, guarantees etc.

16.41 Where the Retained Benefit is the benefit that can be purchased from a cash fund (as in paragraph 16.46), the amount that could be secured or provided at the relevant date under the
current employer's scheme in a) or b) of paragraph 16.40 above is calculated by applying an appropriate deferred annuity rate to the fund. In the case of a member retiring before normal retirement date, appropriate deferred annuity rate means the amount of pension the cash fund would buy at the date of early retirement, assuming that the retained benefits will take the same form as the benefits being provided under the current employer's scheme as explained above. In the case of a member leaving pensionable service before normal retirement date in circumstances not giving rise to the immediate payment of relevant benefits, appropriate deferred annuity rate means the amount of pension the cash fund would buy at the date of leaving pensionable service, again assuming the retained benefits will take the same form as the benefits being provided under the current employer's scheme, but taking account of revaluation during the period of deferment.

**Example**

16.41a Data:

- Member leaves pensionable service of current employer at age 50 - normal retirement date 65.
- Value of Retained Benefit cash fund at age 50 = £10,000.
- Retained Benefit subject to revaluation at fixed 5% pa during deferment.

**Calculation:**

The annuity value of the Retained Benefit at age 65 is, say, 11.62.

Allowing for increases at 5% pa for 15 years and discounting at 8\(\frac{1}{2}\)% pa, the deferred annuity factor at age 50 is 7.11. Therefore, the Retained Benefit should be taken as a pension of £1,406 (£10,000 \(\div\) 7.11).

16.42 Where in the case of a member leaving pensionable service before normal retirement date and not taking immediate benefits, the current employer's scheme is a money purchase scheme offering the member a choice at maturity as to the form of benefits, the principle in paragraph 16.48 should be followed.

16.43 Lump sums which will not come into payment until after the date on which a member's entitlement vests under the current employer's scheme may be appropriately discounted in valuing them as retained benefits for the purpose of any necessary restriction of the lump sum payable from the current employer's scheme.

**Benefits subject to revaluation**

16.44 A Retained Benefit may be subject to a provision for increase by reference to the rise in the cost of living, either fully or up to some stated percentage, during the period before benefit entitlement vests under the current employer's scheme.

Increases for the period before the valuation date should be taken into account or valued on the basis of the appropriate scheme rules subject to the requirements of the relevant Department of Social Security pensions legislation. Notional increases should also be taken into account - in some schemes cost of living increases do not come into payment before age 55. Future increases should be assumed at 5% per annum compound or by reference to the stated percentage if less.

A pension subject to automatic increases at a fixed rate regardless of the rise in the cost of living should be valued by reference to that fixed rate.

**Benefits under with profits policies**

16.45 A benefit may be secured by a with-profits or investment-linked insurance policy which will continue to increase in value during deferment. Its value as a Retained Benefit should be calculated on the assumption of a reasonable return (consistent with current and future expectations) on the paid-up value. The Inland Revenue consider that it is reasonable to assume that the policy value for both types of contract will increase at not less than 9% per annum unless
the maturity date is less than 5 years ahead. In that circumstance it should be valued by reference to the current bonus rate or an estimate more closely aligned to yields currently obtainable.

16.46 Where benefits are expressed in terms of a lump sum to be applied on maturity to secure the benefits payable the value of those benefits should be calculated in two stages. The emerging lump sum should first be estimated on the basis set out in paragraph 16.45. An appropriate annuity rate should then be used to convert that figure into its annuity equivalent. The annuity rate should take account of the employee's normal retirement age under the current employer's scheme and the funding assumptions set out in paragraph 13.11(ii),(iii) and (iv). If the calculation is being made at, or shortly before, the annuity commencement date, the life office's current annuity rates should be used.

16.47 The value of a Retained Benefit in the form of a paid-up retirement annuity contract, or under a personal pension scheme should be taken as the notional value of the annuity assuming it will come into payment at the normal retirement date under the current employer's scheme. The same assumptions and annuity rates should be used as under paragraphs 16.45 and 16.46. Where such a Retained Benefit comes into payment either before or after the vesting date (as defined in paragraph 16.36) under the current employer's scheme, paragraphs 16.38 and 16.40 apply as appropriate.

16.48 Some retained benefits, such as those under some buy-out policies or personal pension schemes, offer a choice at maturity as to the form (within certain parameters) of the emerging benefits. In such cases the scheme should take a conservative view (i.e. in order to avoid overfunding, assume that the member will opt for the maximum permissible personal pension) as to what options the member will select at retirement. The basis explained in this paragraph should be used by all schemes irrespective of their date of exempt approval in respect of members joining after 31 July 1994.

16.49 A Retained Benefit valued on entry to the scheme will not be required to be revalued unless:

(a) further improvements are made to the member's prospective benefits from the current employer's scheme;

(b) the deferred pension (not being one from the Armed Forces Pension Scheme) qualifies for a full cost of living increase and exceeded £10,000 per annum at the time the new arrangement was set up. In this case its current value should be taken into account at retirement (or normal retirement date, if earlier, for a member with continued rights); or

(c) the member exercises an option which produces larger initial benefits than had been assumed under paragraph 16.48 above.

16.50 Benefits from the Armed Forces Pension Scheme do not fall within the general pattern of occupational pension scheme benefits and the terms used to describe the benefits require some explanation:

Retired pay (officers) or long service pension (other ranks) An immediate pension payable on retirement from the Armed Forces. It is fully index linked except that increases accruing before age 55 are notional only and do not become payable until that age is reached.

Deferred pension A preserved pension payable from age 60 for personnel not entitled to retired pay. This pension is also fully index linked (notionally before coming into payment).

Life commutation Commutation of part of the original pension award either in one go or piecemeal.
Resettlement commutation  A temporary commutation available to personnel who are under age 55 when they retire. The retired pay surrendered is restored from age 55. It should not be confused with a Resettlement Grant which is not a Relevant Benefit.

Terminal grant  This is a separate lump sum payment of three times the amount of the retired pay or deferred pension, calculated and paid when that pension comes into payment. Because deferred pension is index linked a deferred terminal grant automatically includes cost of living increases. retained benefits from this source should be quantified in accordance with the chart set out in paragraph 16.51.
### Armed Forces Benefits

16.51

<table>
<thead>
<tr>
<th>RETAINED BENEFITS (PENSION)</th>
<th>PENSION IN PAYMENT MEMBER OVER 55</th>
<th>PENSION IN PAYMENT MEMBER UNDER 55</th>
<th>PENSION IN DEFERMENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>RETIRED PAY (OFFICERS)</td>
<td>Pension in payment (includes cost of living to date) Add 5% pa to new NRD</td>
<td>Pension in payment (Cost of living not yet included) Add notional cost of living to date Then add 5% pa to new NRD</td>
<td>Pension in deferment. Add notional cost of living to date. Then add 5% pa to new NRD.</td>
</tr>
<tr>
<td>LONG SERVICE PENSION (OTHER RANKS)</td>
<td>Nothing (Added back to pension at age 55)</td>
<td>Add back actual amount of surrendered retired pay to pension in payment Add notional cost of living to date Then add 5% pa to new NRD</td>
<td>-</td>
</tr>
<tr>
<td>RESETTLEMENT COMMUTATION</td>
<td>Immediate life annuity value at new NRA of the actual amount, using rates prevailing at time of joining new scheme</td>
<td>Immediate life annuity value at new NRA of the actual amount, using rates prevailing at time of joining new scheme</td>
<td>-</td>
</tr>
<tr>
<td>LIFE COMMUTATION</td>
<td>-do-</td>
<td>-do-</td>
<td>Immediate life annuity value at new NRA of the actual amount, using rates prevailing at time of joining new scheme</td>
</tr>
<tr>
<td>TERMINAL GRANT</td>
<td>Resettlement Commutation, Life Commutation, Terminal Grant</td>
<td>Actual amount of all lump sums received</td>
<td>Actual amount of all lump sums received</td>
</tr>
</tbody>
</table>

16.52 Guidance is often sought as to whether retained benefits from earlier employments/occupations should be apportioned when later employments are concurrent.

16.53 When calculating benefits from concurrent employments the treatment of retained benefits from earlier employments or occupations will vary depending on whether or not the employments are associated or the relevant schemes are connected. Where the employments are not associated and the schemes are not connected any such retained benefits should be apportioned by reference to the initial remuneration where the concurrent employments commence.
simultaneously and each amount treated as a separate Retained Benefit. Where the concurrent employments do not commence simultaneously, the retained benefits should either be set fully against the earliest employment and ignored for subsequent employments, or be set fully against the earliest employment and then re-apportioned (on a remuneration basis) when the subsequent employments commence.

16.54 Where the concurrent employments are associated or the schemes are connected, the Retained Benefit in full is set against benefits from the employment which vests first and any unexhausted balance (see paragraph 16.55) is set against the benefits from the other employments successively as they vest. If all the benefits vest together the same principle applies but the sequence is immaterial. In this context the vesting date is defined in paragraph 16.36.

16.55 For the purposes of paragraph 16.54 the unexhausted balance of a Retained Benefit is that proportion which has not reduced benefits on a previous vesting. It is calculated by deducting from the total Retained Benefit the difference between the maximum approvable benefit before taking account of the Retained Benefit and the maximum approvable benefit thereafter. In this context the maximum approvable benefit is calculated in accordance with the relevant paragraph in Part 7 subject always to paragraph 7.3 as qualified by paragraphs 7.10 and 7.42. Where benefits vest at different dates retained benefits will be revalued and at a subsequent vesting date the unexhausted balance will be the same proportion of the revalued benefit.

Example (this forms part of Example No 2 at paragraph 7.26)

Data                                      Service 15 years

final remuneration  £50,000
Retained Benefit  £20,000

At first vesting date

A  Maximum approvable pension  not taking account of retained benefits  15/30 x £50,000  = £25,000

B  Maximum approvable pension  taking account of retained benefits The lesser of A and £33,333 (2/3 x final remuneration - £20,000  = £13,333

A – B  = £11,667

Unexhausted balance £20,000 - £11,667 = £8,333

At second vesting date  Retained Benefit has been revalued at £24,000

Unexhausted balance is (£8,333 x £24,000)/£20,000 = £10,000

16.55a From 5 April 2006 as an alternative to the valuation guidance in paragraphs 16.38 to 16.55 retained benefits may be valued as follows:

For pension rights which have not come into payment on 5th April 2006:

- if the pension rights are money purchase rights other than cash balance rights the amount of the annual pension will be the value of the sums plus the market value of the assets held on 5 April 2006 to provide the individual’s benefits where that value is divided either by 20 or by an annuity rate calculated from the GAD Tables as at 5 April 2006. Administrators are free to choose which divisor should apply. Market value
should be determined in accordance with section 272 of Taxation of Chargeable Gains Act 1992.

- if the pension rights are cash balance rights the amount of the annual pension will be the value of the capital available at normal retirement date for the scheme holding the retained benefit divided either by 20 or by an annuity rate calculated from the GAD Tables as at 5 April 2006. Administrators are free to choose which divisor should apply. The amount of capital available may be reduced to take account of notional immediate payment on 5 April 2006 in accordance with the provisions of the scheme holding the retained benefit.

- if the pension rights are defined benefit rights the amount of the annual pension will be the amount of annual pension available at normal retirement date for the scheme holding the retained benefit. The amount of annual pension available may be reduced to take account of notional immediate payment on 5 April 2006 in accordance with the provisions of the scheme holding the retained benefit.

- if the pension rights are hybrid rights the amount of the annual pension will be the higher or highest value for annual pension for the alternate rights available under the hybrid promise.

- money purchase, cash balance, defined benefit and hybrid are as defined in section 152 of Finance Act 2004.

For lump sum rights which have not come into payment on 5th April 2006 where those rights will not be payable as a consequence of commuting pension rights;

- the amount of the annual pension attributable to the lump sum rights will be the value of the lump sum available at normal retirement date for the scheme holding the retained benefit divided either by 20 or by an annuity rate calculated from the GAD Tables as at 5 April 2006. Administrators are free to choose which divisor should apply. The amount of lump sum available may be reduced to take account of notional immediate payment on 5 April 2006 in accordance with the provisions of the scheme holding the retained benefit.

For pension rights already in payment on 5th April 2006;

- the annual amount of pension in payment on 5th April 2006 or the annual amount of the pension when it first came into payment. Where the pension is being paid under drawdown or income withdrawal the amount of the pension must be valued as the maximum amount annual pension that could have been paid on 5 April 2006.

For lump sums paid on or before 5th April 2006;

- the amount of the annual pension attributable to the lump sums paid will be the amount of the lump sums paid divided either by 20 or by an annuity rate calculated from the GAD Tables as at 5 April 2006. Administrators are free to choose which divisor should apply.

For pre 17 March 1987 members who have lump sum retained benefits;
where the lump sum has not come into payment on 5 April 2006 the value of the retained benefit will be the value of the lump sum that could be paid immediately on 5 April 2006 on the basis that the member is assumed to be aged 50 if he/she has not attained that age on that date

• where the lump sum has been paid on or before 5 April 2006 the value is the amount paid as a lump sum benefit.

Pension Debits

16.56 As well as the necessity to limit benefits by reference to retained benefits, it is also necessary, where a member’s benefits are subject to a pension sharing order made by the courts and the administrative easement described in paragraph 7.7 does not apply, to limit benefits by reference to the pension debit. Pension debits may thus need to be valued:

(a) at the date of assessment when determining the maximum funding rate permissible for fully insured money purchase schemes (see Appendix VIII paragraph a8a.4.5) and small self-administered schemes (see Appendix IX paragraph A9.7),

(b) when a member’s benefits crystallize on leaving pensionable service, or when they become payable. Appendix XIII gives guidance on the calculation of pension debits in these circumstances.

Compliance Monitoring

16.57 As part of the Inland Revenue’s long-term strategy to use its resources more for selective compliance checking than on routine processing, IR SPSS operates a compliance audit system. Its purpose is to check that retirement benefits schemes, once approved, are actually being administered in accordance with their rules and Inland Revenue approval requirements as to benefit limits etc.

16.58 This comprises two main parts:

(a) selective in-depth examination of schemes by the General Examination Sections. Schemes are selected mainly by the application of risk criteria, with a smaller number being selected randomly to ensure a broader coverage; and

(b) inspection visits and other special targeted exercises (e.g. post retirement benefit checks) carried out by the Compliance Audit Section.

16.59 The inspection visits are carried out under the powers contained in regulation 14 of the Information Powers Regulations. (See paragraph 1.10). These require a minimum notice of 28 days.

16.60 The various desk-based compliance checks are carried out by normal correspondence, with the power to issue formal notices (regulation 12 of the Information Powers Regulations) in reserve for use whenever necessary.

Insured Schemes: Loans to Employers (Made on or After 1-12-'99)

16.61 Government policy on self-investment (i.e. the investment of pension scheme funds in the employer's business) does not preclude the use of certain pension scheme policies as security for a loan to the employer (or to any Associated Employer whether or not they participate in the scheme) for a genuine business purpose. Only policies (or such part thereof) taken out solely to secure benefits for a controlling director are suitable for this purpose and the conditions on which the loan is made must satisfy a number of Inland Revenue requirements.

16.62 The PS 8 certificate (a specimen of which is included in Appendix II) is designed to enable
IR SPSS to dispense with the need to examine documentation relating to the loan and to concentrate on monitoring the circumstances and the use of the loan itself. There is generally no requirement to provide IR SPSS with any related documentation but IR SPSS reserves the right to call for documentation in particular cases. If IR SPSS is satisfied with the circumstances of the loan a simple acknowledgement will be issued within 4 weeks of the receipt of the notification. Otherwise the trustees and the life office will be asked for more information or instructed to obtain immediate repayment of the loan.

Facility not to be abused

16.63 The facility of obtaining loans by using pension scheme policies as security must not be operated in such a way as to call into question the sole purpose requirement of section 590(2)(a). A succession of regular loans to bring the total loan outstanding to the maximum permitted might suggest that the employer is using the facility to only partly fund the scheme while claiming a tax deduction for the total pension contributions (see also paragraph 20.57). If such a succession is not to prejudice the approval of the scheme it should be for a genuine commercial reason and not normally extend beyond 2 years.

Conditions to be Satisfied For a Loan to be Acceptable

Loans must be commercial - what is a commercial loan?

16.64 The basic underlying principle is that the loan to the employer (or Associated Employer) should be made on commercial terms. In order to satisfy this basic principle the loan must:-

(a) be at a commercial rate of interest (i.e. at least Clearing Bank Base Rate + 3% will normally be accepted. See also paragraph 16.65 below)

(b) have a duration commensurate with the purpose of the loan (see paragraphs 16.66 and 16.67 below)

(c) be used for the purposes of the borrower's trading activities (see paragraph 16.68 below)

(d) not be made to companies in financial difficulties (see Update No 43 and paragraph 16.69 below)

(e) be secured against a policy (or part thereof) that is specifically and solely for the provision of benefits for a member who is a controlling director of the borrower and who has consented to the policy (or part thereof) being used as security for the loan, and

(f) not exceed 50% of the current value of the policy or policies used to secure the loan (if the lending takes place within 2 years of the establishment of the scheme the amount shall not exceed 25% of the current value of the policy excluding the value of any transfer values received and included therein).

Interest rate less than CBBR+3%

16.65 Where the rate of interest is less than 3% above the current base rate of a particular clearing bank (see paragraph 1(c) of the certificate) written evidence will be required to show that the borrower can obtain a loan on similar terms from an arms-length financial institution.

Duration of loan - maximum

16.66 The maximum duration for such loans is a period expiring 1 year before the normal retirement date of the member whose policy (or part thereof) is used as security for the loan.

Normal

(a) This is, however, the maximum period for which the loan can be made and will be acceptable only in exceptional circumstances. Normally the duration of such loans would not be expected to be more than 3 to 5 years. For some purposes, e.g. the purchase of stock in trade, a duration of 1 year or less may be more appropriate.

IR SPSS may object to duration

(b) Where the duration of the loan appears to be unusually long in the light of its stated
purpose, *IR SPSS* may make enquiries and if appropriate insist that the duration of the loan be reduced to a more realistic period.

- **Level capital repayments**

(c) The duration of the loan will not be permitted to exceed 2 years unless the terms of the loan provide for level capital repayments throughout the loan period with capital repayments being made at least every 6 months.

- **Amendment to loan agreement**

16.67 If the life office and the borrower wish to amend the terms of the loan then fresh documentation and a PS 8 certificate will be required. *IR SPSS* may require the loan to be immediately repaid unless the amendment is for acceptable commercial reasons. If the duration of the loan is to be extended, *IR SPSS* will normally expect the loan agreement to require regular repayments of capital throughout the duration of the loan as well as interest payments. It is unlikely that *IR SPSS* will accept more than two amendments to the terms of the loan.

- **Restriction on purpose of loan**

16.68 The employer (or *Associated Employer*) may not lend the money on to someone else nor use it for some purely speculative purpose such as the purchase of shares or other investment. It may, however, be acceptable in some circumstances for a holding company to use such monies to make or manage share investments in its 50% trading subsidiaries.

- **Credit check required**

16.69 Before the trustees of the scheme grant security for the loan, a credit check on the borrower must be undertaken and the results disclosed to *IR SPSS* when the PS 8 is submitted. There is no requirement for the credit check to take any particular form. However, the credit check should be undertaken no more than 4 weeks before the loan is made. If the credit check does not provide a rating and a financial strength indicator then it should include at least three or more years of analysed accounts (or from when the company commenced trading), the date of the latest accounts and returns filed, details of any County Court Judgements and mentions in Legal Gazette. Although there is no requirement for the credit check to include any form of rating, the inclusion of such a rating would be preferred and would significantly reduce the probability of *IR SPSS* making any further enquiries regarding the loan or requiring the loan to be repaid.

- **Injudicious loans**

(a) If *IR SPSS* do not consider the granting of security to be a judicious act by the trustees *IR SPSS* may require the loan to be repaid. Clearly any loan made to an ailing or insolvent company will not be acceptable.

(b) *IR SPSS* will take into consideration any other information that the trustees of the scheme wish to attach to the PS 8 in support of their decision to grant security for the loan, e.g. copies of the latest company accounts, cash flow projections etc.

- **Information provided by trustees**

(c) If the trustees wish to have certainty that *IR SPSS* is satisfied that a loan was not injudicious then the trustees should ensure that all facts material to the financial health of the borrower are disclosed.

- **Certainty**

(d) The level of risk considered acceptable will depend on several factors including the financial health of the company, the duration of the loan and whether the terms of the loan provide for ongoing capital repayments throughout the period of the loan.

- **Acceptable level of risk**

(e) If there is insufficient information provided by the credit check and the trustees to determine that a loan is judicious then *IR SPSS* will require the loan to be repaid unless the trustees can justify the granting of the security.

- **Injudicious loan can lead to loss of approval**

16.70 The PS 8 has been amended to carry a warning that the making of an injudicious loan or the
securing of an injudicious loan on scheme policies or failure otherwise to comply with IR SPSS requirements may lead to the loss of approval of the scheme (see Part 19).

16.71 Loss of approval of the scheme will give rise to a tax charge under section 591C ICTA 1988 of 40% of the scheme assets (see paragraph 19.5).

Other significant tax consequences as set out in Part 19 will also apply.

16.72 No further loans may be made to an employer (or Associated Employer) secured on scheme policies whilst interest and/or capital is in arrears on an existing loan made to that employer or to an Associated Employer secured on scheme policies. This prohibition extends to loans from any other schemes of the borrower whether or not there are any arrears in respect of loans made by these schemes.

16.73 A loan agreement should not include a provision for future topping up. If an additional loan is necessary, it must be the subject of separate documentation and a separate certificate.

16.74 In some cases the growth in value of the policy used to secure the loan is linked to the interest paid on the loan. Where there is any link between the loanback and the policy returns the interest payable on the loanback may not be waived nor the rate of interest reduced. It is only permissible to waive the interest or to reduce the rate of interest payable in circumstances where this will not have any effect on the scheme policies or on the growth in value of those policies.

16.75 Any reduction of benefits as a result of foreclosure will be first effected against any lump sum retirement benefits payable.

The restriction on the director’s lump sum retirement benefits will be lifted to the extent of the amounts recovered by the scheme trustee(s) under the rights acquired as a result of foreclosure.

16.76 Where interest is not paid by the borrower on the due and payable dates, any payments to life offices intended as repayments of interest or capital will be set off first against current and outstanding interest with any balance then being set off against capital.

PS 8 Certificate

16.77 The certificate PS 8 on which loans to employers (or associated employers) are reported must be sent to IR SPSS (within 90 days of the making of the loan) and requires the following information:-

(a) the identity of the borrower
(b) the results of the credit check (see paragraph 16.69 above) attached to the PS 8 together with any other information that the trustees may wish IR SPSS to take into account when considering whether or not the granting of security by the trustees was a judicious act
(c) certification that the policies used to secure the loan are for controlling directors only
(d) certification of the purpose for which the loan is sought
(e) the duration of the loan
(f) the rate of interest chargeable on the loan and the details of when the interest becomes due and payable.
In addition, the PS 8 and certifications should be signed by both the employer (or Associated Employer) and the trustees of the scheme. It is not acceptable for anyone to sign the PS 8 on behalf of the trustees and/or the employer.

If the employer is also the trustee, then this may require the employer to sign twice in two separate capacities.

**Consequences of Foreclosure**

16.78 Where a life office has recourse to security given by the pension scheme trustees, the trustees acquire, under general law, the right to the original debt. This means that after foreclosure there will be a right of action by the trustees against the employer.

16.79 Where

(a) the granting of security by the scheme trustee(s) was judicious, and

(b) repayment of the original debt has become impossible, (e.g. where the employer is in liquidation and the liquidator has indicated that there will be no dividend payable to the scheme), and

(c) **IR SPSS** is satisfied that the situation has arisen because of genuine commercial reasons,

the approval of the scheme will not be withdrawn provided that there are no other facts concerning the scheme or its administration that warrant withdrawal of approval.

16.80 Any rights accruing to the scheme as a result of foreclosure in the above circumstances will have no value and can be waived without giving rise to a tax charge under section 601 ICTA 1988 (see paragraph 17.38). In these circumstances, the scheme will not become a self-administered scheme.

16.81 Any reduction of benefits as a result of foreclosure will be first effected against any lump sum retirement benefits payable.

16.82 Where the granting of security by the trustee(s) was judicious but foreclosure takes place even though the employer is capable of repaying the original debt either at the date of foreclosure or at some future date, e.g. where the employer is continuing to trade or hold assets following foreclosure, the rights acquired by the trustee(s) as a result of foreclosure have value. In this situation, the waiving of those rights will be a transfer of value to the employer. This will have tax consequences under section 601 ICTA 1988 and will also be grounds for the withdrawal of the approval of the scheme.

16.83 The approval of the scheme will not, however, be withdrawn where the granting of security by the trustees was judicious and, following foreclosure, the rights acquired by the trustees have value, provided that **IR SPSS** is satisfied that there are no other facts concerning the scheme or its administration that warrant the withdrawal of approval and the trustees have:

(a) immediately enforced their rights against the employer, or

(b) have reached a commercial arrangement whereby the outstanding capital, together with the outstanding interest, will be paid to the scheme trustees within a reasonable period of time.
Continuation of approval will be conditional on the commercial arrangement agreed with IR SPSS being adhered to.

- Scheme may become a SSAS

16.84 Where acceptable arrangements are made the scheme will be holding an asset which is not an insurance policy. Whether or not this is an investment will be a question of fact and the scheme may have become a self-administered scheme as a result. An approved scheme which becomes a small self-administered scheme must comply with the requirements of the "SSAS Regulations" as subsequently amended as at the time it becomes such a scheme and thereafter (see paragraph 20.1).

- Restriction on benefits and how to avoid it

16.85 The reduction of the controlling directors benefits will be lifted to the extent of the amounts recovered by the scheme trustees from the employer under the rights acquired as a result of foreclosure. To avoid a restriction to the lump sum retirement benefits the amounts must be recovered before the lump sum retirement benefits are paid.

- Injudicious loan leads to loss of approval

16.86 Where the granting of the security by the trustees was injudicious approval of the scheme will normally be withdrawn. The repayment of the loan and all interest due can usually prevent the loss of approval in these circumstances. Where foreclosure takes place even though the employer is capable of repaying the original debt, a tax charge under section 601 ICTA 1988 will also arise if the acquired rights are waived or not enforced.

- How to avoid loss of approval

16.87 Where the granting of security was approved by IR SPSS then the withdrawal of approval of the scheme on the grounds that the loan was injudicious can only take place if IR SPSS demonstrates that:

(a) there was information available to the trustees relevant to the financial state of the company at the time the loan was made, which was not disclosed to IR SPSS with the PS 8 certificate, and which would have affected the decision made by IR SPSS, or

(b) the information provided to IR SPSS was incorrect or misleading.

Notifications Required

- IR SPSS must be notified of all loans made

16.88 IR SPSS must be notified of all such loans within 90 days by means of a completed certificate (PS 8) that the loan and the scheme documentation meet the necessary requirements. The certificate details all the requirements which need to be certified and all the undertakings required. Customers are free to photocopy the certificate for use but must submit them to IR SPSS on the same coloured paper as the official form as indicated on the Appendix II specimen. Customers on our bulk forms users database will be supplied immediately with copies of the new certificate. Any customer who wants to obtain copies of the new certificate should ring IR SPSS Supplies Line on 0115 974 1670.

- Notify IR SPSS of foreclosure

16.89 The lender must notify IR SPSS whenever foreclosure on a scheme policy takes place within 30 days of the event in question.

- Notify IR SPSS if interest is outstanding

16.90 If interest or capital is outstanding 90 days after the due date for payment then the life office should report this to IR SPSS within a further 30 days.

- Notify amendment

16.91 If an existing loan agreement is amended, a new PS 8 certificate should be submitted to IR SPSS within 90 days of the amendment.
16.92 If the payment of regular contributions under the scheme for the controlling director whose policy (or part thereof) is being used as security for the loan ceases, IR SPSS must be notified by the life office within 90 days of such cessation. If the life office is aware of the reason for cessation of contributions this information should be included with the notification.

Self-Managed Funds

16.93 Where an insured earmarked scheme uses a policy linked to an investment fund (usually held in the name of the insurers) exclusive to that scheme, such investment funds are regarded as self-managed funds and IR SPSS will, under their discretionary powers (section 591(1) ICTA 1998), require as a condition of continued approval that fund to comply with Regulations 4 to 8 of the “SSAS Regulations” as subsequently amended (see paragraph 20.1) despite the fact that the scheme is not strictly a small self-administered scheme. Such self-managed funds should therefore be managed in accordance with those Regulations and paragraphs 20.45 to 20.82 are pertinent to them. This requirement does not, however, apply to investments made before 31 December 1992.

Rebated and Shared Insurance Commission

16.94 Financial advisers or other intermediaries sometimes pass on to their clients part of the commission they receive from insurers on the introduction of new business relating to approved schemes. Any such commission or reward on annuity purchase, transfer of funds or new investment of existing funds of an approved scheme should not be paid to any person other than to a person in their capacity as the administrator/trustee of the scheme concerned. The IR SPSS would regard any payment to an employee or employer as a non-relevant benefit from the scheme that is inconsistent with the scheme’s sole purpose of providing relevant benefits (see paragraph 1.4).

16.95 Similarly, the misrepresentation as an annual premium of any premium applied to new pensions business, so that a higher rate of (rebated) commission is generated, will call into question the bona fides of an approved scheme and jeopardise its approval from inception.

16.96 Additional tax charges could also arise on the recipient of the unauthorised benefit under Section 596A, 600 or 601 as appropriate.
Part 17. Tax Treatment of Approved Schemes

**Taxation of Pensions**

17.1 All pensions paid under any scheme (including any amounts paid under income drawdown – see Appendix XII) which is approved or being considered for approval under Chapter I Part XIV are chargeable to tax under Schedule E and PAYE is to be operated (section 597(1)). This applies whoever pays the pension, whether it be the employer, the administrator or a life office from which an annuity under the scheme has been purchased. The person paying the pension is responsible for applying PAYE and accounting for the tax to the Inland Revenue. Where an annuity has been purchased from an EC insurance company falling within section 659B, that company must appoint an individual resident in the United Kingdom (or a non-individual with a place of business in the UK) to be responsible for applying PAYE to the annuity, or come to some other arrangement with the Inland Revenue.

17.2 A scheme is "being considered for approval" from the time when an application for approval is made under section 604 until it is finally approved, the application is withdrawn or refused, or it appears to IR SpS to have been abandoned (see paragraph 14.14) and the applicant has been notified accordingly.

17.3 Annuities paid by a life office to the administrator of a scheme who in turn pays the pensions are not pensions and section 597(1) does not apply. In strictness the life office should deduct basic rate tax under section 349 but, where the administrator is obliged by virtue of section 597(1) to apply PAYE to the pension, there is no objection to the annuity being paid to the administrator without deduction of tax.

17.4 The Taxes Act provides no general exemption from income tax under Schedule E to pensioners resident abroad. The Income Tax (Employments) Regulations 1973 do however preclude the operation of PAYE in respect of a pension arising wholly from an employment carried on abroad and payable to a non-resident. In practice this is extended to apply to pensions where:

(a) the last 10 years' service in respect of which the pension is paid was abroad, or

(b) half the total service in respect of which the pension is paid and at least 10 of the last 20 years' service were both abroad.

17.5 Exemption at source may be available under a Double Taxation Agreement between the United Kingdom and the country of residence. Where there is no exemption, tax relief may be due to British subjects and certain other persons resident abroad under section 278. The Financial Intermediaries and Claims Office authorises exemption at source and deals with applications for tax relief. Where a non-resident pensioner subsequently becomes resident in the United Kingdom, his or her pension will become liable to United Kingdom income tax.

17.6 An approved scheme, the membership of which is restricted to employees serving abroad, may provide for the purchase of pensions from, or payment by, an overseas source. In the case of an individual arrangement this may apply only if the employment of the individual concerned will be wholly abroad and it can be demonstrated that the pensioner is and will remain exempt from tax as a non-resident (see paragraphs 17.4 and 17.5).

**Lump Sum Benefits: Tax Exemption**

17.7 A lump sum benefit payable on retirement or otherwise under an approved scheme is not liable to income tax under Schedule E by virtue of section 189. Liability under section 148 is also excluded by virtue of sub-paragraph 4, Part I, Schedule 9 Finance Act 1998.

17.8 Lump sum death benefits payable under an approved scheme are similarly exempt from liability under section 148 by virtue of sub-paragraph 3, Part I, Schedule 9 Finance Act 1998.
Scheme Investments

17.9 Income from investments, deposits or other property held for the purposes of an approved scheme is exempt from the additional rate tax charge on certain trusts (section 686(2)(c)).

17.10 The following tax exemptions apply to exempt approved schemes:

(a) income derived from investments or deposits held for the purposes of the scheme is exempt from income tax (section 592(2));

(b) income derived from transactions relating to futures contracts and options contracts is exempt from income tax (section 592(2)) by virtue of section 659A (inserted by section 81(2) Finance Act 1990);

(c) underwriting commissions to the extent that they are applied for the purposes of the scheme and would otherwise be chargeable under Case VI of Schedule D are exempt from income tax (section 592(3));

(d) profits or gains arising from transactions in certificates of deposit are exempt from income tax (section 56);

(e) profits from sale and repurchase agreements (repos) and "manufactured payments" are exempt from income tax (SI 1995 No 3036);

(f) a gain arising from the disposal of investments (including (b) above) held for the purposes of the scheme is exempt from capital gains tax (section 271(1)(g) Taxation of Capital Gains Act 1992).

17.11 It should be noted that income from trading by an exempt approved scheme does not fall within the exemption described at paragraph 17.10(a) above as it is not income derived from investments or deposits. But section 659 provides for contracts entered into in the course of dealing in financial futures or traded options to be regarded as investments for the purposes of section 592(2). Stock lending by an exempt approved scheme is regarded as an integral part of investment operations but the fees received under such arrangements are not from "investments or deposits held for the purposes of the scheme". Such fees received by an exempt approved scheme up until 2 January 1996 are assessable to tax under Case VI of Schedule D. Where these fees are received by an exempt approved scheme under approved stock lending arrangements entered into on or after 2 January 1996, they are exempt from tax by virtue of section 157 Finance Act 1996.

17.12 exempt approved schemes or a scheme being considered for exempt approval (provided there is no reason to doubt its eventual approval) may pool their investments in common investment funds without impairing the title of each participating scheme to exemption in respect of those investments, provided that the share of each in the common fund is always identifiable. The hallmark of a common investment fund which distinguishes it from a unit trust is that it should not subject the assets of the participating schemes to any trusts in addition to those which govern those schemes. It is merely an investment agency for the assets of a number of exempt approved schemes of the same employer or associated employers. Where this is the case special arrangements are available for the managers of the fund to submit centralised repayment claims on behalf of all the participating schemes. There is no requirement that all of the assets of a scheme must be included in the common investment fund. Any proposals to set up a common investment fund should be submitted in the first instance to IR SS.

17.13 An exempt approved scheme or, by concession, a scheme being considered for Exempt Approval may be a unit holder in an exempt unit trust. Such a unit trust is exempt from capital gains tax by virtue of section 100 Taxation of Chargeable Gains Act 1992 on the basis that
eligibility to hold units is restricted to bodies which are wholly exempt from capital gains tax or corporation tax. A unit holder who no longer holds that exemption is required to sell its units. Distributions are treated as annual payments for income tax purposes and the appropriate income tax relief must be claimed by the unit holders themselves.

17.14 Once an exempt unit trust has been set up it is necessary for the exemption position of any new unit holder to be confirmed. For this purpose the application form to be completed by the purchaser should show IR SPSS reference number of the scheme and should authorise the Inland Revenue to disclose to the unit trust managers the exemption position. IR SPSS will then advise the manager of the unit trust on application whether or not the intending purchaser has the exempt status appropriate to the status of the trust.

17.15 When an exempt approved scheme applies funds as premiums on an insurance policy it loses its entitlement to exemption under section 592 on the return on those funds because they are no longer the property of the scheme. Chapter I Part XII, however, which deals with the taxation of insurance companies, provides for a similar exemption for income and gains from investments within their "pension business fund". Thus scheme benefits secured by policies which qualify for pension business treatment enjoy tax-free build up comparable with that under section 592.

17.16 To qualify for pension business treatment, policies taken out by an exempt approved scheme must be "so framed that the liabilities undertaken by the insurance company under the contract correspond with liabilities against which the contract is intended to secure the scheme" (section 431B(2)(b)). As this statutory wording implies, it is not necessary for the policy to secure the whole of the scheme's liabilities. Normally the life office will ensure that the correspondence requirement is satisfied by agreeing the terms of the policy in relation to a standard form of scheme rules, with the Standard Documents Section of IR SPSS.

17.17 It is also possible to agree as corresponding, a policy intended as an investment vehicle for any exempt approved scheme, irrespective of the form of its rules. Such a policy needs to satisfy 4 basic requirements, viz.:

(a) it must be in the name of and held by the trustees or administrator of an exempt approved scheme;

(b) it must be a contract to provide scheme benefits rather than just the wherewithal to secure those benefits, i.e. not purely an investment medium for the administration of the scheme's assets by a life office (e.g. deposit administration). It should be clear from the terms of the policy that the underlying assets are owned by the insurer;

(c) if the scheme benefits include annuities, the policy must include provision for the payment of annuities; and

(d) the policy should include an overriding provision to ensure correspondence on the lines of:

"The benefits payable under this policy shall correspond with the liabilities of the grantees under the scheme insofar as these liabilities are or are intended to be, secured by the policy. Any options or provisions in the policy will be exercised only in such a manner and to the extent permitted by the scheme provisions and in the form and at the time permitted by the scheme provisions."

17.18 The correspondence requirements will not be regarded as prejudiced by the inclusion in a policy securing only Additional Voluntary Contribution benefits, of a provision for the policy benefits to be paid to the scheme administrator as a lump sum to secure the payment of additional pension under the scheme in circumstances where:
(a) the policy proceeds are trivial (not more than £2,500), and

(b) some or all of the pension benefits payable to the member in respect of the employment are paid by the administrator out of scheme assets.

17.19 Premiums to a corresponding policy must be referred to pension business so long as the scheme is Exempt Approved but premiums made in advance of approval may also be so referred provided that an application for the scheme's approval has been made. Exceptionally, where a "Hancock" annuity (see paragraph 2.2) is the subject of a direction under section 592(1)(b), the sum paid may remain in the general annuity fund if the life office so decides.

17.20 With effect from 1 July 1994, buy-out policies which provide only those relevant benefits which could be provided directly by a hypothetical approved scheme (see paragraphs 6A.25 and 10.42-10.51), qualify for pension business treatment.

17.21 Contracts to secure immediate benefits under an open market option (see paragraph 6.12) will also qualify for pension business treatment if they correspond. This will normally be the case if they provide an immediate annuity with no option other than for immediate commutation and/or allocation in accordance with the scheme rules.

**Refunds of Contributions**

17.22 Section 598 imposes a charge to tax on the administrator of an exempt approved scheme or a relevant statutory scheme in respect of any refund of a member's contributions during the member's life time. The tax is chargeable at the rate of 20% on the amount paid (inclusive of any interest element) or, if the rules permit or require the administrator to deduct this tax before payment, on the amount before such deduction.

17.23 The charge to tax does not extend to any part of an amount otherwise repayable which is withheld either under a lien rule (see paragraphs 7.32(b) and 17.39(d)) or in respect of a state scheme premium.

17.24 The section 598 charge does not apply where the employee's employment was carried on outside the United Kingdom (section 598(6)). This condition will be regarded as satisfied if the employee worked abroad throughout at least 75% of the period during which he or she was a member of the scheme.

17.25 If a scheme ceases to be an exempt approved scheme the charge continues to apply to subsequent refunds of all contributions made before it ceased to be Exempt Approved (section 598(5)).

17.26 When an employee rejoins a scheme, the rules may permit the provision of benefits in respect of pensionable service lost through taking a refund of contributions (see paragraph 10.52) and the position here depends on whether or not the refund is paid back into the scheme (see paragraph 7.23). If it is paid back in the same year of assessment as the refund occurred, for the purposes of the tax charge the refund of contributions can be treated as not having taken place.

**Tax on Certain Commutation Payments**

17.27 Section 599 imposes income tax at the rate of 20% on the administrator of an approved or relevant statutory scheme on part of a commutation payment made under a rule permitting full commutation of a member's or pension credit member's pension on grounds of triviality or exceptional circumstances of serious ill-health.

Where the retirement is on grounds of serious ill-health and the member is in contracted-out employment
• the GMP and/or “Section 9(2B)” Rights, and
• 50% of Protected Rights where that individual is married or in a civil partnership at the time of payment

may not be commuted. As full commutation is not possible the charge to tax will not apply.

No tax liability arises under section 599 in respect of widows’, widowers’ surviving civil partners’ or dependants’ pensions which have been commuted on grounds of triviality.

17.28 For an employee whose benefit rights have not been subject to a pension sharing order or an employee whose benefit rights also include pension credit rights which the scheme does not treat separately from employee benefit rights (see paragraph 6A.19), tax under section 599 is charged on the excess of the commutation payment over the greater of:

(a) 3/80ths of final remuneration for each year of service with the relevant employer less any lump sum received other than by commutation. For this purpose final remuneration must be calculated using the statutory definition in section 612(1), i.e. the average annual remuneration (subject to the permitted maximum where appropriate) of the last 3 years’ service, and

(b) the maximum lump sum payable in commutation of pension under the scheme rules otherwise than on grounds of triviality or exceptional circumstances of serious ill-health. Where the rules provide incapacity benefits which take account of future notional service to normal retirement date, that service may, in appropriate circumstances, be taken into account in calculating this maximum lump sum. In triviality cases, any amounts which are otherwise non-commutable under the contracting-out requirements should be excluded from the calculation of the maximum lump sum deductible.

NB GMPs, “Section 9(2B)” rights and Protected Rights are commutable on grounds of triviality and all Protected Rights might also be commuted in certain circumstances where the member is in exceptional circumstances of serious ill-health. Therefore full commutation is possible and so the section 599 charge applies.

17.29 Where an employee’s benefit rights have been subject to a pension sharing order (including an employee within the administrative easement described in paragraph 7.7), tax under section 599 is charged on the excess of the commutation payment over the amount determined in accordance with paragraph 17.28(b) only.

17.30 Where the rules of a scheme allow for the commutation of the entire pension payable to a pension credit member from pension credit rights on grounds of triviality or exceptional circumstances of serious ill-health, and

• the pension credit rights are the only benefits held under the scheme for the pension credit member, or

• the scheme makes provision for the pension credit rights to be treated separately from any benefits that the pension credit member also has in the scheme as a result of membership of the scheme as an employee (see paragraph 6A.18)

Tax under section 599 is charged on the excess of the commutation payment over the largest lump sum that would have otherwise been receivable by commutation of any part (but not the whole) of the pension payable under the scheme, from the pension credit rights (see paragraph 6A.8).

Where the pension credit member is under age 50 when full commutation on the above grounds takes place, an age 50 annuity rate may be used to determine the pension that could have been provided for the pension credit member. For this purpose, the “age 50 annuity rate” must be determined either by an appropriate available market rate or by the scheme actuary. The largest
lump sum otherwise receivable by commutation in accordance with paragraph 6A.8 is then calculated by reference to the pension so determined.

17.31 Where the scheme provides for a separate lump sum rather than for commutation of pension, and the pension is commuted e.g. on grounds of triviality, the whole of the payment will normally be chargeable to tax. No deduction can be made under paragraph 17.28(b) because the largest amount otherwise receivable in commutation of pension would be nil.

Two or more schemes

17.32 Where an employee takes a lump sum in full commutation of benefits under 2 or more separate schemes relating to the same employment, the calculation of section 599 tax should be based on the aggregate of the lump sums payable, each scheme being liable for the relevant proportion of the total tax payable.

Overseas employment

17.33 The section 599 charge does not apply where the employee's employment was carried on outside the United Kingdom (section 599(4)). This condition will be regarded as satisfied where the employee is resident abroad if sufficient of his or her service was carried on abroad to fulfil the conditions set out in paragraph 17.4. Alternatively, irrespective of the country of residence, the payment will be treated as exempt if at least 75% of his or her service was carried on abroad. For this purpose "service" means the service in respect of which the pension was granted.

17.34 When an administrator is accounting to the Inspector of Taxes for tax due under section 599, a statement should be enclosed showing the basis on which the tax is computed. IR SPSS may be consulted in cases of special difficulty.

**Taxation of Repayment of Surplus AVCs**

17.35 When a surplus of Additional Voluntary Contributions funds is repaid to a member or, to his or her personal representatives (in the event of the member's death) (see paragraph 4.7) from an exempt approved scheme or a relevant statutory scheme the administrator becomes liable to tax under Case VI of Schedule D. The tax is charged under section 599A at the appropriate rate on such amount as, after deduction of tax at that rate, would equal the amount repaid to the member or his/her personal representatives. Where a member takes a refund of contributions on leaving service (see paragraphs 10.52 and 10.53), any part of that refund which comprises a return of Additional Voluntary Contributions, is chargeable under section 598 (see paragraph 17.22) and not under section 599A.

17.36 In the member's or personal representatives hands the repayment is treated as being net of basic rate tax. This tax is not repayable and a higher rate taxpayer will have to pay additional tax on the grossed up amount. There is, however, no higher rate liability if the repayment arises on death. The administrator is required to give the member a certificate showing the amount to be declared in his or her tax return. This figure should be the amount which, after deduction of tax at the basic rate, would equal the amount repaid.

**Example**

17.36a A surplus of Additional Voluntary Contributions funds of £1,000 is held by the scheme administrator.

**STEP A**

The scheme administrator, in satisfaction of its liability, deducts tax at 32%, viz.

\[
\begin{align*}
\text{Surplus} & = £1,000 \\
\text{less tax} & = £320
\end{align*}
\]
**payable to member** = £ 680

**STEP B** - The member receives £680. This is treated as income which has suffered basic rate tax of 22%, viz.

Net received = £ 680
grossed up at basic rate = £ 871.79 (amount to be certified and declared in employee's tax return)

If the member is a basic rate taxpayer, there is no further liability.

**STEP C** - If the member is a higher rate taxpayer he or she will be chargeable at the higher rate on the grossed-up repayment, viz.

£ 871.79 @ 18% = £ 156 further liability
(40% - 22%)

**NB** For 1997/98 – 1999/00 the basic rate of income tax was 23%, for 1996/97 it was 24% and for earlier years i.e. 1992/93 - 1995/96 it was 25%.

**Taxation of Unauthorised Payments**

17.37 If a payment other than a pension is made to or for the benefit of an employee or pension credit member from an approved scheme (whether or not exempt approved) and the payment is not expressly authorised by the rules of the scheme, the employee or pension credit member is liable to tax on the payment under Schedule E for the year of assessment in which it was made (section 600).

**Taxation of Payments to an Employer**

17.38 Section 601 imposes liability to tax on payments (including refunds of surpluses - see Part 13) received by an employer from an exempt approved scheme. Where the rate of charge is 35%, the tax is not capable of being reduced or offset by reference to the employer's position in respect of other tax but in most cases no payment will be necessary by the employer as the tax deducted from the refund (see paragraph 13.27(d)) will cover the liability. If, however, tax is not paid to the Inland Revenue by the administrator, it will be collected from the employer (as will interest charged for tax paid late).

17.39 The 35% charge does not apply to payments made before the scheme became exempt approved and an employer which is a charity is exempt from the charge. Nor does it apply to the following:

(a) reimbursement of expenditure incurred by the employer on behalf of the administrator which was a proper obligation of the administrator;

(b) interest on or repayment of a loan from the employer;

(c) a loan to or investment of scheme funds with the employer on a commercial basis;

(d) reimbursement of a state scheme premium paid by the employer or of an amount withheld from the provision of benefits for a member under a lien rule (see paragraphs 7.32(b) and 17.23); and

(e) refund of premiums or contributions paid in error where the circumstances are as set out in paragraph 5.17.
18.1 The statutory requirements relating to applications for approval are set out in section 604. It:

- provides for the form of application for approval to be prescribed by the **Board**,
- requires the trustees (or sponsors in the case of a non-trust scheme) to make the application in writing before the end of the first year of assessment for which approval is required, and
- requires the application to be accompanied by 2 copies of the scheme documents and certain other information.

18.2 The **Board** have prescribed the following 4 application forms:

- PS176 for schemes open to more than one employee,
- PS177 for individual arrangements,
- PS178 for Hancock annuities, and
- PS400 for simplified defined contribution schemes (see Part 22).

See Appendix II for details of how to obtain these forms. Supplies of these forms are available from **IR SPSS**. Practitioners may print their own supplies provided that they are identical in all respects (including colour) with the Inland Revenue application forms. Where practitioners wish to produce their own forms, they should notify **IR SPSS** Audit & Pension Schemes Services and insert a user identifier at the bottom right hand corner of the form, e.g. PS176 (1/95) (XYZ Ltd).

18.3 Because the statutory requirements are often not practicable the **Board** have authorised certain concessionary relaxations. An application must be made on the correct prescribed form accompanied by the relevant documents (see paragraph 18.4) and be made within the concessionary period described in paragraph 18.5.

18.4 Applications in relation to different types of scheme require different accompaniments. Although the statutory requirement is for 2 copies of the scheme documents to accompany the application, in practice **IR SPSS** will be content to accept one copy of each of the required accompaniments. The application should comprise:

**A Schemes for more than one member**

All such schemes

- Application on form PS176 signed by all of the trustees/sponsors
- Completed form PS 176(A/T)
- A copy of the document(s) establishing the scheme if the documentation is **not** based on, and accords in all respects with,
standard or model documents agreed or under negotiation with IR SPSS (where standard or model documents are used, a copy of that documentation or an Inland Revenue Documentation Certificate is not required)

- If the scheme is using interim documentation within the terms of paragraph 2.13, form PS 176(INT) must also be completed

Additionally for all self-administered schemes

- Initial actuarial report or advice (signed by an Actuary) on which funding is based

Additionally for all small self-administered schemes

- List of current investments

In practice IR SPSS will be prepared to dispense with the need for an initial actuarial report and a list of current investments in the case of:

- a small self-administered scheme where the initial investment is in a policy or policies with a single life office,

- a self-administered contracted-out money purchase scheme which is accepting only minimum payments and, where appropriate, incentive payments under the relevant Department of Work and Pensions legislation, has less than 12 members but is not treated as "small" (see paragraph 20.1) and does not provide benefits for its members which are additional to final salary benefits

B  Individual arrangements

- Application on form PS177 signed by all of the trustees/sponsors

- Completed from PS 177(A/T)

- Copy of exchange letter and/or rules if the documentation is not based on, and accords in all respects with, standard or model documents agreed or under negotiation with IR SPSS (where standard or model documents are used, a copy of that documentation or an Inland Revenue Documentation Certificate is not required)

C  Hancock annuities

Application on form PS178 signed by all of the trustees/sponsors.

18.5 An application for approval should be made as soon as practicable after the establishment of a scheme for which approval is required and in any case (where approval is desired from the date
of establishment) not later than the appropriate date under the following table:

<table>
<thead>
<tr>
<th>Date scheme established</th>
<th>Date by which application must be received by IR SPSS</th>
</tr>
</thead>
<tbody>
<tr>
<td>In the 6 months ending 5 October by the following 5 April</td>
<td></td>
</tr>
<tr>
<td>In the month ending 5 November 5 May</td>
<td></td>
</tr>
<tr>
<td>&quot; &quot; &quot; &quot; 5 December 5 June</td>
<td></td>
</tr>
<tr>
<td>&quot; &quot; &quot; &quot; 5 January 5 July</td>
<td></td>
</tr>
<tr>
<td>&quot; &quot; &quot; &quot; 5 February 5 August</td>
<td></td>
</tr>
<tr>
<td>&quot; &quot; &quot; &quot; 5 March 5 September</td>
<td></td>
</tr>
<tr>
<td>&quot; &quot; &quot; &quot; 5 April 5 October</td>
<td></td>
</tr>
</tbody>
</table>

"Date scheme established" means the date on which there was first evidence of an intention to set up the scheme. Usually this will be the date of the declaration of trust, notwithstanding any later commencement date referred to in the documents.

Where the date by which an application must be received by IR SPSS falls on a weekend or a Bank Holiday the last immediately preceding working day should be substituted for the date above.

18.6 An application will not be accepted as valid unless it is made on the appropriate form fully and accurately completed and accompanied by the appropriate documents. It will, if invalid, be rejected under cover of a printed note which will indicate why the application is deficient. It will not be possible to authorise provisional relief on employees' contributions until a fully completed application is received. The date on which the resubmitted complete application is eventually received will then constitute the valid application date. This may affect the date from which approval can be given. Applications received by IR SPSS after 5th April 2002 may not be submitted with only interim documentation unless the scheme falls within the terms of paragraph 2.13.

18.7 On receipt, before 6th April 2002, of a valid application for approval of a scheme set up under interim documentation (see paragraph 2.10), provided that the Inland Revenue are satisfied that the scheme is properly established and that the members have been advised of the essential features of the scheme, immediate relief on a provisional basis will be allowed in respect of contributions made by employees. This relief is given by means of the net pay arrangement (see paragraph 4.3) which will be authorised by the Inspector of Taxes dealing with the Schedule E affairs of the employer on production to the Inspector of form PS 4(B) which is issued by IR SPSS. If the scheme is set up under trust and operated through insurance policies, premiums may be referred to pension business (see paragraph 17.15).

The essential features, should as a minimum, cover:

- the formula which will determine the pension promised or targeted at normal retirement date,
- a description of the death in service benefits,
- the amount of the members' contribution required.

18.8 The interim documentation on which the initial application for approval is based states that definitive documentation will be adopted within 24 months. If this is not done, the application for approval will be treated as withdrawn. As a consequence, any provisional tax reliefs will be withdrawn and the scheme will be taxed as a funded unapproved retirement benefits scheme (FURBS) from the date of commencement. This paragraph only applies to valid applications received by IR SPSS before 6th April 2002.

18.8a Applications received by IR SPSS after 5th April 2002 may only be submitted with just interim
documentation if the scheme falls within the terms of paragraph 2.13. Where the interim deed meets the requirements of paragraph 2.15 and the application is otherwise acceptable the scheme will be approved. However the scheme approval will have a specific condition attached to it. The scheme will be required to submit definitive documentation to IR SPSS within 12 months of the scheme’s establishment.

18.9 Until formal approval is granted no relief can be given under section 592(4) on the employer’s contributions nor does the law provide for tax suffered on scheme investments to be repaid. Approval, once given however, is backdated in all schemes except discretionary schemes to the later of:

- commencement of the scheme or, if later, the date of the declaration of trust, or
- the start of the tax year in respect of which a valid application for approval was made (in the case of an application made outside the relevant time limit in paragraph 18.5)

In the case of discretionary schemes (see paragraph 3.2), it is backdated to the later of:

- commencement of the scheme or, if later, the date of the declaration of trust,
- the date on which the first contribution was paid to the trustees (or in an insured scheme, the date of payment of the first premium to the life office),
- the date on which the first employee was notified of his or her membership and of his or her rights under the scheme, or
- the start of the tax year in respect of which a valid application for approval was made in the case of an out of time application.

Assessments on the employer can then be adjusted and any tax suffered by the scheme on its investments may be repaid.

If approval is not granted from the commencement of the scheme relief will not be allowed in respect of contributions made by employees in the period prior to the date of approval and any provisional tax relief (see paragraph 18.7) will be withdrawn. The employer’s contribution to the scheme prior to the date of approval will be assessed on the employees under section 595(1) and a deduction under section 76(1) Finance Act 1989 can be given only if the employees are so assessed under section 595(1). Relief in respect of the income and gains of the scheme in that period will not be allowed.

Where however, the employees are not responsible for the delay in applying for approval, and either:

(i) the scheme documents contain no unapprovable features, or
(ii) any unapprovable features in the original executed documents are removed before they have been acted upon

the Inspector of Taxes may consider on an individual basis the waiver of the S595 (1) liability for the period between commencement and approval where, if the scheme was to be wound up and a new scheme set up in its place, the new scheme would receive tax relief under Section 596 (3) ICTA 1988 for the contributions liable to a Section 595 (1) charge in the original scheme.

18.10 The tax system provides ways for the employer and the scheme to avoid, or to be compensated for, any financial disadvantage through delay in approval. The collection of tax related to the non allowance of the employer’s contributions may be held over and repayments of tax which are delayed may qualify for the addition of a supplement under section 824.

18.11 Some large self-administered schemes set up using interim documents may, nevertheless,
suffer financial loss in the period before they are approved because they cannot reinvest the tax suffered on investments. To meet this situation the Board have authorised an indemnity procedure to allow provisional repayments of tax in suitable cases for a period up to 2 years. To benefit from this procedure trustees of the scheme need to enter into a deed of indemnity to safeguard the Inland Revenue if, for any reason the scheme should not be capable of approval. Copies of a model deed may be obtained from IR SPSS. This paragraph only applies to valid applications received by IR SPSS before 6th April 2002.

18.12 The indemnity procedure is not practicable in small cases (the amounts of tax repayable must be at least £5,000 a year) nor where the definitive documents are at an advanced state of preparation. Nor is it intended to shelter schemes from the consequences of any lack of diligence in preparing and executing definitive documentation. The Inland Revenue retain the right to refuse requests for the indemnity procedure. This paragraph only applies to valid applications received by IR SPSS before 6th April 2002.

18.13 If scheme documentation does not meet the requirements for approval, IR SPSS will, within reason, identify the shortcomings. The documentation will then need to be amended before approval can be given.

Amendment of Approved Schemes

18.14 Section 591B(2) (inserted by section 36(1) Finance Act 1991) provides that where an alteration is made to a retirement benefits scheme, no approval already given will continue to apply unless the alteration is approved by the Board, or the scheme is of a kind and the alteration is of a type in relation to that kind of scheme, as is specified in Regulations as not requiring the approval of the Board. All amendments requiring the approval of the Board (or a documentation certificate PS6 in the case of a standard rule amendment agreed by the Standard Documents Section of IR SPSS; a specimen of this certificate is included in Appendix II) must therefore be forwarded to IR SPSS (see paragraph 16.12) who will, if satisfied, issue a formal notification that the alteration has been approved. It is not necessary to send copies of amendments to members booklets or announcement letters to IR SPSS unless specifically asked to do so.

Examination Procedures

18.15 The preparation and the examination of pension scheme documents is very time consuming and it is therefore in the interests of both practitioners and the Inland Revenue that standard forms of wording should be agreed for multiple use. IR SPSS will therefore consider the agreement of standard documents (consisting of interim and/or definitive trust documents and rules) for conventional schemes, small self-administered schemes and simplified defined contribution schemes. Ideally, once agreed, such standard documents should be used unamended but, if some limited tailoring is necessary in a particular case the document should be accompanied by a marked-up copy of the agreed standard document to indicate where the deviations from the agreed wording occur.

18.16 Where the formal standards procedure is not appropriate, because schemes are expected to be too few in number to warrant full examination on the standards basis, practitioners may seek to agree documentation with IR SPSS on a leading case. The approval of other schemes may then be facilitated by quoting the leading case reference number when the scheme documents are submitted for approval.

18.17 Where new schemes do not adopt definitive documentation at the outset but propose to adopt documentation which is under negotiation or has only recently been agreed with IR SPSS’s Standard Documents Section, the standard reference indicator of the proposed documentation should be shown on the application form.

18.18 Where scheme rules have been amended repeatedly, interpretation is made more difficult and time consuming. The Inland Revenue reserve the right to require a marked-up copy or a
18.19 When a scheme is approved *IR SPSS* will issue a formal letter of approval. This letter, when produced to the appropriate Inspector of Taxes, will enable the consequent tax reliefs and exemptions to be obtained.

18.20 As mentioned in paragraph 7.11 it is necessary for the documentation of all approved schemes to contain a comprehensive limits rule.
Part 19. Withdrawal of Approval

General

19.1 Section 591B(1) (inserted by section 36(1) Finance Act 1991) empowers the Board to withdraw approval of a scheme if they consider that approval is no longer warranted. If an approved scheme has not been involved in tax avoidance then withdrawal of approval due to a transgression of the tax approval conditions will only take place after the administrator has been given a full and clear warning of what the consequences will be and an opportunity to put matters right. Where an approved scheme is involved in or used for the purposes of tax avoidance the Board will not be bound by the practice of giving a prior warning to the administrator and may withdraw approval without such prior warning. Withdrawal is effected by a notice in writing to the administrator, specifying the grounds for, and the operative date of, the withdrawal. The operative date will normally be that of a particular event which has made the scheme no longer approvable or 17 March 1987 if later.

19.2 Approval may be withdrawn for such reasons as serious breaches of the rules e.g. payment of excessive or unauthorised benefits; over-funding to an unacceptable extent; use of the scheme for tax avoidance; persistent failure to furnish information or meet the scheme’s tax liabilities. Approval will also lapse automatically where a scheme:

(a) makes an unapprovable alteration (section 591B(2));

(b) fails to comply with Regulations made under section 591 within a period of 3 years of those Regulations coming into force (section 591A(2)).

In the case of (b) approval lapses at the end of the 3 year period.

19.3 The following taxation consequences arise following withdrawal or lapsing of approval:

(a) all benefits payable from the scheme on or after 27 July 1989 become chargeable to tax under section 596A except to the extent that they are chargeable under section 19(1) or section 58;

(b) employees will become liable to tax under section 595 in respect of any subsequent contributions by the employers;

(c) all exemptions and reliefs flowing from exempt approval by virtue of section 592 are forfeit from the date that approval is withdrawn or lapses;

(d) exemption from Capital Gains Tax under section 271(1)(g) Taxation of Chargeable Gains Act 1992 is not available on any capital gains realised by the scheme on or after the date of withdrawal;

(e) tax continues to be chargeable:

(i) under section 598 on repayments to employees of contributions paid before the scheme ceased to be exempt approved (see paragraph 17.22);

(ii) under section 601 on repayments to an employer out of funds held at any time for the purposes of the scheme (see paragraph 17.38 et seq.);

(iii) under section 599A on repayments of surplus funds arising from the payment of Additional Voluntary Contributions (see paragraph 17.35 et seq.); and

(iv) under section 600 on payments (made in the period between withdrawal of approval and 26 July 1989) not expressly authorised by the rules of the scheme (see paragraph 17.35).
19.4 If an insured scheme ceases to be exempt approved any premiums already paid which have been referred to pension business (see paragraph 17.15 et seq.) and the accumulated income applicable to those premiums, may remain in pension business as long as they are used solely to provide relevant benefits within the Revenue limits applicable to exempt approved schemes. (The tax treatment of any benefits paid on or after the effective date of the withdrawal of the scheme's approval will be that applicable to benefits paid by unapproved schemes - see paragraph 19.3(a)). Otherwise the premiums and accumulated income should be transferred to basic life assurance and general annuity business and any future premiums should be treated similarly.

19.5 In addition, for certain schemes which have their approval withdrawn or otherwise cease to be approved on or after 2 November 1994, tax will be chargeable under section 591C at the rate of 40% on the value of the scheme assets on the day before approval ceases. Debt due from the employer (or any connected company) or from a person who has at any time been a member of the scheme (or any connected person) will be taken at face value, otherwise the value of the scheme assets will be their market value ascertained in accordance with section 272 Taxation of Chargeable Gains Act 1992. Schemes subject to this 40% tax charge are those which:-

(i) immediately before the date of cessation of approval had less than 12 members (members include pensioners and deferred pensioners as well as active members), and / or

(ii) in the year before tax approval ceased had as a member a person who was in that year, or had been at any time, a controlling director of a company which has at any time contributed to the scheme, and / or

(iii) in the three years before tax approval ceased* received a transfer value from another approved scheme, personal pension scheme or retirement annuity contract for a controlling director of a company or a person whose earnings were chargeable to tax under Schedule D.

*sub-paragraph (iii) applies only to schemes which cease to be approved on or after 17 March 1998.

The tax is chargeable under Case VI of Schedule D and liability for paying it rests with the scheme administrator. The administrator is normally the scheme trustees unless they have appointed someone else to be responsible for the statutory duties imposed under the tax approval legislation. Section 606 sets out the fallback position in the case of default by the administrator. In such cases, responsibility for complying with the administrator's duties reverts to the employer or, if the employer defaults, to those scheme members whose entitlement under the scheme (whether from the current or an earlier employment or occupation) derives from controlling directorships or Schedule D earnings.
INTRODUCTION

20.1 As the term indicates, a small self-administered scheme is a self-administered scheme with a small number of members. The Inland Revenue's discretion to approve a small self-administered scheme is limited by the Retirement Benefits Schemes (Restriction on Discretion to Approve) (Small Self-administered Schemes) Regulations 1991 (SI 1991 No 1614, as amended). References in this Part to the "SSAS Regulations" are to those Regulations and the guidance in this Part should be read in conjunction with those Regulations. The SSAS Regulations define a small self-administered scheme as a self-administered scheme with less than 12 scheme members where at least one of those members is connected with another member, or with a trustee or an employer in relation to the scheme. For the purpose of the definition of a small self-administered scheme only, "scheme member", means a member who is currently accruing benefits in the scheme as a result of service as an employee of a participating employer. It does not include deferred benefit members, pensioner members, pension credit members or other beneficiaries. The Inland Revenue may also require a scheme with 12 or more members to be treated as a small self-administered scheme and to comply with the special requirements set out in this Part. An example would be a scheme established primarily for a few family directors, to whom were added some relatively low-paid employees with entitlement to a very low level of benefits, included as makeweights to bring the total membership to 12 or slightly more. Conversely it will not be necessary to apply "small scheme" treatment to a scheme with less than 12 members if all the members are at arm's length from one another, from the employer and from the trustees. An approved insured scheme which becomes a small self-administered scheme will lose its approval unless it complies with the requirements of the SSAS Regulations as at the time it becomes such a scheme and thereafter.

20.2 The reasons why the Inland Revenue consider special requirements necessary for the approval of such schemes are:

(a) Under trust law which evolved before the advent of pension schemes, a trust with one or a few beneficiaries is susceptible to being broken regardless of the terms in which the trust is constituted.

(b) The funding of a self-administered scheme for a few members is difficult because the small membership limits the extent to which statistical fluctuations can be smoothed out (e.g. for mortality).

(c) Small self-administered schemes are usually established to provide benefits for directors. Often the scheme members control the employer company and are also trustees of the scheme. This multiplicity of roles can face a trustee with a conflict of interests leading to actions concerning the scheme being taken for reasons other than the provision of benefits on retirement.

20.3 The special requirements thus fall into three categories viz.

(a) control of the format of the trust,

(b) control of funding, and

(c) control of investments.

THE TRUST

Pensioneer Trustee

20.4 The SSAS regulations restrict the Board's discretion to approve a small self-administered scheme to one whose governing documentation contains provisions requiring one of the trustees
to be a “pensioneer trustee”. A pensioneer trustee is an individual or body recognised by the Inland Revenue as being widely involved with small self-administered schemes and having dealings with IR SPSS, who has given an undertaking to the Inland Revenue. In the undertaking the pensioneer trustee agrees

- not to consent to any action that the pensioneer trustee considers infringes any approval requirement relating to a small self-administered scheme, and
- not to consent to the termination of a small self-administered scheme otherwise than in accordance with the approved terms of the winding-up rule, and
- to provide to IR SPSS at least annually, details of the IR SPSS scheme reference numbers (where allocated) together with the corresponding scheme’s and sponsoring employer’s names for which the pensioneer trustee acts.

20.5 An individual who acts as a pensioneer trustee has demonstrated to the Inland Revenue that he or she has a knowledge of Inland Revenue requirements concerning the approval and continued approval of small self-administered schemes and has evidenced that knowledge in relation to at least 20 small self-administered schemes. The individual can also demonstrate effective management systems and procedures which ensure that the terms of the undertaking can be met.

20.6 Where a corporate body, including an insurance company or an associated company established for the purpose of acting as a pensioner trustee, is recognised as a pensioner trustee all the directors of that corporate body have signed the undertaking given to the Inland Revenue. The corporate body can also demonstrate that a person or persons with the required experience and knowledge detailed in paragraph 20.5 holds a position of authority within the corporate body’s management systems that enables the terms of the undertaking to be met.

20.7 The pensioneer trustee must, in accordance with the normal requirements of trust law, be a registered owner (along with the other trustees) of all scheme assets and a mandatory co-signatory to all scheme bank accounts (including accounts with building societies and licensed deposit takers).

20.8 Another object of the appointment of a pensioneer trustee is to block any proposal that the trust should be terminated and the funds distributed among the members. It is however accepted that the trustees have no power to resist such a proposal if all the persons having an interest under the trust are agreed in requiring this action (Saunders v Vautier 1841). Such a consensus is unlikely in the context of a typical pension scheme where, even if the number of members is small the existence of further contingent beneficiaries can rarely be excluded.

20.9 The trust provisions of an approved small self-administered scheme must be framed to allow the pensioneer trustee to fulfil his or her function. Thus a provision that allows the trustees to act on a majority rather than unanimous decision must be qualified so as not to apply in relation to the termination of the scheme. A scheme subject to Scottish law must expressly require the pensioneer trustee’s concurrence in any decision about the scheme’s termination. Also, scheme documents must be drafted in such a way to permit a pensioneer trustee to become a co-signatory of scheme bank accounts and co-owner of scheme assets.

20.10 A pensioneer trustee should not act as such in any scheme of which he or she is a member. Similarly a corporate trustee should not act in that capacity for a scheme for its own employees. A pensioneer trustee must not be connected with a scheme member, any other trustee of the scheme or any employer in relation to the scheme.

20.11 The circumstances and conditions under which a pensioneer trustee’s appointment in relation to a particular small self-administered scheme can be terminated are set out in Regulation 9 of the SSAS Regulations or, for schemes approved on or before 17 March 1998, paragraph 7 of
Schedule 15, Finance Act 1998. A pensioneer trustee’s appointment cannot be terminated unless there is an immediate replacement by another pensioneer trustee. There are some limited exceptions to this requirement, which are

- the death of the pensioneer trustee
- a court order removing the pensioneer trustee from an appointment
- the pensioneer trustee is prohibited, suspended or disqualified from being a trustee under section 3, 4 or 29 of the Pensions Act 1995 or the corresponding Order for Northern Ireland
- the loss of Inland Revenue approval to act as a pensioneer trustee
- the appointment is terminated due to the pensioneer trustee committing a fraudulent breach of the trust in relation to a scheme.

Where an appointment is terminated by virtue of any of the limited exceptions listed above, the appointment of a successor pensioneer trustee must be made no more than 30 days after the date on which the former pensioneer trustee’s appointment was terminated.

A copy of the document(s) removing a pensioneer trustee and immediately appointing a replacement pensioneer trustee must be sent to IR SPSS within 30 days of date on which the change of pensioneer trustee took effect.

Where a pensioneer trustee’s appointment is terminated without an immediate successor by virtue of any of the limited exceptions listed above, a report (together with copies of any relevant documents) must be sent to IR SPSS within 30 days of the terminated appointment. A successor pensioneer trustee must be appointed within 30 days of the terminated appointment and a copy of the document(s) appointing the replacement pensioneer trustee must be sent to IR SPSS within 30 days of the date on which the new appointment took effect.

20.12 The Inland Revenue reserves the right to withdraw pensioneer trustee status should the circumstances warrant, each case being considered on its own facts. Facts taken into account would include

- tax avoidance, for example, if the individual or corporate body or any of its directors or staff is found to be involved in or promoting tax avoidance, whether or not the avoidance relates to pension schemes
- the terms of the undertaking they have signed are not complied with
- it is apparent that there are no satisfactory systems in place to ensure that the undertaking is complied with
- action taken by Opra under section 3, 4 and 29 (3) or (4) of the Pensions Act 1995

Pensioneer trustee status will not normally be withdrawn without prior written warning. Such a warning will explain why status as a pensioneer trustee is jeopardised, give an opportunity for problems to be rectified and for representations to be made. Pensioneer trustees involved in tax avoidance or evasion should not expect these procedures for withdrawal of pensioneer trustee status to apply.

20.13 The names of all Inland Revenue approved pensioneer trustees is published on the IR Website www.inlandrevenue.gov.uk.
Entitlement against the whole fund

20.14 It is not permissible for an approved small self-administered scheme to secure a member's benefits against particular trust assets. There is no objection to the calculation of the amount of the member's benefits being notionally linked to the value of particular assets but the trust provisions must ensure that the member's entitlement to benefit is against the funds of the trust as a whole.

Multiple small schemes

20.15 Regulation 3 of the SSAS Regulations prohibits the Board from approving a small self-administered scheme in respect of an employer where that employer already has such a scheme approved by the Board to which it was or is entitled to pay contributions, and that scheme has not been wound-up. Thus if more than one employee is to be pensioned through this medium they should all be included in one scheme. Where an employee is employed by several companies in a group of associated companies, one centralised small self-administered scheme may be established in which all the relevant companies participate (see paragraphs 21.3 and 21.4 in this context) or, alternatively, each employer may set up its own small self-administered scheme to provide benefits for the employee based on his or her salary and service with it alone.

Death benefits

20.16 The scheme rules should provide that lump sum benefits payable on death (including any lump sum payable under a pension guarantee) are, except where paragraph 11.12 applies, to be distributable at the trustee's/administrator's discretion among a wide class of beneficiaries.

FURTHER REQUIREMENTS FOR PENSIONEER TRUSTEES

Co-ownership of scheme assets

20.17 As a trustee of the scheme, the pensioneer trustee must be a co-owner of scheme assets along with the other scheme trustees. The guiding principle is that, where it is legally possible, the pensioneer trustee should be the registered owner (along with the other trustees) of all assets owned by the schemes for which he/she/the company acts as a pensioneer trustee. The prime object is for the pensioneer trustee’s name to be on the document of title. It is not acceptable for just the title “Pensioneer Trustee” put on the documentation instead of the actual name of the pensioneer trustee. If it is not possible for the pensioneer trustee’s name to be put on the title document or there is no such document, there should be a legally enforceable restriction in place to prevent the assets being realised for cash without the written authority of the pensioneer trustee. Any proceeds from the sale/disposal of any assets owned by the scheme must be paid to a scheme bank account of which the pensioneer trustee is a co-signatory.

20.18 The name of the pensioneer trustee should appear on the document evidencing any interest in land/property owned by the trustees of the SSAS along with the names of the other trustees. This should be the case for any document of title in respect of registered and unregistered land both inside and outside the UK. If there is any restriction on the number of names that can be placed on the title deed, the name of the pensioneer trustee must be included.

20.19 As an alternative to the registered co-ownership requirement explained in paragraph 20.18, there is no objection to the pensioneer trustee registering a legally binding “restriction” in respect of land/property that is held in the name of the other trustees.

20.20 For land/property registered in England and Wales a “restriction” may be registered at HM Land Registry using Form 75: “Application to register a Restriction”. In the case of registered land in Northern Ireland, an “inhibition” may be registered at the Land Registers of Northern Ireland. A “caution” in respect of land/property registered at the Land Registers of Northern Ireland is not an acceptable alternative to the registered co-ownership requirement or registered “inhibition”.

20.21 It is not possible to register a “restriction” in respect of land/property situated in Scotland so
for such property paragraph 20.18 applies. Where a scheme owns land in Scotland or Northern Ireland and the land had been charged to secure an existing loan from a bank or other financial institution prior to 29 August 2000 it will not be necessary for the Pensioneer Trustee to become a co-owner of that land until the property ceases to be so charged.

20.22 The pensioneer trustee must be a party to the agreement evidencing loans made by the scheme trustees. Loans made before 1 October 2000 are not subject to this requirement. Where a loan made prior to 1 October 2000 is “rolled-over”, see paragraph 20.60, it is not necessary for the pensioneer trustee to be a party to the document evidencing the “roll-over” unless new money is being loaned.

All cash repayments of loans and cash payments of loan interest should be paid into a scheme bank account of which the pensioneer trustee is a mandatory co-signatory. All repayments/payments in non-cash form should be transferred into the names of all the trustees, including the pensioneer trustee.

20.23 These types of assets owned by schemes should be registered to show that the pensioneer trustee is a co-owner of the asset. If there are any restrictions on the number of names that can be placed on the share certificate etc, the name of the pensioneer trustee must be included. As regards portfolios of securities the position is set out in paragraph 20.24.

20.24 The pensioneer trustee must be signatory to any arrangement between the trustees and fund manager/broker. This arrangement must ensure that any proceeds paid from the portfolio to the trustees is paid only into a scheme bank account of which the pensioneer trustee is a mandatory co-signatory. The pensioneer trustee does not have to be co-signatory to any nominee account that is set up by the fund manager/broker as part of the management of the portfolio, as it should not be possible for funds held in these accounts to be accessed by anyone other than the fund manager/broker. If the trustees can access the nominee accounts the pensioneer trustee must be a co-signatory. A “fund manager/broker” is someone who is professionally engaged in the provision of investment or fund management services.

20.25 The requirements in paragraph 20.24 also apply for other management arrangements where shares are held on behalf of the trustees by a nominee and any share transactions undertaken on non-United Kingdom stock exchanges that might require the share certificate to be registered in the name of a recognised nominee. Where shares are registered in the name of “Crest” it is acceptable for written arrangements to be put in place in the effect that the shares cannot be transferred out of the control of the duly appointed fund manager (other than in the normal course of managing investments) without the written consent of the pensioneer trustee.

20.26 The pensioneer trustee must be a party to insurance policies and annuity contracts taken out for the purpose of the scheme. The wording of the policies/contracts must require that any proceeds (e.g. on the surrender of the policy) are paid only if the pensioneer trustee agrees in writing to the insurance company. This requirement does not apply in respect of policies/contracts taken out before 1 October 2000.

20.27 There should normally be a document, which evidences the trustees’ ownership of the asset. Such documentation should show that the pensioneer trustee is one of the owners.

20.28 The pensioneer trustee must be a party to all scheme borrowings undertaken on or after 1 October 2000.

Co-signatory requirements

20.29 It is the duty of a trustee to ensure, among other things, that a scheme is properly
administered. Money in scheme bank accounts belongs to the trustees. In order to ensure that
to mandatory co-signatories of scheme bank accounts. Accounts that give rise only to a
liability, such as loan or overdraft accounts, do not have to be covered by this co-signatory
requirement.

20.30 All money contributions paid by employers and scheme members, money transfers into the
scheme and any other monies paid into a scheme must be paid into a scheme bank account to
which the pensioneer trustee is a mandatory co-signatory.

20.31 There is no objection to trustees (other than the pensioneer trustee) making regular, routine,
payments from a scheme bank account, provided the payments are covered by a standing order or
direct debit arrangement which the pensioneer trustee has previously authorised. Such payments
may include, for example, payment of pension (but not lump sums), premiums paid on insurance
policies, rents, rates, standing charges for electricity, gas, telephone, mortgage/loan repayments,
ground rents, bank charges. The pensioneer trustee does not have to authorise, for example,
increases in pensions made to reflect cost of living increases provided the original standing order
has been authorised by the pensioneer trustee. There is no objection to contributions being paid
by the employer direct to an insurance company in respect of a policy provided the pensioneer
trustee is aware of and in agreement with the particular arrangements. Employer contributions
paid direct to a unit/investment trust can be made on the same basis. Also, the pensioneer trustee
does not have to be involved with the transferring of money from one trustee bank account to
another (for example, from a current account to a deposit account) provided the pensioneer trustee
is aware of and in agreement with the arrangement. The pensioneer trustee must be a co-
signatory to transfer payments, pension scheme refunds, benefit payments (in non-pension form)
and other non-regular payments.

20.32 Where a small self-administered scheme is submitted for approval the trustees must give
written confirmation that the pensioneer trustee is a mandatory co-signatory to the scheme bank
accounts and co-owner of scheme assets. Where the confirmation accompanies the application it
must be in respect of all scheme bank accounts open, and all assets held by the scheme, at the
date of the application. Any such confirmation given at a later date must be in respect of all
scheme bank accounts open, and all assets held by the scheme at that later date.

20.33 Failure to meet the co-signatory and co-ownership requirements will lead to a small self-
administered scheme’s tax approval status being reviewed and possibly withdrawn. A small self-
administered scheme seeking approval will not be approved if it fails to meet the co-signatory and
co-ownership requirements.

FUNDING

20.34 An approved small self-administered scheme, like any other approved scheme, must comply
with the general funding principles set out in paragraph 13.1. The more specific requirements of
Part 13 are, however, qualified as described in paragraphs 20.35 to 20.44.

Actuarial reports

20.35 An approved small self-administered scheme is required to obtain an actuarial valuation of
its assets and liabilities at its inception and thereafter at intervals no greater than 3 years. A copy
of each actuarial report must be submitted to **IR SPSS** not later than one year from the effective
date of the valuation.

The requirement for the production and submission of an actuarial valuation report to **IR SPSS** on
small self-administered schemes stands until the scheme has completed winding up. If, however,
a scheme completes winding up within a year of the as at date of the actuarial valuation report in a
small self-administered scheme **IR SPSS** will be prepared to dispense with the actuarial valuation
report.
Contributions

20.36 No contributions are to be paid to the scheme unless justified by the latest actuarial report. It is not permissible to make contributions when money is available irrespective of the needs of the scheme (it is a popular misconception that a scheme may hold a general reserve equal to one year's Ordinary annual contribution).

Death benefits

20.37 All death benefits, insofar as they exceed the value of the member's interest in the fund based on his or her accrued pension and other retirement benefits, must be insured.

Purchase of annuities

20.38 To ensure that pensions from small self-administered schemes are pensions for life as required by paragraph 7.32, pensions should normally be secured from the outset by the purchase of an annuity from a life office. The annuity should be non-commutable and non-assignable. It may be purchased either in the name of the trustees or member. An annuity to secure a widow's/widower's/surviving civil partner's or dependant's pension (see paragraphs 20.42 and 20.43) may also be purchased in either the name of the trustees, or in the name of the widow/widower/surviving civil partner or dependant.

20.39 Annuity rates, however, do fluctuate and when the costs are high the immediate purchase of an annuity may not make economic sense. Rules may, therefore, provide:

- subject to paragraphs 20.40, 20.41, 20.51, 20.53, 20.56 and 20.62 for the purchase of the annuity to be deferred and the pension to be paid directly from the resources, or alternatively
- for the facility set out in Part I of Appendix XII to be adopted.

To the extent that pensions are so secured, post-retirement increases in respect of the secured pension must also be immediately secured. In the case of the second alternative, the requirements and conditions set out in Appendix XII must be applied.

20.40 Deferment of the purchase of annuities may not extend beyond the age of 75. The intention of allowing deferment is to provide scheme members with more flexibility in deciding the most opportune time to purchase the annuity rather than automatic deferral to age 75. Scheme members or survivors should be made aware of the importance of keeping the purchase of the annuity under review taking such professional advice as is considered necessary.

20.41 When pensions are paid directly out of scheme resources under paragraph 20.31 above, the scheme actuary must certify the amount of pension payable in accordance with the scheme rules and which can be maintained whilst taking account of:

(a) any contingent widow's, widower's, surviving civil partner’s or dependant's pension payable; and

(b) the scheme's income and assets, particularly those notionally underpinning the provision of the member's benefits.

This certificate should compare the pension with an annuity on the same terms that could be secured on the open market at that time with the funds available. Any divergences by more than 10% between the two amounts should be explained by the actuary. The amount of any unsecured pension in payment must form part of a scheme's triennial actuarial report. Certificates should be provided to IR SPSS with the next actuarial valuation report, or earlier on request.

20.42 Subject to paragraph 20.43 the purchase of an annuity to secure a widow's/widower's/surviving civil partner’s or dependant's pension payable on the member's death.
either while still in service or after retirement but before the member attains age 75, may be deferred until the earlier of the attaining by the widow/widower/surviving civil partner or dependant of age 75 or the date on which the deceased member would have attained age 75. As for deferral of members’ pensions, the need to purchase an annuity for a widow/widower/surviving civil partner or dependant should be kept under continuous review. The requirements set out in paragraph 20.41 will apply except that when a widow's/widower's/surviving civil partner's or dependant's pension is in payment (a) will not be relevant and the actuarial certificate will take account under (b) only of the scheme's investments and assets underpinning the provision of the widow's/widower's/surviving civil partner's or dependant's benefit. The initial certificate should compare the pension with an annuity that could have been purchased at the time of the member's death. Where the member dies in retirement on or after age 75, the widow's/widower's/surviving civil partner's or dependant's pension should be secured by the purchase of an annuity not later than the time of the member's death.

20.43 A prospective widow's/widower's/surviving civil partner's reversionary pension should be secured by the purchase of a contingent annuity at the same time as the member’s own pension is so secured. If, however, the pension is payable to whichever person is the member's spouse or civil partner when the member dies (i.e. the entitlement is not limited to the current spouse or civil partner at the time of retirement), its purchase may be deferred in accordance with paragraph 20.42 above.

20.44 Any cost of living increases granted in respect of a pension already secured in accordance with paragraphs above should be secured with a life office as soon as they are awarded. Where scheme rules provide for pension increases at a fixed rate of up to 3% per annum compound (paragraph 9.4(a)), the increases should be secured when the basic pension is secured.

INVESTMENTS

20.45 The Inland Revenue's interest in the investments of a small self-administered scheme flows from the statutory condition of approval that a scheme should be "bona fide established for the sole purpose of providing relevant benefits" (section 590(2)(a)). The concern is that tax exempt investments held for the provision of the scheme benefits should not be of a kind or used in such a way as to produce a non-relevant benefit for the beneficiaries or the employer.

Effect of Regulations

20.46 The SSAS Regulations contain requirements in relation to the power of the trustees of small self-administered schemes to:

(a) borrow money;
(b) hold certain assets as investments;
(c) lend money and purchase shares; and
(d) purchase, sell or lease assets.

The SSAS Regulations restrict the Board's discretion to approve such a scheme to one whose governing documentation contains requirements complying with those Regulations in relation to (a) - (d) above.

20.47 The only exception to paragraph 20.46 is where at the date, on which the SSAS Regulations were made, the scheme was in existence and either had not been submitted to the Board for approval or was before the Board awaiting approval. In these circumstances approval will not be precluded by reason of provisions in the scheme's documentation, which allow the trustees to retain as an investment of the scheme:

(i) personal chattels other than choses in action (see paragraph 20.75);
(ii) residential property other than is described in paragraph 20.72); or

(iii) shares in an unlisted company which carry more than 30% of the voting power in that company or entitle the trustees to more than 30% of any dividends declared by that company (see paragraph 20.80),

Provided that such an investment was held by the trustees prior to the date on which the Regulations were made and was acceptable under previous Inland Revenue discretionary practice. Similarly, a provision in the scheme's documentation authorising the trustees to:

(iv) continue to lend money or retain shares in an employer or any Associated Employer, where that money was being lent or the shares were being held prior to the date on which the SSAS Regulations were made and when the money was first lent or the shares were acquired, the scheme had been in existence for 2 years or less and the 25% restriction but not the 50% restriction described in paragraph 20.53 was exceeded; or

(v) sell assets held by them immediately before that date to a member of the scheme or to any person connected with a member of the scheme,

will not prevent approval being given. It should be noted, however, that in relation to (v), the sale must be on an arm's length basis at full market value.

20.48 It is a condition of approval that when actuarial reports are submitted to IR SPSS (see paragraph 20.35) they must be accompanied by a statement detailing how the funds of the scheme are invested. This enables the Inland Revenue to monitor whether the bona fides of the scheme are being maintained.

20.49 Regulation 5 of the Information Powers Regulations requires the scheme administrator to provide to the Board information and documents relating to certain transactions within a period of 90 days of the date of the transaction. Failure to comply may lead to the imposition of a monetary penalty on the scheme administrator under section 98 Taxes Management Act 1970. Continued failure to furnish the information may lead to withdrawal of approval under our discretionary powers contained in section 591B.

The types of transaction involved are:

(a) the acquisition or disposal of land including buildings and other structures;

(b) the lending of money to an employer or an Associated Employer;

(c) the acquisition or disposal of shares in an employer or an Associated Employer;

(d) the acquisition or disposal of shares in an unlisted company, NB an Open Ended Investment Company (OEIC) is not an unlisted company for the purposes of the Information Powers Regulations;

(e) the borrowing of money; and

(f) the purchase, sale or lease from or to an employer, or any Associated Employer, of any asset other than one as described in (a), (c) or (d).

The information and documents required are as may be specified on the relevant form - specimen copies are included in Appendix II.

The relevant forms are:

PS 7012 - for details of the acquisition or disposal of land (including buildings and other structures).

PS 7013 - for the lending of money to an employer or Associated Employer.
PS 7014 - for the acquisition or disposal of shares, in the employer, Associated Employers or unlisted companies.

PS 7015 - for the borrowing of money.

PS 7016 - for the purchase from, or sale or lease to an employer, or any Associated Employer, of any asset other than as described in (a), (c) or (d) above.

20.50 Apart from the requirements of regulation 5 of the Information Powers Regulations, when requested, Scheme administrators should provide full details of any transaction to IR SPSS. The following paragraphs contain details of the various restrictions which are imposed on scheme trustees by the SSAS Regulations in relation to their powers as described in (a) - (d) of paragraph 20.46 together with some guidance on Inland Revenue views and requirements on particular aspects of investment.

**General principle**

20.51 The Inland Revenue will not necessarily regard any form of investment as consistent with approval just because it is within the trustees' powers and not prohibited under the terms of the SSAS Regulations. In general the Inland Revenue do not interfere in the way trustees invest trust monies except:

(a) where tax avoidance is suspected; or

(b) where an investment appears to be irreconcilable with the bona fides of the scheme having regard to the sole purpose requirement and the scheme's cash needs for purchasing annuities.

For example, investment in land or buildings may be a good long-term investment when the members are many years from retirement but becomes less appropriate as their retirement approaches and, even if the purchase of a member's, widow's/widower's/surviving civil partner's or dependant's annuity is deferred, it is necessary to ensure that the scheme is in a position to buy an annuity between the ages of 70 and 75 without becoming involved in a forced sale of property. This is particularly so if the property purchased is an important part of the employer's own commercial premises and thus potentially difficult to realise.

**Loans to members and connected persons**

20.52 Regulation 6(1) of the SSAS Regulations prohibits scheme trustees from making loans to a member of the scheme or to any person, apart from an employer or any Associated Employer, who for the purposes of those Regulations is connected with a member of the scheme. For this purpose, “member of the scheme” includes members who are currently accruing benefits in the scheme as a result of service as an employee of a participating employer, deferred benefit members, pensioner members, pension credit members, other beneficiaries and former scheme members who are still in the service of a participating employer. Thus if a scheme is to be approved, its trust documents should specifically preclude loans to such individuals or persons. The reason why this prohibition is considered necessary in small self-administered schemes in particular is because of the possibility (arising from the less than arm's length relationship of all the parties) that such a loan would become, in reality, a charge on the retirement benefit, or that the pension scheme would be used in this way so as to avoid the tax liability arising on loans direct from a close company to its "participators".

**Self investment**

20.53 Regulation 7 of the SSAS Regulations restricts trustees' investment in loans to and shares in an employer company during the first 2 years from the date the scheme was established, to 25% of the market value of its assets which are derived from contributions made to it by an employer and the members since it was established. After the end of the 2 year period the figure increases to 50% of the market value of all the assets of the scheme.
For the purpose of applying the limits in regulation 7 of the SSAS Regulations, the market value of the assets excludes:

a) any portion of the funds notionally underpinning retired members', pension credit members', widows'/widowers'/surviving civil partners' or dependants' benefits in payment where the purchase of an annuity has been deferred (prospective widows/widowers/surviving civil partners of retired members or pension credit members in receipt of a pension, whose pensions must be secured at the same time as the retired members or pension credit members in accordance with paragraph 20.43 being regarded for this purpose as in receipt of a pension), and

b) any sums borrowed to purchase scheme assets which are outstanding at that time and any other liabilities incurred by the trustees which are outstanding at the time, other than liabilities to pay benefits under the scheme.

Within 5 years of the commencement of pensions to new pensioners, or on attainment by the pensioner of age 70 if earlier, the trustees must ensure an appropriate proportion of any loan to the employer or Associated Employer is repaid. Where the pensioner has already attained age 70 when payment of pension commences, repayment of the loan must take place immediately.

20.54 Where all members of the scheme have retired/taken their pension/died, no new loans or share purchases in the employer or associated employer will be permitted following the later of the first payment of the final retiring member's pension or the final pension credit member taking a pension and the first payment of the final widows/widowers/surviving civil partners' or dependant's pension (prospective widows/widowers/surviving civil partners of retired members or pension credit members in receipt of a pension, whose pensions must be secured at the same time as the retired members' or pension credit members' in accordance with paragraph 20.43 being regarded for this purpose as in receipt of pension). Existing loans and shares should be repaid or sold within 5 years of the commencement of such pension payments or on attainment by the pensioner of age 70 if earlier. If the pensioner has already attained age 70 when payment of pension commences, such repayment or sale must take place immediately. Where a scheme holds a policy or policies, including a unit linked policy or policies, as part of its assets, IRSPSS would regard an acceptable interpretation of the market value of such a policy or policies to be the surrender value (calculated on the same basis as a transfer value). In the context of regulation 7 of the SSAS Regulations investment means both loans to, and the purchase of shares in the employer company and any Associated Employer whether or not they participate in the scheme. The Inland Revenue also applies these limits in relation to loans to, or shares in, other persons connected with a scheme through a member (see paragraph 20.52), trustee or an employer. It is not possible to provide a comprehensive definition of a connected party in this context, but broadly it includes:

(a) an individual who is a business associate of a member of the scheme, or of a trustee or employer in relation to the scheme (see paragraph 20.52), or who is a relative of a trustee or employer;

(b) a partnership where one of the partners is connected as in (a) with a member of the scheme (see paragraph 20.52), trustee or employer; and

(c) a company in which a director or influential shareholder (i.e. one who controls 20% or more of the voting shares in the company) is connected as in (a).

20.55 An individual is connected with a corporate trustee or employer if he or she is a relative or business associate of any director or influential shareholder (as defined in (c) above) of the trustee or employer company. For practical purposes a "business associate" means a partner in a partnership, a fellow director of a company, or a fellow influential shareholder in a company. A director of a company is regarded as a business associate of an influential shareholder of the same company and vice versa. Forms PS 7013, PS 7014 and PS 7016 (headings suitably amended where necessary) should be used to provide details of loans to, shares (acquired and disposed of) in, or purchases, sales or leases from or to, connected parties other than an employer or Associated Employer. The required documentation should accompany the completed forms.
Subject to paragraph 20.53 and Department of Social Security legislation, a scheme may lend funds to an employer or any Associated Employer but if it is to be approved, regulation 6 of the SSAS Regulations requires that such lending may only be made for the purposes of the borrower's business (broadly an activity other than that of making or managing investments, except that a holding company is permitted to make or manage share investments in its 51% trading subsidiaries) and that the loan is:

(a) for a fixed term;

(b) at a commercial rate of interest; and

(c) evidenced by an agreement in writing which contains all the conditions on which it is made and provides for immediate repayment of the loan if the borrower:

(i) breaches the conditions of the agreement,

(ii) ceases to carry on business,

(iii) becomes insolvent, or

if repayment is required to enable the trustees to pay benefits which have already become due under the scheme. Where the purchase of an annuity has been deferred (see paragraph 20.39) the funds necessary to purchase the whole annuity must be regarded as required to pay benefits no later than 5 years after the commencement of the pensioner has already attained age 70 when payment of pension commences, the funds necessary to purchase the whole annuity must be regarded as required immediately.

The Inland Revenue will also expect these requirements to be met where a loan is made to connected persons other than an employer or Associated Employer as described in paragraph 20.54. The pensioner trustee must be a party to all loans made on or after 1 October 2000 – paragraph 20.22 refers.

Loans should not be of such an amount and frequency as to suggest that the employer is only partly funding the scheme while claiming a tax deduction for the total pension contributions. Regulation 6 of the SSAS Regulations requires that a loan must be for a fixed term. The length of the term is a matter for decision between the parties to the loan agreement but it should be realistic. It is not acceptable for a series of 364 day loans to be made when in reality the intention is that the employer will not repay the loan for, say, 3 years. Nor is it acceptable for the term to be longer than necessary - scheme funds should not lodge unnecessarily with an employer.

It is an Inland Revenue requirement that a commercial rate of interest (see paragraph 20.56) must be charged and paid. The commerciality of the interest will not be questioned if it is at least 3% above the Clearing Banks' Base Rate and an interest rate on this basis will be acceptable for both secured and unsecured loans. IR SPSS will be prepared to consider a lower rate of interest only if written evidence is produced demonstrating that the borrower can obtain a loan on similar terms from a bank or other arm's length financial institution at a rate below Clearing Banks' Base Rate + 3%.

Trustees/Administrator duties in respect of loans

Quite apart from the requirements of the SSAS Regulations, IR SPSS require scheme trustees to act in the best interests of scheme members in their capacity as scheme members and not as employees, shareholders etc. If they fail to do so IR SPSS are likely to take the view that the scheme is not being properly administered and that exempt approval should be withdrawn (see Part 19). Such action may be taken if the following responsibilities, in relation to loans, are not adhered to by the trustees/administrator:

(a) As a rule loans should not be made to an employer or any Associated Employer unless the trustees would be prepared to lend the same amount on the same terms to
an unconnected party of comparable standing. All the scheme trustees, other than the pensioner trustee, are therefore required to certify on the form PS 7013 that in the light of all the evidence before them, they are satisfied that the borrower's financial circumstances are healthy and that the loan is a prudent investment. IR SPSS are prepared to consider any other information that the trustees wish to submit with the PS 7013 to support their view that the loan is a prudent investment. Such information could be a copy of the borrower's most recent company accounts (together with any more recent management accounts);

(b) The scheme trustees should also ensure that where they lend money, the borrower fully honours the terms of the loan agreement. Trustees should ensure that they pursue the payment of any arrears promptly and effectively. The administrator is required, within 90 days of a loan default occurring, to notify IR SPSS in writing where the defaulted interest/capital has not been paid/repaid in the interim. Within a further 90 days of the default occurring the scheme administrator will be required to notify IR SPSS in writing of the steps the trustees have taken to recover the debt (including supplying copies of letters sent by the trustees and/or their legal or other representatives formally demanding repayment). A failure by scheme trustees to pursue loan arrears may jeopardise approval;

(c) Other responsibilities of the trustees include:

(i) ensuring that loans are not made solely to keep an ailing business afloat;

(ii) ensuring that loans are not made to employers who are technically insolvent; and

(iii) taking all available legal steps to enforce the repayment of a loan to an employer in the circumstances described in paragraph 20.56 (c).

20.60 The SSAS Regulations do not prohibit an outstanding loan from being "rolled over" into a fresh loan agreement. IR SPSS will not, however, agree to a loan being "rolled over" more than twice nor to it must satisfy the conditions described in paragraphs 20.53 – 20.58

Back to back loans

20.61 Any attempt to circumvent the ban on loans to members (see paragraph 20.52) and connected persons or the restrictions on loans to employers by entering into arrangements whereby the scheme loans money to an unconnected party on the understanding for instance that a similar loan will be made by that party (or an associate) to the employer or a member, will almost certainly lead to withdrawal of approval from the scheme(s) involved.

Borrowing

20.62 Trustees of schemes sometimes wish to borrow funds to enable them to acquire particular assets. Regulation 4 of the SSAS Regulations restricts trustees' borrowing so that at the time of any borrowing, the aggregate amount borrowed does not exceed the total of:

(a) three times the ordinary annual contribution paid by the employers;

(b) three times the annual amount of the basic or contractual contributions paid by the scheme members in the year of assessment ending immediately before the time of borrowing; and

(c) 45% of the market value of the assets of the scheme*.

* For the purpose of applying this limit, the market value of the assets excludes:

i) any portion of the funds notionally underpinning retired members' pension
credit members', widows'/widowers'/surviving civil partners' or dependants' benefits in payment where the purchase of an annuity has been deferred (prospective widows/widowers/surviving civil partners of retired members or pension credit members whose pensions must be secured at the same time as the retired members or pension credit members in accordance with paragraph 20.43 being regarded for this purpose as in receipt of benefits), and

ii) any sums borrowed to purchase scheme assets which are outstanding at that time and any other liabilities incurred by the trustees which are outstanding at the time, other than liabilities to pay benefits under the scheme.

20.63 Any borrowing in existence when a member retires or when a pension credit member's, widow's/widower's/surviving civil partner's or dependant's benefits come into payment (prospective widows/widowers/surviving civil partners of retired members or pension credit members in receipt of a pension whose pensions must be secured at the same time as the retired members or pension credit members in accordance with paragraph 20.43 being regarded for this purpose as in receipt of benefits) must be reduced to the levels set out in (c) above within 5 years of those events or on attainment by the pensioner of age 70 if earlier. If the pensioner has already attained age 70 when payment of pension commences, any reductions in borrowing to comply with the level set out in (c) above must take place immediately.

20.64 For the purpose of regulation 4 of the SSAS Regulations, ordinary annual contribution has a different meaning to that contained in the Appendix 1 glossary. For the purpose of regulation 4 it means the smaller of:

(i) the average annual amount of the contributions paid to the scheme by the employers in the 3 years ending at the end of the last scheme accounting period that immediately preceded the date of the borrowing or, where at that date the scheme had been established less than 3 years, the total amount of contributions paid to the scheme by the employers up to the time of the borrowing divided by the number of years since the scheme was established (a part of a year counting as one year), and

(ii) the amount of the annual contributions which, within the period of 3 years immediately preceding the date of the borrowing, an actuary has advised in writing would have to be paid in order to secure the benefits provided under the scheme.

20.65 Monies borrowed by trustees must be used to benefit the scheme. Thus if the borrowed monies are on-lent to the employer (or any Associated Employer) the trustees must receive a higher rate of interest than they have to pay to obtain the finance.

20.66 As an administrative relaxation, IR SPSS do not require notification of short term borrowings for a period not exceeding 6 months where the aggregate amount borrowed does not exceed the lesser of 10% of the market value of the fund or £50,000 and the borrowing is repaid at or before the due date. If, however, the borrowing or part of it is rolled over into a further term it must be reported.

**Purchase of assets from members, connected persons or an employer**

20.67 Regulation 8 of the SSAS Regulations prohibits the direct or indirect purchase by scheme trustees of an asset from a member of the scheme (see paragraph 20.52) or any person, apart from an employer or any Associated Employer, connected with a member of the scheme. For this purpose, the purchase of an asset by the trustees will not be regarded as being an indirect purchase from a member of the scheme or connected person if at the time of purchase 3 or more years have passed since the asset was owned by the member or connected person. Regulation 8 does not preclude the scheme trustees purchasing an asset from an employer or any Associated Employer but it requires that such purchase may only be made:

(a) after the trustees have obtained independent professional advice in writing, and
(b) in accordance with that advice.

20.68 Although the purchase of an asset from an employer or an Associated Employer is permissible, *IR SPSS* will need to be satisfied that it is consistent with the scheme's approval. *IR SPSS* should, whenever possible, be advised in advance of any such proposed transactions. *IR SPSS* will generally need to consult the appropriate Inspector of Taxes to determine whether tax avoidance is involved and whether the acquisition is part and parcel of a "transaction in securities" to which section 703 might apply. Trustees may wish to satisfy themselves that the vendors have obtained clearance under section 707 (from the Inland Revenue Compliance and Collection Division) before making such an acquisition. If such clearance cannot be given or if tax avoidance is involved, the transaction will not be consistent with the scheme's approval.

**Sale of assets to members, connected persons or an employer**

20.69 Subject to the exception explained in paragraph 20.46, regulation 8 of the SSAS Regulations prohibits the direct or indirect sale by the trustees of a scheme asset to a member of the scheme (see paragraph 20.52) or any person, apart from an employer or any Associated Employer, connected with a member of the scheme. For this purpose, the sale of a scheme asset by the trustees will not be regarded as being an indirect sale to a member of the scheme or connected person, if the purchase by the member or connected person took place 3 or more years after the sale by the trustees. Regulation 8 does not preclude the sale by the trustees of a scheme asset to an employer or any Associated Employer but such a sale may only be made subject to the conditions described in (a) and (b) of paragraph 20.67.

**Lease of assets to an employer**

20.70 Regulation 8 of the SSAS Regulations permits scheme documentation to provide for the lease by the trustees of scheme assets to an employer or any Associated Employer but only where the conditions described in (a) and (b) of paragraph 20.67 are satisfied. The pensioneer trustee must be a party to the documentation – paragraph 20.9 refers.

**Lease of assets to members or to connected persons**

20.71 Regulation 8 of the SSAS Regulations prohibits the trustees from leasing any scheme assets to a member of the scheme (see paragraph 20.52) or any person, apart from an employer or any Associated Employer, connected with a member of the scheme.

**Residential property**

20.72 Regulation 5 of the SSAS Regulations prohibits scheme trustees from investing in residential property other than:

(a) residential property which is, or is to be, occupied by an employee who is not connected with his or her employer and who is required as a condition of employment to occupy the property, or

(b) residential property which is, or is to be, occupied by a person, other than a scheme member or a person connected with a scheme member, in connection with that person's occupation of business premises (for example, a shop with an integral flat above) where those business premises are held by the trustees as a scheme asset.

In relation to (a) above, an employee is connected with his or her employer in circumstances where:

(i) the employer is a partnership and he or she is connected with a partner (viz. *is the partner's spouse or civil partner*, or is a relative, or the spouse *or civil partner* of a relative, of the partner or the partner's spouse *or civil partner*) in the partnership, or

(ii) the employer is a company and he or she or a person connected with him or her (viz. *in this context the spouse or civil partner*, or a relative, or the spouse or civil
partner of a relative, of the employee or the employees' spouse or civil partner) is, or at any time during the preceding 10 years has been, a controlling director of the company.

20.73 For the purposes of regulation 5 of the SSAS Regulations, the scheme trustees are not regarded as indirectly holding as an investment residential property other than as is described in (a) and (b) above where:

i) they hold as investment units in a unit trust scheme:
   - which is an authorised unit trust scheme within the meaning of section 468(6), or
   - where all the unit holders would be wholly exempt from capital gains tax or corporation tax (otherwise than by reason of residence) if they disposed of their units,

and the trustees of the unit trust scheme hold such property as an investment subject to the trusts of the scheme, or

ii) they hold as an investment subject to the trusts of the scheme a right which confers entitlement to receive payment of any rent charge, ground annual, feu duty or other annual payment reserved in respect of, or charged on or issuing out of, that property, and the property is not occupied by a scheme member or a person connected with a scheme member.

Holiday property

20.74 Investment by scheme trustees in holiday property is not regarded as being consistent with approval.

Pride in possession articles

20.75 Regulation 5 of the SSAS Regulations prohibits scheme trustees from investing in personal chattels other than choses in action (or, in Scotland, movable property other than incorporeal movable property). A "chose in action" is something which is not corporeal, tangible, movable or visible and of which a person has not the present enjoyment but merely a right to recover it (if withheld) by action. Examples of personal chattels which are prohibited investments include works of art, jewellery, vintage cars, yachts, gold bullion etc. Examples of choses in action which are permitted investments include company shares, copyrights, financial futures etc. If scheme trustees are uncertain as to whether a particular investment would be acceptable, they should consult their professional advisers before making the investment.

Shared investments

20.76 There is no objection in principle to a scheme joining with other parties to make a single investment (e.g. In a property) provided that the other parties do not include a member of the scheme (see paragraph 20.52) or any person, apart from an employer or any Associated Employer, connected with a member of the scheme. The trustees should not, however, allow any restriction of the scheme's freedom to realise its investment how and when it wishes. The pensioneer trustee must also be a party to the documentation – paragraph 20.8 refers.

Transactions between tax approved occupational pension schemes and non-approved (or "top up") schemes

20.77 Transactions of any description between any tax approved scheme and non-approved schemes are prohibited. This applies in respect of any transactions between

- tax approved schemes and non-approved schemes of the same employer, and
- tax approved schemes of one employer and non-approved schemes of another
employer – whether or not there is any connection between the employers or the schemes.

Non-approved schemes are generally retirement benefits schemes to which the provisions of sections 595 to 596C of the Taxes Act apply. Other than being a retirement benefit scheme, they do not have to adopt any particular form and there are no tax rules which govern their structure or the type, or amount, of benefits they provide.

Non-approved schemes are often known as

- FURBS (funded unapproved retirement benefit schemes)
- UURBS (unfunded unapproved retirement benefit schemes)

Non-approved schemes may also include pension schemes that

- lose tax approval – they become non-approved schemes from the effective date of withdrawal of approval
- are approved from a date later than their commencement date because of a late application for approval
- applied for approval but approval was refused.

20.78 The reason why transactions are not permitted is because there must be a clear demarcation between an employer’s tax approved scheme and non-approved schemes. Otherwise, a blurring of the monies/investments held for the purposes of approved and non-approved schemes could result in tax reliefs/exemptions subsidizing the unlimited benefit provision of a non-approved scheme. There is also the possibility that conditions that might apply to the assets held for the purposes of an approved scheme can be avoided by temporarily sheltering those assets in a non-approved scheme.

20.79 The following list gives examples of prohibited transactions between tax approved schemes and non-approved schemes. This list is by no means exhaustive.

- A loan from a tax approved small self-administered scheme to a non-approved scheme
  - Regulation 6(1)(a) of the SSAS Regulations has the effect of prohibiting direct or indirect loans to the members (and connected persons) of tax approved SSASs. An indirect loan could occur where the trustees of a SSAS make a loan to the trustees of a non-approved scheme set up for the benefit of the member (or connected person) of the SSAS. Paragraph 20.61 contains a prohibition on “back to back” loans.

- Tax approved SSASs selling assets to non-approved schemes
  - The effect of Regulation 8(1)(a) of the SSAS Regulations is to prohibit the trustees of a tax approved SSAS from directly or indirectly selling assets to members (or connected persons) of the SSAS. An indirect sale of an asset could occur by the setting up of a non-approved scheme in respect of the SSAS member and the SSAS trustees selling the asset to the trustees of the non-approved scheme.

- Joint investment between a tax approved SSAS and a non-approved scheme

The trustees of a tax approved SSAS are able to invest in a particular asset with other parties (such as syndicated property investment) provided the other parties do no include members of the SSAS or other persons connected with a member and provided also the nature of the investment is in itself unobjectionable. A joint investment with a member of the SSAS could occur by setting up
a non-approved scheme for the member of the SSAS and the trustees of the non-approved scheme entering into the joint investment on behalf of the member.

Trading

20.80 It is not necessarily inconsistent with approval for the trustees of a scheme to enter into trading activities but, as explained in paragraph 17.11, any profits are outside the protection of section 592(2). There have been, however, instances of scheme trustees either setting up a trading company or acquiring a controlling interest in such a company either directly or indirectly in order to convert non-tax exempt trading profits into tax exempt dividends. This is not consistent with approval and therefore regulation 5 of the SSAS Regulations prohibits scheme trustees from investing in the shares of an unlisted company which:

(a) carry more than 30% of the voting power in the company, or

(b) entitle the shareholder to more than 30% of any dividends declared by the company in respect of shares of the class held.

20.81 Where all members of the scheme have retired/taken their pension/died, no new investments in any stock or shares of any unlisted company will be permitted following the later of the first payment of the final retiring member's pension or the final pension credit member's pension and the first payment of the final widow's/widower's/surviving civil partner's or dependant's pension (prospective widow's/widower's/surviving civil partner's of retired members or ex spouse members in receipt of a pension, whose pensions must be secured at the same time as the retired members' or pension credit members' in accordance with paragraph 20.43 being regarded for this purpose as in receipt of pension). Existing stocks/shares should be sold within 5 years of the commencement of such pension payments or on attainment by the pensioner of age 70 if earlier. If the pensioner has already attained age 70 when payment of pension commences, such sale must take place immediately.

20.82 Where the scheme has both non-pensioners and pensioners, any portion of the funds notionally underpinning retired members', or pension credit member's, or widows', widowers', surviving civil partners', or dependants' benefits in payment where the purchase of annuity has been deferred must be excluded in determining the amount which may be used to buy stock or shares in any unlisted company. Within 5 years of the commencement of pensions to new pensioners or on attainment by the pensioner of age 70, if earlier, the trustees must ensure an appropriate proportion of the value of any stock or shares held in any unlisted company is sold. Where the pensioner has already attained age 70 when payment of pension commences, sale of an appropriate proportion of the stock/shares must take place immediately.

OTHER REQUIREMENTS

Serious ill-health commutation

20.83 An approved small self-administered scheme may not exercise any provision for full commutation of an employee's or pension credit member's pension on grounds of exceptional circumstances of serious ill health without the specific prior agreement of IR SPSS.

Employer in Liquidation

20.84 Scheme documentation should provide that, if an employer goes into liquidation without a successor, the scheme is to be wound-up or partially wound-up as appropriate. The proceeds are to be used in accordance with the documentation to purchase or transfer the accrued benefits. Any surplus is to be returned to the employer (see Part 13).

20.85 Alternatively, subject to scheme rules permitting, winding-up may be postponed and the scheme can continue as a paid-up scheme (see paragraph 14.4). The enabling provision must make such postponement subject to the agreement of the Board of the Inland Revenue and also subject to the such amendments or conditions as the Board may require.
20.86 The provisions allowing the scheme to continue must be in place before the employer goes into liquidation. If the employer that goes into liquidation is also the scheme administrator, the rules of the scheme should provide for a new administrator to succeed the liquidated employer.
Part 21. Centralised Schemes

Introduction

21.1 A scheme's documentation may contain provisions enabling more than one employer to participate. Where more than one employer participates the scheme is regarded as a centralised scheme. Each employer participating in the scheme must be under an obligation to observe the rules of the scheme. This condition is usually met by the employer being a party to the documents governing the scheme or undertaking the necessary obligations by a separate document. Centralised schemes fall into 2 very different categories and different requirements need to be satisfied if they are to be approved. The 2 categories are:

(a) schemes established to provide benefits solely for employees of associated employers and/or for employees of employers who are associated through a permanent community of interest, and

(b) schemes established to provide benefits for the employees of any employer, whether or not those employers are associated.

21.2 The rationale for centralised schemes is that they are able to provide a degree of expertise and lower administrative costs which would not be possible if each employer were to establish its own scheme.

Associated Employers

21.3 A centralised scheme for associated employers may adopt any method of funding (in accordance with Part 13) which would be acceptable for the scheme of a single employer. A centralised scheme for or including employers associated through a permanent community of interest may, in relation to employees of those employers, also fund on the basis which is acceptable for associated employers except in the case of controlling directors. The funding of benefits for controlling directors in such circumstances must be on the basis that each employer contributes only in respect of its own employees and these contributions should be related to the employees' salary and service with that participating employer.

21.4 A centralised scheme for associated employers may provide benefits for an employee (including a controlling director) by reference to his or her final remuneration from and aggregate service for the participating employers irrespective of moves from one to another as though they comprise one employer (but see paragraphs 7.20 and 7.21 in relation to controlling directors). A centralised scheme for or including employers associated through a permanent community of interest may, in relation to employees of those employers, also provide benefits on this basis except for controlling directors where benefit provision in respect of service and final remuneration with such employers must be calculated separately.

21.5 Where an employer is admitted to participation in a centralised scheme for associated employers and/or for employers associated through a permanent community of interest, the administrator is required under regulation 6 of the Information Powers Regulations (see paragraph 16.4 et seq.) to inform IR SPRS within a period of 180 days after the end of the scheme year in which the participation commences. Failure to comply may lead to penalties under section 98 Taxes Management Act 1970. Notification should be on a form PS 274, completed in accordance with the notes on completion PS 274(Notes), together with a copy of the Deed of Accession or other instrument binding the new employer to observe the scheme rules. Where a new principal employer is admitted, notification should be made on form PS 257. The Inland Revenue reserve the right to decline to approve any participation which is found to be unacceptable. Similarly, IR SPRS should be notified in the same way where changes occur which may have a bearing on the continued inclusion in the scheme of existing participating employers, e.g. arising from a change of status or residence. Such reports should be made on form PS 256.

21.6 The rules must provide for the withdrawal of an employer who ceases to be sufficiently closely...
associated with the others, or who goes out of business or who leaves the scheme for other reasons. This usually involves segregation and winding-up of the appropriate proportion of the scheme (see paragraph 14.10). If the departing employer is continuing in business, the segregated assets may be transferred to a new scheme set up by that employer or to another centralised scheme which it has joined. If the departing employer requires time to set up replacement pension arrangements, continued participation in the original scheme is acceptable for a period of up to twelve months provided the rules of the centralised scheme allow for this. In these circumstances, it is not necessary to approach the IRSPSS for agreement. During this period new employees of the departing employer may be admitted to membership of the scheme. Where, on the other hand, part of a participating employer’s business is sold to an employer outside the associated group, those employees who were transferred on the sale of the business may be retained in membership of the ‘old’ centralised scheme for a limited period whether or not their new employer formally adheres to the scheme (adherence may be necessary in order to preserve contracted-out employment). New employees of the new employer may not, however, be admitted to membership of the ‘old’ scheme.

21.7 A company or partnership formed as a joint enterprise by 2 or more parent companies may participate in a scheme established by any one of those parents, even though that parent has less than a 50% interest in it. In these circumstances the general principles set out in paragraphs 21.3 and 21.4 apply so far as funding and benefits are concerned.

21.8 Some groups of companies may designate one particular company to act as the employer for all the employees of the group. This service or management company then seconds employees to the various operating companies in return for a service fee covering pay and superannuation contributions. Any retirement benefits scheme set up by the service or management company is not a centralised scheme as described in this Part. The service or management company is the sole employer and consequently it is not appropriate for any of the other group companies to join the scheme.

21.9 An Associated Employer outside the United Kingdom may participate in an approved centralised scheme but only in respect of employees who are effectively chargeable to United Kingdom tax under Case I or II of Schedule E. Any service while not so chargeable is not pensionable under an approved scheme (see paragraphs 15.3, 15.5 and 15.7).

Non-Associated Employers

21.10 Many existing centralised schemes for non-associated employers fall within the category of "industry-wide" schemes which are usually sponsored by a professional or trade association and available only to employers in a particular industry. Other schemes are established on a commercial basis (e.g. by a life office) and are open for any employer to participate.

21.11 Schemes in either category can be approved with the minimum of restriction if they are established as simplified defined contribution schemes which comply with the requirements of Part 22 for automatic approval.

21.12 The Inland Revenue are also prepared to approve centralised schemes for non-associated employers which take the more conventional form where benefits, rather than just contributions, are limited. In general such schemes should follow simple straightforward lines to ease the problems of administration which can flow from the separation of the employer and the administrator. The quality of administration is very pertinent to the approval of such a scheme.

21.13 If, however, it is desired to set up such a scheme in more complex form, approval will not necessarily be precluded but it will be subject to more stringent conditions. Indeed the more complex the scheme the greater the necessary degree of regulation. The Inland Revenue will expect a particularly high level of compliance procedures (with suitably qualified staff to put them into effect) where schemes include any of the following features:

(a) provision for augmentation of benefits beyond 1/60th of final remuneration for each year of scheme membership,
(b) provision to allow investment to be subject to employer or broker control, or

(c) provision to allow membership of controlling directors.

21.14 The additional administrative requirements for the approval of a centralised scheme for non-associated employers are that:

(a) IR SPSS must be satisfied that the sponsor and its staff are suitably experienced and capable of administering a scheme of this type satisfactorily;

(b) on entry each participating employer must covenant to observe the scheme rules and IR SPSS must be advised of the admission and be supplied with a fully completed PS 274 together with a copy of the Deed of Accession or other instrument binding the new employer. In accordance with the Information Powers Regulations (see paragraph 16.4 et seq.) such notification to be made within a period of 180 days after the end of the scheme year in which the participation commences. Failure to comply may lead to penalties under section 98, Taxes Management Act 1970. Similarly, IR SPSS should be notified in the same way where changes occur which may have a bearing on the continued inclusion in the scheme of existing participating employers, e.g. arising from a change of status or residence. Such reports to be made on form PS 256 (see Appendix II).

(c) the scheme rules must preclude any self-investment or loans to the employers or the members;

(d) the scheme rules must specifically exclude from membership any employee who is accruing benefits under another scheme of the employer, except where:

(i) those benefits are accruing under another centralised scheme for non-associated employers which is a contracted-out money purchase scheme to which minimum contributions only are made and, provided that, the administration of both schemes is in the same hands and an assurance is given that there will be adequate liaison between the schemes to ensure compliance with limits etc, or

(ii) the benefits under the centralised scheme are well within Inland Revenue limits and the rules of the scheme contain no power of augmentation (the rules must, however, contain adequate aggregation of benefit provisions), or

(iii) benefits under the other scheme are limited to lump sum death in service benefits only and the lump sum death in service benefit under the centralised scheme cannot exceed twice final remuneration. In these circumstances IR SPSS will require to be satisfied that the aggregate benefit cannot exceed the limits set out in paragraph 11.2, or

(iv) benefits are accruing under a Free standing Additional Voluntary Contribution Scheme provided that the centralised scheme can assure IR SPSS of the adequacy of its administrative systems to cope, or

(v) benefits are accruing under a personal pension scheme to which only minimum contributions (as in (i) above) are made;

(e) the scheme should adopt a conventional normal retirement date within the age range set out in paragraph 6.6. It may, however, be possible for a scheme which is established exclusively for a category of employees to whom paragraph 6.7 applies, to be approved;

(f) the rules should make provision for the withdrawal of an employer and if the employer goes into liquidation, for the winding-up of the relevant part of the scheme; and

(g) the rules should be complete in themselves, they should not allow individual participating
employers to adopt their own special rules which qualify the general rules of the scheme. There is, however, no objection to the rules consisting from the outset of general rules together with a range of special rules from which the individual employer may choose on entry to the scheme. Any subsequent extension of the range of special rules would constitute an amendment to the scheme.

21.15 Normally the basis of funding will be that each employer provides benefits only for its own employees but the Inland Revenue will be prepared to consider the use of controlled funding where the employers accept that, taking one year with another, substantial cross subsidies will not occur.

21.16 As a matter of principle benefits payable under a centralised scheme should not exceed the maximum approvable under an employer's own approved scheme. Thus where an individual has been a member of the scheme in relation to service with more than one employer his or her scheme benefits should not be greater than the maximum approvable aggregate benefits payable had he or she been a member in succession of approved schemes of each of those employers i.e. other than for the employment ending with retirement, on the basis set out in paragraphs 10.9 - 10.18. This successive slice method of calculating benefits is both complicated and requires detailed records to be kept of service and final remuneration in respect of each period of scheme membership. It may well be the case that the basis for calculating the maxima in relation to the different employments will vary i.e. the member may be entitled to Pre 17 March 1987 and/or pre 1 June 1989 continued rights in respect of earlier periods of membership. In particular the final paragraph of the definition of pre 1 June 1989 continued rights must be borne in mind.

21.17 The Inland Revenue are content for schemes to provide total benefits calculated by reference only to total service for participating employers and ultimate remuneration (i.e. final remuneration in respect of the member's last period of scheme employment). The maximum benefit so calculated must not exceed 1/60th of ultimate remuneration for each year of relevant service. This limit should take into account any benefits provided for the member under any other schemes of the participating employers. This does not apply to the calculation of lump sum benefits which must be limited by reference to the successive slice method described in paragraph 21.16.

21.18 The rules of a centralised scheme for non-associated employers should normally incorporate a limits rule which restricts total benefits on retirement to a pension of 1/60th of ultimate remuneration for each year of total relevant service (up to 40 years) or such greater amount (calculated in accordance with paragraph 21.16) as may be specifically agreed by the Board. The lump sum benefits however, should be limited in the rules as explained in paragraph 21.17 and provided on the basis of 3/80ths of final remuneration from the employer in question for each year of service with that employer, although as for total benefits, provision may be made for such greater amount (calculated in accordance with paragraph 21.16) as may be specifically agreed by the Board. Otherwise a rule which specifies calculation of all benefits on the successive slice basis may be acceptable if IR SPSS are satisfied that it will always produce the correct result.

21.19 Where the trust provisions of a centralised scheme for non-associated employers allow the employer to control the investment policy in relation to the funding of benefits for its employees the investment powers must be restricted to investment in:

(a) stocks and shares quoted on the United Kingdom Stock Exchange including securities traded on the Unlisted Securities Market;

(b) stocks and shares traded on a recognised overseas stock exchange;

(c) unit trusts and investment trusts;

(d) insurance policies including managed funds and unit-linked funds;
(e) deposit accounts; and

(f) commercial property (subject to paragraph 21.14(c)).

21.20 A centralised scheme which is self-administered, provides benefits on a money purchase basis and admits controlling directors is to be treated as a small self-administered scheme and must meet the special requirements of Part 20 including the appointment of a pensioneer trustee. In these circumstances IR SPSS will expect the scheme's governing documentation to satisfy the requirements for small self-administered schemes generally, although where in the case of a particular participating employer, it is clear that the special requirements of Part 20 would be inappropriate because, for example, that particular employer's participation does not involve controlling directors, IR SPSS will be prepared to waive all or any of the requirements of Part 20 so far as that particular participation is concerned.

21.21 The Inland Revenue will be prepared to consider all proposals to establish centralised schemes for non-associated employers on their merits. IR SPSS should be consulted as soon as the sponsoring body is in a position to explain the main features of the proposed scheme.

**Continued Rights**

21.22 Where a centralised scheme for non-associated employers or for employers who are not associated was approved before 27 July 1989, those members of the scheme with pre 1 June 1989 continued rights who change participating employers without leaving the scheme, remain entitled to those continued rights provided the employer to whom they move, commenced to participate in the scheme before 14 March 1989.

21.23 Where a scheme as described in paragraph 21.22 is approved on or after 27 July 1989, those members with pre 1 June 1989 continued rights lose those rights if they move on to the employment of another participating employer in the scheme.

21.24 Paragraphs 21.22 and 21.23 do not apply where the participating employers are associated. In these circumstances where a member with pre 1 June 1989 continued rights changes participating employers without leaving the scheme, entitlement to those rights is retained.

**Abandonment of Participation**

21.25 There should be provision in the rules of a centralised scheme for an employer to withdraw from participation (see paragraphs 21.6 and 21.14(f)). If a participating employer wishes to abandon/cancel that participation from the start this will be possible only within the principles set out in paragraph 14.14 (centralised scheme not approved) and paragraph 14.15 (centralised scheme approved).
Part 22. Simplified Defined Contribution Schemes

General

22.1 Prior to 1 April 2001 the Board exercised its discretion under section 591 to approve retirement benefits schemes which provided benefits limited only by the rate of contributions to be paid. Such schemes which meet these requirements of this part are known as simplified defined contribution schemes (SDCS). With effect from 1 April 2001 the Board will not consider new applications for approval for such schemes. Existing approved SDCS will not be affected. Applications for employers to participate in a SDCS approved before 1 April 2001 will be considered in the normal way (see Part 21).

22.2 A simplified defined contribution scheme may be used for contracting-out of the State Earnings Related Pension Scheme under the terms of Memorandum No 93 (Money Purchase Contracting-Out).

Sole purpose

22.3 The sole purpose of a simplified defined contribution scheme must be the provision on a money purchase basis of relevant benefits. In the first instance these benefits must be for and in respect of employees. However, such a scheme may also provide relevant benefits on this basis to the ex spouse and/or former civil partner of an employee member where that employee’s benefits in the scheme are subject to a pension sharing order.

22.4 It is not permissible to guarantee benefits at a level determined by reference to final salary. A simplified defined contribution scheme set up solely to provide death benefits will not be approved.

Membership

22.5 An employee may not accrue benefits concurrently under a simplified defined contribution scheme and another scheme or arrangement of the employer or an Associated Employer other than one providing benefits only on death. This requirement does not, however, preclude a member of a simplified defined contribution scheme from contributing to a Free standing Additional Voluntary Contribution Scheme. An employer may establish more than one simplified defined contribution scheme.

22.6 The rules of a simplified defined contribution scheme must exclude from membership any controlling director, any director or employee of a service company associated with a partnership of whom the director or employee is, or was, a partner and, the spouse or civil partner of a sole proprietor, partner or controlling director.

Temporary absence

22.7 If an employee is seconded to a non-resident employer (see paragraph 15.9 et seq.) contributions by or for that employee must cease for the duration of the secondment. An employee who is temporarily absent within the United Kingdom may remain a member if he or she satisfies the requirements of paragraphs 3.12 to 3.15.

Split scheme

22.8 The Board will not exercise discretion under section 611(3) to treat a simplified defined contribution scheme as being 2 or more separate schemes for tax approval purposes.

Contributions

22.9 Contributions to a simplified defined contribution scheme may consist of contributions paid by the employer and employee but the total contributions (including any made to a Free standing Additional Voluntary Contribution Scheme) must not exceed 17.5% of the member’s remuneration.
in any year of assessment. For this purpose age related rebates (that is, the excess over the flat-rate percentage rebate) made under the Social Security (Reduced Rates of Class 1 Contributions and Rebates) (Money Purchase Contracted-out Schemes) Order 1996 (SI 1055/1996) may be ignored for the purposes of the 17.5% limit. Similarly, contributions to a death benefit scheme of the employer are not required to be taken into account for the purpose of this limit nor are minimum contributions to a personal pension scheme where a member is not in contracted-out employment by reference to the simplified defined contribution scheme.

22.10 The aggregate of the member's own contributions (including his or her share, if any, of the minimum payment for contracting-out) in a year of assessment must not exceed 15% of his or her remuneration for that year. The only exception being as set out in (a) of paragraph 4.4. Any contributions made by the employee to a death benefit scheme of the employer must be taken into account for the purpose of this limit. Minimum contributions to a personal pension scheme are not contributions for this purpose.

22.11 The maximum amount of contributions in respect of an employee that may be made in any year to secure benefits payable on that employee's death before retirement is 5% of the employee's remuneration for that year. Minimum payments for contracting-out may not be used for this purpose.

22.12 For the purposes of this Part remuneration is subject, where appropriate, to the permitted maximum.

22.13 The employer must contribute to any simplified defined contribution scheme which provides benefits for its employees (i.e. paragraph 5.1 applies).

Benefits

22.14 Benefits, other than those derived from Protected Rights, from a simplified defined contribution scheme may be taken on retirement at any time between attaining age 50 and attaining age 75. Any proposal to adopt a specific age or spread of ages outside this range is not acceptable except that earlier retirement on grounds of incapacity is permissible. It is not a requirement that the rules of a scheme should stipulate a normal retirement date. Where, following a pension sharing order, an ex spouse or former civil partner is given membership of a simplified defined contribution scheme, pension credit rights may be paid in accordance with paragraphs 6A.2 - 6A.4.

22.15 The maximum benefit limits set out in Parts 7, 8, 11 and 12 do not apply to benefits emerging from a simplified defined contribution scheme, though any other approved scheme providing benefits in respect of service with the employer will need to apply the requirements for aggregation (paragraphs 7.25 - 7.27 and 8.10) to the benefits from a simplified defined contribution scheme.

22.16 The benefits payable from a simplified defined contribution scheme on retirement should be in the form of a pension (part of which may be taken as an immediate lump sum - see paragraph 22.21 below) for the member payable for life either with or without contingent pension(s) for the widow, widower, surviving civil partner and/or dependants (see paragraph 22.27 below). Benefits from any Protected Rights Fund must be paid in accordance with the requirements of Memorandum No 93. These same general principles apply to the payment of pension credit rights where pension credit member's are given scheme membership.

22.17 A simplified defined contribution scheme which is not contracted out can also offer the annuity purchase deferral income drawdown facility explained in Appendix XII. For further information regarding the general requirements and conditions, please refer to this Appendix.

22.18 Continued life cover may be provided only on retirement on grounds of incapacity and should cease no later than the attainment of age 75, or where a normal retirement date is stipulated such date. Protected Rights may not be used for this purpose.
Pension increases

22.19 Pensions payable under a simplified defined contribution scheme may be increased each year by the greater of 3% or the rise in theRetail Prices Indexfor that year.

22.20 Pension derived from Protected Rights must increase in line with orders made under the relevant DSS pensions legislation. Such orders are based on the lesser of 3% per annum compound or the annual increase in the Retail Prices Index.

Lump sum benefits and commutation

22.21 On retirement the employee may receive part of his or her benefits in the form of a tax-free lump sum. The lump sum must not exceed 25% of the total value, at the time of payment, of the aggregate retirement benefits provided for the employee (i.e. excluding the value of any contingent pensions payable on his or her death) by the scheme and by any Free standing additional voluntary contribution schemes in respect of the service pensioned through the simplified defined contribution scheme. For members with pre 1 June 1989 continued rights the lump sum must not exceed £150,000, or such other sum as may be derived from an order made by the Treasury under section 590(3). Benefits from transfer payments received, except from a Free standing additional voluntary contribution scheme in respect of the same service as pensioned through the simplified defined contribution scheme, do not count for the purpose of the 25% calculation. An additional lump sum may be paid from such transfer payments to the extent certified by the transferring scheme (see paragraph 16.17) and the amount so certified may be increased in proportion to the increase in theRetail Prices Indexsince the date of transfer. Where following a pension sharing order, an ex spouse or former civil partner is given membership of a simplified defined contribution scheme, he or she may, subject to paragraph 6A.5, receive a tax free lump sum in accordance with paragraph 6A.8.

22.22 If the scheme is used for contracting-out, the value of the (notional) immediate benefits which could be paid to the employee from the Protected Rights assets as at retirement after making allowance for a qualifying widow’s or widower’s or surviving civil partner’s benefit, may be taken into account when determining the maximum lump sum in accordance with paragraph 22.21. The pension derived from Protected Rights however may be commuted only in the limited circumstances set out in Memorandum No 93.

22.23 Full commutation of pension for reasons of exceptional circumstances of serious ill-health or triviality is permissible subject to the restrictions relating to Protected Rights.

Benefits before retirement

22.24 The option in paragraph 7.44 available to a member with continued rights continuing in service after normal retirement date, to take the pension and/or lump sum while deferring the remaining benefits to actual retirement (or age 75 if earlier) may not be provided unless the rules include a specified normal retirement date below age 75.

22.25 In relation to a member in contracted-out employment who has exercised the option described in paragraph 22.24 it is acceptable for minimum payments to continue to be made until state pension age.

22.26 On the death of an employee or a pension credit member (where ex spouses or former civil partners are given membership following a pension sharing order - see also paragraph 6A.9) before the payment of any retirement benefits, the funds available in respect of the member may, subject to any contracting-out requirements, be used to provide:

(a) a lump sum (see paragraph 11.5),

(b) pension(s) for the surviving widow, widower, surviving civil partner and/or any other dependants (see paragraph 11.9), or

(c) a combination of (a) and (b).
Pensions under (b) may not be guaranteed for a minimum number of years except in accordance with requirements relating to Protected Rights.

**Benefits in other circumstances**

22.27 The benefit payable from a simplified defined contribution scheme on the death of a member after retirement or on the death of an pension credit member after pension credit benefits have come into payment, should be in the form of pension(s) for the widow, widower, surviving civil partner and/or dependants (see paragraph 22.16). The payment of widows’ or widowers’ or surviving civil partners’ benefits from a member’s Protected Rights Fund should be made in accordance with the requirements of Memorandum No 93.

22.28 Widows’, widowers’, surviving civil partners’ and dependants’ pensions may commence on the employee’s death or, where ex spouses or former civil partners are given membership, the pension credit member’s death, and continue for life irrespective of any later change in the beneficiary’s circumstances. If desired, however, a widow’s or widower’s or surviving civil partner’s pension may cease on remarriage or forming a civil partnership or cohabitation. A pension for a child must cease when the child ceases to be a dependant. Widows’, widowers’, surviving civil partners’ and dependants’ benefits may be guaranteed for up to 5 years in accordance with requirements relating to Protected Rights.

22.29 Lump sum benefits are not permissible on death in retirement other than a lump sum payable under continued life cover (see paragraph 22.18), or in the case of a contracted-out simplified defined contribution scheme, in the circumstances set out in the final paragraph of paragraph 12.1, or under a guarantee attaching to the member’s pension. Such a guarantee may not be for a period in excess of 5 years.

22.30 On leaving pensionable service the options described in paragraphs 10.2 and 10.8 are available to a member of a simplified defined contribution scheme but the form of benefits must remain subject to paragraphs 22.15 - 22.29.

22.31 Transfers may be made or accepted by a simplified defined contribution scheme in accordance with paragraphs 10.21 - 10.26. A transfer value received should be applied to provide additional benefits in accordance with paragraphs 22.15 - 22.21. Paragraphs 10.39 - 10.41 may also be relevant.

22.32 On the termination of a simplified defined contribution scheme a member will become entitled to benefits on the same basis as on leaving pensionable service. The winding-up rule may permit trivial pensions (see paragraph 8.12 et seq.) to be commuted.

22.33 If on discontinuance Protected Rights are extinguished by the payment of a Contracted-out Protected Rights Premium and additional payments are required to buy the member fully back into SERPS, the additional payment will not qualify for tax relief under section 592.

**Centralised schemes**

22.34 Centralised schemes for associated employers, employers associated through a permanent community of interest (see paragraph 21.1), or for non-associated employers may be set up under this simplified procedure for tax approval using simplified defined contribution scheme model documents (see paragraph 22.3). Where an employer is admitted to participation in a centralised scheme which has been set up under this procedure, the general principles set out in paragraph 21.5 apply except that a fully completed form PS 403 should be provided. A specimen of this form is included in Appendix II.

**Funding**

22.35 Contributions to a simplified defined contribution scheme which is not used for contracting-out must be applied as premiums under a policy or contract of insurance, or invested with a building society, bank or authorised unit trust.
22.36 Contributions to a contracted-out simplified defined contribution scheme may be invested in the assets permitted by the Money Purchase Contracted-out Schemes Regulations 1987 (SI 1987 No 1101). Irrespective of the number of members such schemes are not subject to the special requirements for small self-administered schemes (see Part 20).
Part 23. Ex Gratia Relevant Benefits

General

23.1 It is the view of the Inland Revenue following legal consideration that an arrangement by an employer to pay ex-gratia relevant benefits to an employee constitutes a retirement benefits scheme as defined in section 611.

23.2 An arrangement in this context includes not only any prior formal or informal understanding with the employee but also any system, plan, pattern or policy connected with the payment of a gratuity. Examples of such arrangements include:

(a) a decision at a meeting to make an ex-gratia payment on an employee's retirement; or

(b) where, say, a personnel manager makes an ex-gratia payment under a delegated authority or on the basis of some outline structure or policy; or

(c) where it is common practice for an employer to make an ex-gratia payment to a particular class of employee.

It is not necessary for the employee concerned to have been involved in, or made aware of, the decision by the employer to pay an ex-gratia Relevant Benefit in order for an arrangement to exist.

23.3 There may be some exceptional situations where a gratuity is not paid under an "arrangement". The position in individual cases can be determined only on their facts. If an employer is unsure whether a gratuity is paid under an arrangement, advice may be sought in writing from the Technical Support Section of IR SPSS. Any such request should give full details of the circumstances in which the gratuity is to be paid.

23.4 The only ex-gratia payments affected are those which come within the definition of relevant benefits in section 612(1). In broad terms this covers pensions, lump sums, gratuities and similar benefits which are, or will be, given:

(a) where a person retires or dies; or

(b) in anticipation of retirement; or

(c) after a person has retired or died (if the reason for payment is in recognition of past service); or

(d) as compensation for any change in the conditions of a continuing employment (as distinct from compensation on loss of employment).

23.5 The most common situations will be:

(a) ex-gratia payments made on retirement or death (or in anticipation of retirement) by an employer who has no tax-approved pension scheme in respect of the employment;

(b) ex-gratia payments made on retirement or death (or in anticipation of retirement) for an employee where benefits also arise under a tax-approved pension scheme in respect of the employment (this will probably be the case where the benefits are taken at the scheme’s specified retirement age or on voluntary early retirement), or

(c) other ex-gratia payments (not being for reasons of redundancy or compensation for loss of office) which are made in anticipation of retirement.

23.6 It is likely that the last of these situations could be in point where an ex-gratia payment was made shortly before the employee was planning to retire. Careful consideration of the facts will be necessary before deciding on what the appropriate tax treatment might be.
23.7 Approval will not be given to an arrangement for paying an ex-gratia lump sum where the employee is already a member of the employer’s tax-approved pension scheme. Nonetheless, where the benefits fall short of the normal tax approval limits, the employer could (instead of making an ex-gratia payment to the employee or a dependant) pay a special contribution to the approved scheme so that the benefits it pays may be increased (within the tax approval limits).

**Excluded payments**

23.8 Severance payments on genuine redundancy or loss of office are not relevant benefits within section 612(1). In this regard it is not necessary to distinguish between ordinary employees and directors or senior executives. In each case, provided the reason for the ex-gratia payment is to compensate for loss of employment it will not be a Relevant Benefit. The same is true of severance payments which are made in order to compensate for an employee's loss of health.

23.9 In looking at the reason for the ex-gratia payment no account will normally be taken of contemporaneous payments under other arrangements. For example, the fact that on being made redundant, the employee is given early retirement benefits from an approved scheme will not necessarily affect the nature of the ex-gratia redundancy benefits.

23.10 Disability benefits (whether regular payments or lump sums) are not relevant benefits as defined if they are payable solely because of an employee's death or disablement by accident.

23.11 Tax approval will not be granted to ex-gratia relevant benefits which are paid prior to an employee's retirement. In the case of directors, approval will not be granted until such time as the person’s directorship has been relinquished.

**Applications for approval**

23.12 It is no longer necessary for approval purposes for benefits to be contractual. Approval may be given to an ex-gratia lump sum payment provided that it:

(a) is the only Relevant Benefit potentially payable to the employee in respect of the employment; in other words the employee should not be a member of either of the following:

(i) a retirement benefits scheme that is either approved or is being considered for approval, or

(ii) a relevant statutory scheme,

unless the payment is made on retirement and the scheme provides benefits only on death-in-service; and

(b) satisfies the normal requirements for tax-approval of a retirement benefits scheme.

23.13 A separate application form (PS 60) should be used for each ex-gratia lump sum payment for which approval is sought. Supplies of these forms are available from IR SPSS (see Appendix II).

23.14 As a work saving measure, an arrangement to pay a single ex-gratia lump sum Relevant Benefit to a particular employee need not be submitted for approval where:

(a) the conditions at paragraph 23.12(a) above are satisfied, and

(b) the total of all lump sum payments from all associated employers made in connection with the retirement or death do not exceed one-twelfth of the permitted maximum for the year of assessment in which the payments are made.

In these cases the payments will be treated as from an approved retirement benefits scheme and
no application to *IR SPSS* will be necessary.

**Non-approved arrangements**

23.15 Not all ex-gratia *relevant benefits* will attract approval. Some ex-gratia payments will, therefore, need to be treated as non-approved *retirement benefits schemes*. They will attract the same tax treatment as payments from contractual non-approved “top-up” schemes.

**Statement of Practice SP 13/91**

23.16 This Part reiterates and amplifies the Inland Revenue's views on ex-gratia payments as published in the Statement of Practice SP 13/91.
CONVERTING AN EXISTING APPROVED RETIREMENT BENEFITS SCHEME

24.1 Since 1 October 2000, certain approved retirement benefits schemes may apply to convert to a personal pension scheme.

In converting, the scheme adopts the conditions for tax approval for personal pensions in its entirety (i.e. on funding, contribution limits, benefits, membership, etc) as set out in IR 76 (2000).

If a conversion application is approved, the scheme will be given fresh approval by IR SPSS as a personal pension scheme under Chapter IV of Part XIV of ICTA 1988, subject to certain conditions (see paragraphs 24.21-24.30 below).

24.2 A converting scheme will not have been granted an approval date under Chapter IV earlier than 6 April 2001, and will continue to operate as a retirement benefits scheme under Chapter I until its Chapter IV approval date.

The proposed date of change of approval (see paragraph 24.22 (e)) should therefore be a future date, allowing time for the approval process to take place, and from which the employer will realistically be in a position to change the method of giving tax relief on employees' contributions (see paragraph 4.3a), as this change must take place as soon as Chapter IV approval takes effect.

24.3 Existing members of the converting scheme may have arranged to make voluntary contributions to a Free Standing Additional Voluntary Contribution Scheme, alongside the Chapter I scheme. Once the employer's scheme has converted to Chapter IV approval the member will no longer be able to contribute to the Free Standing Additional Voluntary Contribution Scheme, other than as described in paragraph 4.8 of the FSAVCS Guidance Notes (IR12 Supplement). The employer should therefore inform employees that they are applying for Chapter IV approval for the scheme and that this will mean any Free Standing Additional Voluntary Contribution Scheme contributions being made by employees will have to stop.

24.4 If the scheme wishes to become contracted-out of the state earnings-related pension scheme (SERPS) for the first time at the time of conversion, a separate election must be made to the IR SPSS for a certificate allowing them to do so. If the scheme is already contracted-out, it should nonetheless notify the Contracted-out Employments Group (COEG) of the Inland Revenue’s National Insurance Contributions Office of the change unless it is applying for registration as a stakeholder pension scheme, in which case the contracting-out application may be made to IR SPSS as stated at paragraph 24.5.

24.5 If the converting scheme wishes to become a stakeholder pension scheme, the trustees must also apply to the Occupational Pensions Regulatory Authority (Opra) for stakeholder registration. The two applications will be considered at the same time. Stakeholder registration will only be given if both applications are successful (see paragraph 24.37).

Whether such a scheme is already contracting-out prior to conversion or not, if it is to contract out as a stakeholder pension scheme, a fresh election must be made to IR SPSS. A stakeholder Employer Contracting-out Number (ECON) will be allocated, and the scheme will be supervised by IR SPSS rather than COEG.

WHICH SCHEMES MAY CONVERT - GENERAL

24.6 A converting scheme must:

- be a retirement benefits scheme,
- be approved under Chapter I of Part XIV of ICTA 1988,
be an occupational pension scheme for the purposes of section 1 of the Pension Schemes Act 1993/section 1 of the Pension Schemes (Northern Ireland) Act 1993,

be a money purchase scheme (section 181 Pension Schemes Act 1993/section 1 Pension Schemes (Northern Ireland) Act 1993,

adopt suitable rules for a personal pension scheme, and

satisfy the valuation conditions (see paragraphs 24.22 - 24.30).

24.7 Converting schemes must appoint a pensioneer trustee if the scheme at any time mirrors the description of a SSAS in regulation 2 (1) of the Retirement Benefits Schemes (Restriction on Discretion to Approve) (Small Self-administered Schemes) Regulations 1991 [SI 1991 No 1614 as amended by SI 1998 No 728].

24.8 If the member is in receipt of all or part of their benefits from the scheme as approved as a retirement benefits scheme, then unless their rights under the scheme have been secured by the purchase of an annuity by the date of conversion, that member may not be included in the converting scheme.

REQUIREMENTS FOR PARTICULAR TYPES OF RETIREMENT BENEFITS SCHEMES

Defined benefits schemes

24.9 Defined benefits schemes will have to become money purchase schemes prior to the conversion application being made.

Simplified defined contribution schemes

24.10 Schemes which are simplified defined contribution schemes mentioned in Part 22 are not required to satisfy the further conditions described in this Part. Their application may be made without surplus checks, valuations or trustees’ statements on allocation of assets.

Common trust funds

24.11 Schemes operating as common trust funds must review their structure to ensure that, as a personal pension scheme, they are able to identify the assets held for each member as necessary, and allocate assets accordingly (see paragraph 24.27). Such allocation may be notional.

Scheme documentation

24.12 The converting scheme must have, immediately prior to the date of change of approval, rules which fully comply with the requirements for approval as a retirement benefits scheme at that time, ie all necessary rule amendments have been incorporated. This is to ensure completeness and certainty of the pre-conversion provisions.

Scheme investments

24.13 The converting scheme must hold as assets at the date of conversion only assets which are acceptable as a personal pension scheme.

If it is intended to convert the scheme to a stakeholder pension scheme, the assets must also comply with the provisions of the Stakeholder Pension Schemes Regulations 2000 [SI 2000 No1403, as amended].

Partial conversion

24.14 Trustees may apply to regard a scheme as having two parts and retain approval as a retirement benefits scheme for one part, and obtain approval as a personal pension scheme for the other (subject to paragraph 24.15). This may happen, for example, where some members do not
wish their benefits to become subject to the personal pension rules. The scheme must be able to identify at any time the part of the scheme to which a member belongs.

Following a successful application, the scheme will be treated by IR SPSS as two different schemes, approved under Chapters I and IV respectively.

An individual may be a member of both of the separately approved parts. This may happen, for example, when someone has rights as an employee in one scheme and pension credit rights in the other. Or when someone has rights relating to different parts of their career, or a member is entitled to concurrent membership of Chapter I and Chapter IV schemes.

**NB** Member contributions to the retirement benefits scheme will be paid gross using the net pay arrangement (see paragraph 4.3). Member contributions to the personal pension scheme will be made net of basic rate income tax under the relief at source method (see paragraph 4.3A).

24.15 It is not possible to convert part of a retirement benefits scheme to a stakeholder pension scheme, as the stakeholder minimum requirements must relate to the whole scheme. If an employer wishes to have both a retirement benefits scheme and a stakeholder pension scheme, it will be necessary to set up a new scheme for both tax approval as a personal pension scheme and registration by the Opra as a stakeholder pension scheme.

**Surplus Funding**

24.16 Where a scheme is wholly converting, the conversion will take the form of a transfer of the fund. But the transfer will not be subject to the conditions of the Personal Pension Schemes (Transfer Payments) Regulations 2001. Instead, particular members will be subject to a funding check as stated in paragraph 24.23. The scheme will not be required to certify that it is not in surplus as a whole in relation to the conditions described in Part 13, but it should nonetheless ensure that any surplus funding is removed prior to conversion, since any reduction of a surplus by means of a payment to the scheme administrator of the personal pension scheme would prejudice the tax approval status.

24:17 The converting scheme must ensure that all regular actuarial valuations required on the scheme under Chapter I legislation have been carried out and submitted to IR SPSS by the due date, in relation to due dates which fall prior to the date of change of approval.

The legislation on conversion does not include provisions about how the views of members are sought in the process of a scheme reaching a decision whether to convert. This is a matter for the employer, the scheme trustees and the scheme administrator.

**Can a scheme convert back?**

24.18 No. The conversion is irrevocable, and there is no legal provision for any personal pension scheme to convert to a retirement benefits scheme for approval under Chapter I.

**New Chapter IV part to an otherwise unchanged scheme**

24.19 An existing approved retirement benefits scheme may keep the existing part intact but create a new section of the scheme, and apply for approval under Chapter IV for the new section. This is not a conversion as no members nor funds need to be moved between the sections.

**New Dual Approved Schemes**

24.20 An entirely new scheme may be established with two sections, one for approval as a retirement benefits scheme under Chapter I and one as a personal pension scheme under Chapter IV, both of which will apply separately for approval.

The result will be that the scheme receives two letters of approval, one for each section of the scheme (dual approval). Each part scheme will have its own date of approval, which may be different from that of the other part scheme.
HOW TO APPLY FOR APPROVAL FOR OR DUAL APPROVAL

24.21 The trustees/scheme administrator must:

- identify which employees are to move to the personal pension scheme,
- value the assets which are to provide their benefits, and
- either
  - apply to IR SPSS to convert the whole scheme to a personal pension scheme for approval under Chapter IV, or
  - apply to IR SPSS for the scheme to have dual approval, and receive fresh Chapter IV approval in respect of the members who wish to transfer, while retaining Chapter I approval in respect of the rest of the membership.

Application

24.22 The application should include the following:

a) completed application form for conversion on form SHP 101 if a stakeholder pension scheme, or form PSPP 101 for other cases, signed by the trustees,

b) an additional declaration signed by the trustees, in accordance with Update number 96.

c) a copy of the deed of conversion,

d) if the integrated model rules (IMR2000 for personal pension schemes) are adopted, a completed schedule specifying which of the optional parts (e.g. contracting-out) apply, and if the model rules are not adopted, a copy of the scheme rules,

NB The conditions of tax approval under Chapter IV (unlike Chapter I) do not allow for repayment of contributions in the first two years of membership. The tax approval rules for personal pension schemes provide for full preservation rights and therefore meet the minimum conditions for occupational pension schemes in Chapter I of the Pension Schemes Act 1993. The model rules must not therefore be amended to permit this.

e) the date from which the new rules are intended to apply,

f) confirmation that the scheme has identified the members to which the conversion relates (where dual approval is to apply),

g) confirmation that the scheme will be able to identify at any time the part of the scheme to which any member belongs (where dual approval applies),

h) confirmation for "prescribed members" (see paragraph 24.23) that the valuation checks have been carried out and the member satisfies the tests. The check required (see paragraph 24.24) is similar to the maximum benefit check for transfers for certain categories of individuals under the Personal Pension Schemes (Transfer Payments) Regulations SI 2001/119,

i) statements about the assets in respect of each member involved in the conversion,

- confirming that the assets have been identified (see paragraph 24.27)
- stating how this was done (see paragraph 24.27) and
- showing the extent that assets, or part of specific assets if applicable, have been earmarked for each member as part of the fund within Chapter IV approval,
j) confirmation that the valuation at g) above is in accordance with The Personal Pension Schemes (Conversion of Retirement Benefit Schemes) Regulations 2001 [SI 2001/118]. These valuations should be made no more than 3 months before the date of the scheme application to convert,

k) contracting-out forms if appropriate,

l) written confirmation from the employer, including any other employer participating in the scheme, showing consent to the making of the application to convert.

Which members need valuations?

24.23 The prescribed members who require their funds to be valued prior to conversion, are as follows:

- a "high earner", that is a person
  - aged 45 or over at the proposed date of conversion, and
  - who had earnings from an employment which is the subject of the conversion, and
  - those earnings arose in any tax year falling wholly or partly in the period of 6 years prior to the date of the scheme application to convert, and
  - those earnings exceeded the allowable maximum in force on the date the conversion application is made,

and

- any person who is, or who has been in the ten years prior to the date of the scheme application to convert, a controlling director;

and

- if a controlling director is a member of the converting scheme and will continue to be after conversion, any relative of the controlling director who is also converting will also be required to undergo a valuation check.

What is the valuation test?

24.24 The valuation test is set out in Appendix XI or, for valuations made before 6 April 2001, in regulation 6 of the Personal Pension Schemes (Transfer Payments) Regulations 1988 [SI 1988/1014]. The check is carried out by comparing the proposed ‘transfer value’ with the amount produced from the calculation under Appendix XI or the formula in regulation 6(3), as appropriate.

What happens if the member's fund exceeds the permitted value?

24.25 If the value of the fund exceeds the permitted value, that member may not be a member of the converting scheme. The only exception is if a further valuation prior to the date of intended conversion showed the current value is within the permitted value. The member may not become a member of the Chapter IV scheme unless and until the fund value has become lower and does not exceed the permitted value.

Allocation of assets

24.26 The scheme trustees must provide statements with their application to convert the scheme (see paragraph 24.22(i)). These statements deal with the change in status from what may be pooled assets for the purpose of Chapter I approval, to earmarking of assets for the purpose of Chapter IV approval.
24.27 The extent of change required will vary from scheme to scheme and indeed vary even within the Chapter IV regime.

- Example 1

A Chapter I approved scheme could be run on the basis of members holding units, and the only difference from member to member is in the number of units held. Such a structure could continue within Chapter IV virtually unchanged. In such a set-up, the underlying assets within the scheme might be varied but the members’ interests are expressed in a common form.

- Example 2

Under Chapter I, the rights may be expressed in the form of notional earmarking of assets within a pooled fund. This is usually the case in a self-administered occupational pension scheme. One member may have particular assets shown as producing their rights, and those assets may differ to those used for another member. In this example, there can also be a continuation of form within Chapter IV so long as the separation of assets is clear, continuous, and known to all parties involved.

24.28 The trustees’ statement (following any appropriate actuarial advice) should include a description of the way assets have been held under Chapter I approval, and an explanation of the principles according to which assets are to be held in future under Chapter IV approval.

24.29 The trustees’ statements accompanying an application for conversion should include sufficient information to show that any change required to the form of the scheme has been effected. If the statements are not sufficiently clear, IR SPSS may have to make further enquiries, which may delay the processing of the application. The trustees should produce a report of the position. This report, which should list the assets and indicate which asset or which proportion has been allocated to individual members, need not be referred to IR SPSS but the trustees may be asked to produce it at a later date.

24.30 In making the statements, the trustees (following advice as necessary) may choose to express them as in the following examples. These are illustrative only, and are not intended to be prescriptive. Scheme trustees should take advice as necessary, and provide statements which reflect the circumstances of their scheme.

- Illustration A

'We confirm that we hold a list of the assets of the scheme as at –/--/---- and that we have allocated, in relation to each member who is currently a member and who is to be a member in the personal pension scheme following conversion, specific assets in whole or in part to each of those members. We confirm also that each member has been informed of what assets, or type of assets, form the basis of their fund within the scheme.'

NB It is not necessary to actually earmark assets for each member - unless the scheme requires otherwise, the earmarking may be notional - providing each member is aware of the investments producing their benefits.

- Illustration B

'We confirm that the scheme assets for each member as allocated were identified by:

- continuation of the existing basis whereby assets had already been earmarked and whereby each member is aware of what assets, or type of assets they hold; or

- reviewing the existing basis of allocation of assets, and re-allocating by taking into account member’s known choices on how they want their contributions invested, or in a way which we believe fairly allocates the assets following consultation with members.'

- Illustration C
‘We confirm that, for each current member who is to be a member in the personal pension scheme, that either whole assets have been allocated to the member’s fund or assets have been partly allocated to more than one member. This has been done as described in a report made by the trustees on --/--/---- which is available for inspection to an officer of the Board of Inland Revenue.’

**ACTION ON RECEIVING A CONVERSION APPLICATION**

24.31 *IR SPSS* will check the application and all accompanying documents, and either

- approve the application (see paragraphs 24.33 - 24.35), or
- reject the application (see paragraphs 24.36 - 24.37).

24.32 If the scheme has also applied to Opra to be registered as a **stakeholder pension scheme**, *IR SPSS* will await the outcome of that application before approving the **conversion** application.

**Approval of conversion to a personal pension**

24.33 If the **conversion** has been approved, *IR SPSS* will issue an approval letter which should be retained by the scheme provider.

The approval date will not be earlier than 6 April 2001. It will, if possible, be the date which was shown on the application form as the date from which the provider intended the new rules to apply.

24.34 If the scheme has also applied separately to Opra for stakeholder registration, the approval letter will not be issued until the stakeholder application has also been approved. If the scheme does not obtain stakeholder registration with Opra, it will not be approved under Chapter IV for tax purposes either.

The approval date will not be earlier than 6 April 2001. Again it will, if possible, be the date which was shown on the application form as the date from which the provider intended the new rules to apply.

24.35 For a stakeholder pension scheme applying to *IR SPSS* for contracting out of SERPS, it is *IR SPSS* that will issue a fresh contracting-out certificate.

**Where Conversion to a personal pension cannot be approved**

24.36 If the new Chapter IV scheme does not meet tax approval requirements, *IR SPSS* will issue a letter explaining why it has been refused approval. The scheme will have to apply again, having made the appropriate changes, if it still wishes to **convert** to a Chapter IV scheme.

24.37 If the scheme has also applied for stakeholder pension scheme registration, the **conversion** can only be approved if the scheme both meets the DWP (formerly DSS) minimum requirements for a **stakeholder pension scheme** and obtains Chapter IV tax approval. If the scheme fails to meet either of these requirements, *IR SPSS* or Opra, as appropriate, will write explaining why the application was refused. The scheme may make a further application to **convert** once changes have been made.

**Tax position on conversion**

24.38 There is no tax charge on **conversion** of the scheme. Section 591C (which applies a tax charge on certain schemes or part of such a scheme ceasing to be approved under Chapter I) has been amended and does not apply where the scheme loses its Chapter I approval as part of the process of **conversion** to Chapter IV.

**Controlling directors: restrictions on benefits while scheme is operating under Chapter IV approval**

24.39 Where a **controlling director** is a member of the scheme at the time of **conversion** and
becomes a member of the scheme under Chapter IV approval, particular conditions apply to the benefits payable on retirement or death.

**Retirement lump sum certificate**

24.40 A lump sum may only be paid from the *controlling director's* fund (as *converted*) if a certificate showing the amount payable as a lump sum is held by the trustees under Chapter IV approval. The amount shown on the certificate should be calculated as if a transfer payment was being made, and may be increased by reference to the changes in the *Retail Prices Index* between the date the certified amount was calculated and the date of the scheme application for conversion. In the receiving Chapter IV scheme, the amount paid at *pension date* will be as stated in the rules governing transfer payments.

**Death**

24.41 On the death of a *controlling director*, the benefits paid from the *converted* fund will be the same as if the *converted* fund had been a transfer payment.
Appendix I. Glossary

GLOSSARY OF TERMS USED IN THE PRACTICE NOTES

Additional Voluntary Contributions

Additional Voluntary Contributions are contributions by an employee other than basic or contractual contributions, i.e. over and above contributions (if any) required as a condition of membership and include any such contribution paid under a Free standing Additional Voluntary Contribution Scheme.

Administrator

Administrator is defined in section 611AA.

Allowable Maximum

Allowable maximum is defined in section 640A and means £60,000 for the year 1989/90. For later years, the relevant indexed figures specified in Treasury Orders are as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Maximum</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990/91</td>
<td>£64,800</td>
</tr>
<tr>
<td>1991/92</td>
<td>£71,400</td>
</tr>
<tr>
<td>1992/93</td>
<td>£75,000</td>
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<tr>
<td>1993/94</td>
<td>£75,000</td>
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<td>2001/02</td>
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<tr>
<td>2004/05</td>
<td>£102,000</td>
</tr>
<tr>
<td>2005/06</td>
<td>£105,600</td>
</tr>
</tbody>
</table>

Arrangement

Arrangement means a contractual arrangement made by an individual under a personal pension scheme. Benefits from different arrangements may be taken at different and be paid in different forms. From 6 April 2001, benefits from a single arrangement may be taken at different times and in different forms.
**Associated Employers**

Associated Employers are defined in section 590A(3) and (4) as companies where one is directly or indirectly controlled by the other or both or all are controlled by a third person. Control is construed in accordance with section 416 in relation to close companies or with section 840 for other corporate bodies.

**Associated Employments**

Associated Employments means in relation to a member any employment held concurrently with the member's employment with the employer where benefits in respect of each employment are payable under the scheme in respect of a period while the employments were or are concurrent and, during that period, the employers in question were or are associated.

**Basic or Contractual Contributions**

Basic or Contractual Contributions are contributions which an employee is required to make as a condition of membership of a scheme. They include contributions which the member, either alone or with the agreement of the employer or administrator, can vary but only if they are subject to a requirement that such a rate of contributions must continue for a minimum period of a year or until retirement, leaving service or death if earlier. If this requirement is not met the contributions will be regarded as Additional Voluntary Contributions.

**Board**

Board means the Board of Inland Revenue.

**Connected Scheme**

Connected Scheme is defined in section 590A in relation to an employee. Schemes are connected if they are approved or seeking approval under Chapter I Part XIV and:

- (a) there is a period during which the member has been the employee of 2 associated employers, and

- (b) the period counts under both schemes as a period in respect of which benefits are payable, and

- (c) the period counts under one scheme for service with one employer and under the other for service with the other employer.

**Continued Rights**

Continued Rights includes both pre 17 March 1987 continued rights and pre 1 June 1989 continued rights (see also Appendix III).

**Controlling Director**

Controlling Director is defined in paragraph 5(5) of Schedule 23 as a person who is a director and within paragraph (b) of section 417(5) in relation to the employer company. For practical purposes this means a member who, at any time after 16 March 1987 and within 10 years of retirement or leaving service or leaving pensionable service, has been a director and, either on his or her own or with one or more associates has beneficially owned or been able to control, directly, indirectly or through other companies, 20% or more of the ordinary share capital of the company. For the purposes of this definition:

(i) "Associate" means in relation to a director, any relative (i.e. spouse or civil partner, forebear, issue or sibling) or partner (within the meaning of the Partnership Act 1890), the trustees of any settlement in relation to which the director is, or any relative of his or her (living or dead) is or was, a settlor and, where the director is interested in any shares or
obligations of the company which are subject to any trust, or are part of the estate of a deceased person, the trustees of the settlement concerned or, as the case may be, the personal representatives of the deceased, and

(ii) The expression "either on his or her own or with one or more associates" requires a person to be treated as owning or, as the case may be, controlling what any associate owns or controls, even if he or she does not own or control share capital on his or her own.

Conversion

Conversion means a retirement benefits scheme which is approved under Chapter I of Part XIV of ICTA 1988 but which applies to cease being approved in that way and instead receive approval as a personal pension scheme under Chapter IV of Part XIV of ICTA 1988 (see Schedule 23ZA (ICTA 1988).

Dependant

Dependant means a person who is financially dependent on the employee or pension credit member or dependent on the employee or pension credit member because of disability or who was so dependent at the time of the employee’s death or retirement or the time of the pension credit member’s death or when the pension credit member’s pension credit commenced payment. An ex-spouse or former civil partner of the employee who was in receipt of payments from the employee up to his or her death in respect of, for example, a financial provision order under the Matrimonial Causes Act 1973 may be regarded as financially dependent on the employee.

An adult relative who is not or was not supported by the employee or pension credit member is not that employee’s or pension credit member’s dependant. Subject to the following paragraphs a pension paid to an adult dependant who qualifies on grounds of financial dependency or disability may continue indefinitely.

Natural or adopted children of the employee or pension credit member may automatically be regarded as dependent on the employee or pension credit member if at the time of his or her death they were:

(a) under 18

(b) over 18 but continuing to receive full-time education or vocational training

(c) dependent on the employee or pension credit member because of disability

Any pensions paid by reason of (i) and (ii) should cease when age 18 is reached or full-time education or vocational training ceases* whichever is the later. A pension paid by reason of (iii) may continue indefinitely.

Other children (i.e. neither natural nor adopted children of the employee or pension credit member) may qualify as dependants only if they were financially dependent on the employee or pension credit member, or dependent on the employee or pension credit member by reason of disability. Any pension paid to such children on grounds of financial dependence should cease when age 18 is reached or full-time education or vocational training ceases* whichever is the later. This ensures parity of treatment between offspring and other minor dependants. A pension paid because of dependency by reason of disability may continue indefinitely.

It is not necessary to show financial dependency for a person dependent on the employee or pension credit member because of disability or in the case of widows or widowers or surviving civil partners. The latter automatically qualify for survivors’ benefits on the basis that partners in a legal marriage or civil partnership may always be assumed to be financially dependent on one another.
But a partner (neither married to, nor in a civil partnership with, the employee or pension credit member), whether of the same or opposite sex, can qualify for a survivors pension only if he or she were financially dependent on the employee or ex spouse. Financial interdependence of the employee or pension credit member and his or her partner would be an acceptable criterion, e.g. where the partner relied on a second income to maintain a standard of living which had depended on joint income prior to the employee’s or pension credit member’s death.

Decisions on whether or not a person is dependent are a matter for the scheme trustees. IR SPSS would not challenge the trustees judgement provided they had acted in accordance with the scheme rules.

* A break of not more than an academic year between leaving school and taking up a confirmed place in full-time education or vocational training will not be regarded as a cessation for this purpose, but it is for trustees to decide whether the pension should be paid during the break.

**Exempt Approved Scheme**

Exempt Approved Scheme means any retirement benefits scheme which is approved under Chapter I Part XIV and is either established or held under irrevocable trusts or is the subject of a direction by the Board under section 592(1)(b).

**Ex spouse**

Ex spouse means a person who has received a pension credit as a result of a pension sharing order.

**Final Remuneration**

Final Remuneration needs to be defined in scheme rules for the purpose of applying Inland Revenue limits on benefits. It should not be greater than either:

(a) the highest remuneration upon which tax liability has been determined for any one of the 5 years preceding the relevant date i.e. the date of retirement, leaving pensionable service or death as the case may be, being the aggregate of:

(i) the basic pay for the year in question, and

(ii) the yearly average over 3 or more consecutive years* ending with the expiry of the corresponding basic pay year, of any fluctuating emoluments provided that fluctuating emoluments of a year other than the basic pay year may be increased in proportion to the increase in the Retail Prices Index from the last day of that year up to the last day of the basic pay year. Remuneration that is received after the relevant date and upon which tax liability has been determined will be treated as a fluctuating emolument (providing it was earned or qualified for prior to the relevant date). In these circumstances it may be included provided the yearly average of 3 or more consecutive years begins no later than the commencement of the basic pay year; or

(b) the yearly average of the total emoluments from the employer which are assessable to income tax under Case I or II of Schedule E and upon which tax liability has been determined for any 3 or more consecutive years ending not earlier than 10 years before the relevant date. Where such emoluments are received after the relevant date but are earned or qualified for prior to that date, they may be included provided that in these circumstances the yearly average of 3 or more consecutive years begins no later than the commencement of the year ending with the relevant date.
Provided that -

(i) *remuneration* and total emoluments do not include any amounts which arise from the acquisition or disposal of shares or any interest in shares or from a right to acquire shares (except where the shares or rights etc which give rise to such an amount liable to tax under Schedule E had been acquired before 17 March 1987) or anything in respect of which tax is chargeable by virtue of section 148 or section 313;

(ii) in relation to a *controlling director*, final remuneration shall be the amount ascertained in accordance with (b) and (a) above shall not apply.

(iii) in relation to any other employee whose *remuneration* in any year subsequent to 5 April 1987 used for the purpose of calculating benefits has exceeded £100,000, (or such other figure as may be prescribed by the Treasury), final remuneration shall not exceed the amount ascertained in accordance with (b) above and (a) above shall not apply, unless the individual chooses to adopt £100,000 (or such other figure as may be prescribed by the Treasury);

(iv) where final remuneration is computed by reference to any year other than the last complete year ending on the relevant date, the member's *remuneration* or total emoluments of any year may be increased in proportion to any increase in the *Retail Prices Index* from the last day of that year up to the relevant date. For a member with *pre 17 March 1987 continued rights* this proviso shall not apply to the calculation of the maximum lump sum retirement benefit unless the member's aggregate total benefits are similarly increased beyond the maximum amount which could be paid but for this proviso and/or the first sentence of (a) (ii) above and then only to the same proportionate extent;

(v) final remuneration shall not exceed the *permitted maximum* except in relation to members with *continued rights*;

(vi) for the purpose of calculating the maximum lump sum retirement benefit of a member with *pre 1 June 1989 continued rights* final remuneration shall not in any event exceed £100,000 (or such other figure as may be prescribed by the Treasury);

(vii) an employee who remains, or is treated as remaining, in service but by reason of *incapacity* is in receipt of a much reduced *Remuneration* e.g. under a sick pay or permanent health insurance scheme, for more than 10 years up to the relevant date, may calculate final remuneration under (a) or (b) above with the final remuneration calculated at the cessation of normal pay and increased in accordance with the *Retail Prices Index*;

(viii) the total amount of any profit related pay (whether relieved from income tax or not) may be classed as pensionable remuneration and treated as a *Fluctuating Emolument*;

(ix) an early retirement pension in payment from the employer may not be included in final remuneration.

(x) any amounts of pay used by buy partnership shares in a Share Incentive Plan (formerly known as an All-Employee Share Ownership Plan) that are classed as pensionable *remuneration* qualify for the purpose of paragraph 83 of Schedule 8 of the Finance Act 2000.

**NB**

1. Except as in proviso (i) above, benefits in kind may be taken into account when they are assessed to income tax as emoluments under Schedule E, and will normally be
regarded as *fluctuating emoluments*. If benefits are not so assessable, they may not be included as part of final remuneration except with the agreement of IR SPSS.

2. Where at the relevant date final remuneration cannot be precisely established because tax liability on all the constituent elements of *remuneration* for the year or years in question has not been determined, final remuneration may be calculated on the appropriate basis above using those elements of *remuneration* which have been finally determined for tax purposes. Immediate "on account" pension and lump sum benefits may be provided based on final remuneration so calculated. When tax liability on *remuneration* is finally determined, and final remuneration recalculated providing scope for further benefits (both pension and lump sum), these may be paid but they must not cause total benefits to exceed Inland Revenue limits calculated as at the date benefits were first taken.

Where the above applies in the case of a member who does not have *continued rights* and whose lump sum retirement benefit is calculated on the basis set out in paragraph 8.7, a subsequent additional lump sum will not be possible if final remuneration is not finally determined for tax purposes until after the end of the first year in which the pension has been in payment.

Where immediate benefits are not being provided or where a transfer payment is to be made in respect of accrued pension benefits then final remuneration may only be calculated using *remuneration* assessable to income tax under Case I or II of Schedule E and upon which tax liability has been determined.

3. Where the relevant date occurs during a period of paid maternity leave or within 12 months of the end of a period of paid maternity leave, Final Remuneration (as defined in this definition) can include an amount based on the greater of:

(a) the *remuneration* that the employer would have been obliged to pay to the employee under a contract of employment in force in respect of that employee prior to the start of the paid maternity leave, or

(b) the actual amount of *remuneration* received by the employee from the employer in the period of 12 months immediately before the commencement of the paid maternity leave.

In the case of 3(a) above the *remuneration* that the employer would have been obliged to pay to the employee under a contract of employment in force in respect of that employee prior to the start of the paid maternity leave cannot include any amounts that, had they been paid, would not qualify as *remuneration*.

In the case of 3(b) above only, the *remuneration* may be increased in proportion to any increase in the *National Average Earnings Index* from the last day of the 12 month period immediately before the commencement of the paid maternity leave up to the end of that leave.

* Where *fluctuating emoluments* have not been paid for the full 3 years, they should be averaged over the period from the commencement of their entitlement to payment (or the beginning of the 3 year period, if later) to the end of the relevant basic pay year. Where, however, it is proposed to include in final remuneration a *fluctuating emolument* which was payable in a single year only the agreement of IR SPSS must be sought.

**Fluctuating Emoluments**

Fluctuating Emoluments are any part of an employee's earnings which are not paid on a fixed
basis and are additional to the basic wage or salary. They include profit related pay (see proviso (viii) to the definition of final remuneration), overtime, commission, bonuses or benefits in kind as long as they are assessable to tax under Case I or II of Schedule E. Directors' fees may rank as fluctuating emoluments according to the basis on which they are voted.

**Former Civil Partner**

Former civil partner means a person who has received a pension credit as a result of a pension sharing order.

**Free standing Additional Voluntary Contribution Scheme**

Free standing Additional Voluntary Contribution Scheme means a retirement benefits scheme approved by the Board by virtue of section 591(2)(h), established by a pension provider or the trustees of an approved centralised scheme for non-associated employers (see paragraphs 21.10 - 21.21) to which the employer does not contribute and which provides benefits additional to those provided by a scheme to which the employer does contribute.

**GAD Tables**

The set of tables compiled by the Government Actuary's Department that show the maximum income withdrawals for each and sex on the basis of a single-life annuity.

**Incapacity**

Incapacity means physical or mental deterioration which is sufficiently serious to prevent the individual from following his or her normal employment, or which seriously impairs his or her earning capacity. It does not mean simply a decline in energy or ability.

**IR SPSS**

IR SPSS stands for: "IR Savings, Pensions, Share Schemes". With effect from 1st April 2001, the Pension Schemes Office became a part of IR SPSS. IR SPSS will be responsible for work on pensions, including personal pensions, as well as savings products, employee share schemes and any continuing MIRAS issues.

**Lien Rule**

Lien Rule means a provision allowing recovery by an employer of any money due to it through any criminal, fraudulent or negligent act or omission by the employee. Such recovery may be made from the employee's lump sum retirement benefit (as described in Part 8), from a lump sum death in service benefit or a lump sum payable on death in service after normal retirement date given on the basis which would have applied had he or she retired on the day before death (as described in Part 11), or from the employee's pension benefit. Where the debt does not result from the employee's fraud or negligence it may be recovered from any benefit not subject to preservation requirements. The employer's right of recovery from the scheme must be expressly limited so that the amount payable to it does not exceed the amount of the actual loss sustained. The amount recoverable must not exceed the employee's interest in the scheme and in the event of a dispute as to the amount to be recovered, the employer is not entitled to enforce recovery until after the obligation has become legally enforceable.

**National Average Earnings Index**

National Average Earnings Index means the earnings index issued by the Office of National Statistics.

**Normal Retirement Date**

Normal retirement date means the date of attainment by a scheme member of the age specified in the scheme rules as the age at which a member should normally retire (see paragraph 6.5).
Ordinary Annual Contributions

Ordinary Annual Contributions have no statutory definition but need to be interpreted by reference to the natural meaning of the words which make up the term. It is clear that to come within this term contributions must have the quality of annuity i.e. they must be contributions which are paid each year. The following explanation gives some guidance on how the word ordinary is interpreted by the Inland Revenue. In general there must be a common basis for the amount of the contributions from year to year e.g. a fixed amount or a fixed percentage of payroll. This does not mean that there can be no fluctuation of the annual amounts paid but where fluctuation occurs it may be necessary to demonstrate the nature of the specified basis used to determine the amount of the contributions.

There is no minimum number of years for which a rate of contribution needs to be paid to qualify as ordinary annual contributions but as a rule of thumb that rate should continue for no less than 3 consecutive years. Nor will it normally be necessary in relation to a first payment in a series to demonstrate its nature as an ordinary annual contribution by reference to future annual payments before it is accepted as such - the Inland Revenue will accept the employer's stated intention to continue to contribute on the new or original basis. The Inland Revenue do however reserve the right to challenge whether a series of fluctuating payments constitutes payment of ordinary annual contributions.

It might be possible for the total annual contributions to fluctuate although contributions for individual members are made on a specified basis and are clearly ordinary annual contributions - employers may on occasions be asked to demonstrate that the overall contribution is made up entirely of ordinary annual contributions.

Pensionable Service

Pensionable service means service for an employer in respect of which benefits (other than benefits payable solely on death before retirement) accrue under an approved scheme.

Pension Credit

Pension credit is the amount of benefit rights that the *ex spouse* or *former civil partner* of a scheme member becomes entitled to following a *pension sharing order*. The rights derive from the scheme member’s benefit rights under the scheme.

**Pension Credit Member**

An *ex spouse* or *former civil partner*, whose rights under the scheme derive from a *pension credit*.

Pension Date

Pension Date means in relation to any *arrangement* (or part of an *arrangement* from 6 April 2001) the date on which

- an annuity is first payable, or
- the member elects to make income withdrawals from the *arrangement*.

Pension debit

Pension debit is the amount of benefit rights given up by a scheme member and allocated to the *ex spouse* or *former civil partner* of that member following a *pension sharing order*.

Pension sharing order

Pension sharing order is an order or provision as described in section 28(1) of the Welfare Reform and Pensions Act 1999 (WRPA 99) which is made in accordance with the provisions of that Act. WRPA 99 makes provisions to allow financial settlements on divorce or nullity of marriage.
the dissolution of nullity of a civil partnership to include the splitting of pension rights of either or both parties to the settlement. At the date of the financial settlement the pension rights can be split between both parties (the former couple in marriage or civil partnership) by varying amounts depending on the terms of the settlement.

**Permanent Community of Interest**

Permanent community of interest means there are sufficient links between the participating companies for them to be regarded as associated, for example

(a) there is common management in that the same individuals form a majority on the board of directors of each company;

(b) there are common shareholders even though the pattern of shareholdings may differ. This needs to be looked at with care but a community of interest can be accepted if the same individuals hold a majority of the issued ordinary share capital of each company;

(c) staff are interchangeable or jointly employed, and

(d) the companies' operations are interdependent, for example, one sells most of its products to the other.

**Permitted Maximum**

Permitted maximum is defined in section 590C and came into existence for 1988/89 and 1989/90 at the level of £60,000. For later years the relevant indexed figure specified in Treasury orders were as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990/91</td>
<td>£64,800</td>
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<td>£102,000</td>
</tr>
<tr>
<td>2005/06</td>
<td>£105,600</td>
</tr>
</tbody>
</table>
Personal Pension Scheme

Personal pension scheme means a pension scheme approved under Chapter IV of Part XIV (this includes stakeholder pension schemes). The eligibility requirements for contributing to a personal pension scheme are set out in Part 3 of IR 76 (which is published on the Inland Revenue website, but as far as employees are concerned are broadly as follows.

1. An employee who in a tax year has "relevant earnings" from another employment is eligible to contribute to a personal pension scheme at any time in that tax year by virtue of those "relevant earnings".

2. An employee who in a tax year is a member of an occupational pension scheme which provides only death in service benefits is eligible to contribute to a personal pension scheme in that tax year because their earnings from that employer are "relevant earnings" for personal pensions purposes.

3. An employee is eligible (providing they satisfy certain residence criteria) to contribute to a personal pension scheme in any tax year in which, despite having no "relevant earnings", their pensionable service extends to only part of the tax year. See Part 3 of IR 76.

4. An employee who is not eligible under any of 1-3 above and whose service is, throughout the tax year, pensionable through an occupational pension scheme providing more than death in service benefits in relation to the employment, is not eligible to contribute to a personal pension scheme in that tax year by virtue of earnings in respect of that service but may be eligible to contribute to a personal pension scheme under the "concurrency" criteria. See Part 3 of IR 76.

5. A member of an occupational pension scheme which is not contracted-out may regardless of other circumstances join an appropriate personal pension scheme (APP) purely to contract out of the State Earnings Related Pension Scheme (from 6 April 2002, the State Second Pension). Normally, the administrator of the APP may accept in respect of such a member only the "minimum contributions" paid by Inland Revenue (NICO).

Pre 17 March 1987 Continued Rights

Pre 17 March 1987 Continued Rights A member of a scheme is entitled to pre 17 March 1987 continued rights either if he or she has continued to accrue benefits under the scheme since before 17 March 1987 or in any of the circumstances prescribed in regulation 3 of the Occupational Pension Schemes (Transitional Provisions) Regulations 1988 (SI 1988 No 1436). In a scheme to which those Regulations do not apply a member's entitlement to continued rights in any of the circumstances prescribed in regulation 3, must be agreed with IR SPSS who will consider the particular circumstances in the light of those Regulations (but see Appendix III).

Pre 1 June 1989 Continued Rights

Pre 1 June 1989 Continued Rights A member of a scheme is entitled to pre 1 June 1989 continued rights if:

(a) the scheme commenced before 14 March 1989 and he or she has continued to accrue benefits under the scheme since before 1 June 1989 but not before 17 March 1987, or

(b) he or she falls within the circumstances prescribed in regulation 3 of the Retirement Benefits Schemes (Continuation of Rights of Members of Approved Schemes) Regulations 1990 (SI 1990 No 2101). In a scheme to which those Regulations do not apply a member's entitlement to continued rights in any of the circumstances prescribed in regulation 3, must be agreed with IR SPSS who will consider the particular circumstances in the light of those Regulations (but see Appendix III).

In relation to a centralised scheme (see Part 21) this definition is varied to exclude a member joining or changing employer under the scheme before 1 June 1989 where the member's employer (or new employer in the case of change of employer) did not participate in the scheme before 14 March 1989. This variation, however, does not apply where the employers participating in the
scheme are associated employers as strictly defined (see also paragraphs 21.22 - 21.24).

**Relative**

Relative means, in relation to a controlling director (regulation 6 (4) of the Personal Pension Schemes (Conversion of Retirement Benefit Schemes) Regulations 2001 [SI 2001/118] –

- the controlling director’s spouse or civil partner,
- the controlling director’s brother, sister, parent or remoter forebear, child or remoter lineal descendant,
- the spouse or civil partner of a brother, sister, parent or remoter forebear, child or remoter lineal descendant of the controlling director, or
- a brother, sister, parent or remoter forebear, child or remoter lineal descendant of the controlling director’s spouse or civil partner.

**Relevant Benefits**

Relevant benefits are defined in section 612(1) of the Taxes Act in very wide terms, and broadly cover any type of financial benefit given by an employer on retirement or death or as a result of a pension sharing order but excluding benefits given in connection with genuine redundancy (as opposed to retirement). The definition does not include benefits receivable only in the event of death by accident or disablement by accident during service.

**Relevant Statutory Scheme**

Relevant statutory scheme is defined in section 611A as a statutory scheme either established before 14 March 1989 or established thereafter and registered by the Board as a scheme, having provisions corresponding to those of an approved scheme.

**Remuneration**

Remuneration means (unless qualified as in the definition of final remuneration) any emoluments which are chargeable to tax under Case I or II of Schedule E, including

- profit related pay whether relieved from income tax or not, and
- amounts used to purchase partnership shares in a Share Incentive Plan (formerly known as an All-Employee Share Ownership Plan) that qualify as such under paragraph 83 of Schedule 8 of Finance Act 2000

but excluding

- those items which are specifically excluded therefrom by section 612(1) (e.g. share option gains or golden handshakes),
- amounts chargeable to tax under section 313, and

in relation to members without continued rights, any emoluments in excess of the permitted maximum.

**Retail Prices Index**

Retail Prices Index means the index of retail prices compiled by the Department of Employment or any other index agreed for use by a particular scheme by IR SPSS.
Retained benefits

Retained benefits generally means retained rights to relevant benefits (see Part 7) other than refunds of contributions (and including where appropriate pension debits against such benefits). The retained rights to relevant benefits will have been built up during previous employments or periods of self employment (whether alone or in partnership) in schemes or contractual arrangements which have benefited from tax privileges, i.e.

(a) retirement benefits schemes approved or seeking approval,

(b) relevant statutory schemes,

(c) funds to which Section 608 applies,

(d) retirement benefits schemes which have been accepted by the Inland Revenue as "corresponding" for the purposes of section 596(2)(b),

(e) retirement annuity contracts or trust schemes approved under section 620 which relate or related to relevant earnings from the current employment, or previous employments (including periods of self employment whether alone or in partnership),

(f) personal pension schemes approved under section 631, except for

- arrangements to which only "minimum contributions" may be paid during a period of membership of a non contracted-out occupational pension scheme

and

- personal pension benefits arising from contributions made during a period of eligibility to contribute to the personal pension scheme under section 632B ("concurrency")

(g) transfer payments from overseas schemes held in

- a retirement benefits scheme approved or seeking approval or
- a relevant statutory scheme or
- a retirement annuity contract or trust scheme approved under section 620, or
- a personal pension scheme.

- Transferred benefits

The following also applies in the circumstances described

- benefits from the sources at (a) - (g) above, which have been either

  - transferred to another scheme (in the UK or elsewhere), or

  - bought out,

continue to be retained benefits (see also paragraph 10.27); but for the avoidance of doubt, benefits arising under the two exceptions at (f) continue to be ignored after transfer.

- pension debit - if

  - the transferred benefits were subject to a pension debit in the transferring scheme, and
- the member does not fall within the administrative easement described in paragraph 7.7,

the pension debit will also be a retained benefit (see paragraph 10.27).

- if benefits have been transferred from an approved retirement benefits scheme of the current employer to a personal pension scheme, the benefits from the personal pension scheme in respect of that transfer (to the extent that they relate to service with the current employer) are aggregable benefits for the purposes of paragraphs 7.25 and 7.26.

- **Concurrent employments**

  The following applies -

  - benefits built up in relation to a wholly concurrent employment/occupation are not retained benefits in relation to the other concurrent employment/occupation

  - if the member
    - has continued rights, and
    - the period of concurrent employment extends only to part of the overall period of service,

    the benefits which relate to that period of service where there was no concurrent employment are retained benefits (unless those benefits arise from eligibility for a personal pension scheme under s632B "concurrency" - see (f) above)

  - if the member
    - does not have continued rights, and
    - the concurrent employments are not associated, and
    - the schemes are not connected schemes,

    the benefits which relate to that period of service where there was no concurrent employment are retained benefits (unless those benefits arise from eligibility for a personal pension scheme under s632B "concurrency"- see (f) above). (NB benefits for such members arising under connected schemes and/or under one scheme in respect of associated employments cannot be retained benefits - they are aggregable benefits)

  - benefits from a personal pension scheme or retirement annuity contract which relate to a period of service where there was no concurrent employment or occupation are retained benefits (unless those benefits arise from eligibility for a personal pension scheme under s632B "concurrency"- see (f) above). This applies whether or not there has at any time been an association between the employments (or between the employment and the occupation).

- **Benefits from retirement annuity contracts or personal pension schemes in respect of current employment**

  These are treated as follows

  - for a controlling director without continued rights, benefits from such schemes which arise from contributions paid out of relevant earnings from the current employer are aggregable benefits i.e., treated as benefits provided by the current employer (see paragraphs 7.10 and 8.9) unless the contributions were made to a personal pension scheme
scheme under s632B "concurrency" (see (f) above).

- for all other cases (except under (f) above), such benefits are retained benefits.

- Total benefits

The aggregate retained benefit will be expressed in terms of pension and include the pension equivalent of any retirement benefits in a form other than pension derived from relevant sources. If the aggregate from all sources does not exceed £260 it may be ignored.

- Lump sum retirement benefits

The aggregate retained benefit will be expressed in terms of the amount of lump sum benefits received or receivable from relevant sources. If these do not exceed £2,500 in total, they may be ignored.

- Death benefits

Only lump sum death in service benefits are retained benefits, but they may be ignored if they

- do not exceed £2,500 in total (with the exception of any element derived from a transfer from an occupational pension scheme - see paragraph 10.20), or
- are derived from a return of fund under retirement annuity contracts or personal pension schemes (unless they arise from transfers into retirement annuity contracts or personal pensions out of approved/approveable occupational pension schemes or relevant statutory schemes).

- Survivors' benefits

Retained benefits are not taken into account in the calculation of maximum widows', widowers', surviving civil partners, or dependants' benefits.

- Valuation

Guidance on the valuation of retained benefits is set out in paragraphs 16.35 to 16.55.

Retirement Annuity Contract

Retirement Annuity Contract means a contract approved under Chapter III Part XIV. Approval under this Chapter has been superseded by the approval of personal pension schemes under Chapter IV Part XIV and new contracts of this sort are no longer available.

Retirement Benefits Scheme

Retirement Benefits Scheme is defined in section 611 as a scheme for the provision of relevant benefits for one or more employees but does not include any national scheme (such as the State Earnings Related Pension Scheme) providing such benefits. In this context "scheme" needs to be interpreted widely to include any arrangement creating an enforceable right to such benefits and an arrangement to pay ex-gratia relevant benefits (although the latter type of arrangement is not approvable unless the benefit is in the form of a lump sum and satisfies certain conditions). Employee includes an ex-employee. “Employees” and “employee” are replaced by “scheme members” and “scheme member” in subsection (3) and (4)(b) of section 611 and subsection (b) defines “scheme member” as including both employees and pension credit members.

Special Contribution

Special Contribution means any contribution to a retirement benefits scheme by an employer which is not an Ordinary annual contribution.
**Stakeholder pension scheme**


**State Pension Age**

State Pension Age means "pensionable age" as defined in section 27(1) Social Security Act 1975 i.e. age 65 for a male and age 60 for a female.

**Taxes Act**

Appendix II. Mailing list and forms

IR SPSS MAILING LIST AND FORMS

Mailing List

A2.1 In 1996/97, PSO (now a part of IR SPSS) introduced a subscription for inclusion on its Mailing List. The current subscription (2001/02) for new subscribers and existing subscribers making additional subscriptions is £20.

A2.2 All communications to do with mailing list subscriptions including payments, changes of address and delivery details should be directed to Communications in Print, 8 Repton Close, Burnt Mills, Basildon, Essex SS13 1LJ. Their telephone number is 01268 242 623 and this Helpline will be manned from 09:00 to 17:00 hours every weekday.

A2.3 IR SPSS retains responsibility for the authorship and printing arrangements and will continue to deal with queries on the technical content of the Practice Notes.

Forms

A2.4 Specimens of all the forms referred to in the Practice Notes used to be included in the mailing list version of this Appendix. However due to the logistical differences of forms production these will now be separated out into a pack, available from our printers: both on joining the mailing list and to order. Under the new arrangement, customers joining the mailing list at a later date will obtain a more up-to date collection of forms (under the previous arrangement new customers had to sort through past Updates to find the latest form). Likewise anyone asking for the forms pack should receive the latest available versions.

A2.5 Supplies of individual forms are available from IR SPSS, Yorke House, PO Box 62, Castle Meadow Road, Nottingham NG2 1BG (Ansaphone: 0115 974 1670).

However, IR SPSS has no restriction on the photocopying or printing of the forms provided they are identical with the official form. Customers wishing to produce their own versions of the forms should seek the prior approval of IR SPSS Audit & Pension Schemes Services with a view to inserting a user identifier at the bottom right hand corner of the form, e.g. PS176 (1/95) (XYZ Ltd).
Continued Rights

A3.1 A member is entitled to *continued rights* in circumstances where he or she joined a scheme prior to 17 March 1987 or a pre-14 March 1989 scheme prior to 1 June 1989 as appropriate with entitlement to benefits on a pre-Finance (No 2) Act 1987 or pre-Finance Act 1989 basis as the case may be and benefits continue to accrue on that basis.

A3.2 A member will also normally be entitled to *continued rights* in circumstances where he or she joined a scheme as above and benefits cease to accrue under the scheme by reason of:

a) becoming a member of another scheme established by the same employer or an *Associated Employer*.

b) Becoming a member of a scheme of an employer who has acquired, been acquired by, merged with, or taken over the whole or part of the business of, his or her employer.

c) Being seconded or posted to another employer provided that:
   i) at the end of the period of secondment or posting the individual becomes a member of a scheme of the employer by whom he or she was seconded or posted, or, a scheme of an employer as in a) or b) above, and
   ii) at the time of secondment or posting the member had a definite expectation that condition i) would be met.

d) Unpaid absence, provided that within one month of returning to employment he or she becomes a member of a scheme of the employer by whom he or she was employed immediately before absence began or an employer as in a) or b) above.

e) Absence due to pregnancy or confinement provided within one month of returning to employment she becomes a member of a scheme of the employer by whom she was employed immediately before absence began or an employer as in a) or b) above.

f) Absence other than in the circumstances described in c), d) or e) above provided that within one month of benefits ceasing to accrue, he or she rejoins the scheme.

A member will also be entitled to *continued rights* in the following circumstances:

g) Where the employer was contractually bound to provide benefits for the member:
   i) before 17 March 1987 but had not established a scheme before that date;
   ii) before 14 March 1989 in the case of a scheme coming into existence on or after that date and the member joined the scheme within 3 months of that date;
   iii) before 1 June 1989 in the case of a scheme which came into existence before 14 March 1989 and the member joined the scheme on or after 1 June 1989 and within 3 months of commencing the employment.

h) Where the individual was a member of a scheme of the employer before 17 March 1987 or 1 June 1989 as appropriate and without benefits ceasing to accrue under that scheme, the individual becomes a member of another approved scheme which provides benefits to supplement those under that scheme.

i) Where the individual was not a member of a scheme before 17 March 1987 but nevertheless was regarded as a member before that date for preservation purposes.
In the context of the above it should be noted that membership of a scheme prior to 17 March 1987 which provides benefits solely on death in service does not entitle a member to pre 17 March 1987 continued rights though membership of such a scheme which commenced prior to 14 March 1989 where membership commenced prior to 1 June 1989 does entitle a member to pre 1 June 1989 continued rights.

**Transfers Between Schemes of Employers in Accordance with a. or b. above and Joining a Supplementary Scheme of the Employer as in h. above**

A3.3 Where a member entitled to continued rights in the original scheme, transfers to a scheme in circumstances as set out in a) or b) in paragraph A3.2 above and the receiving scheme is not subject to the relevant statutory override (in Schedule 23 of the Taxes Act or Part II Schedule 6 Finance Act 1989 as appropriate), entitlement to continued rights in the receiving scheme is determined by IR SPSS by the exercise of its discretion in the light of the "disapplying" Regulations (see Appendix I definitions of pre 17 March 1987 continued rights and pre 1 June 1989 continued rights). Where such a transfer is made in circumstances that had the relevant overriding legislation applied it would have been automatically disapplied by the Regulations (SI 1988 No 1436 or SI 1990 No 2101 as applicable), the continued rights of the member concerned will be retained and the specific agreement of IR SPSS is not required.

A3.4 The above relaxation will also apply where a member who is entitled to continued rights in his or her employer's scheme by virtue of the paragraph immediately above joins another scheme of that employer which provides supplementary benefits to the main scheme as in h) in paragraph A3.2 above.

A3.5 Where a member entitled to continued rights established following the first transfer, subsequently transfers on to another scheme (whether or not that scheme is subject to statutory override) in circumstances set out in a) or b) in paragraph A3.2 above, entitlement to continued rights in the receiving scheme must be specifically agreed with IR SPSS. Further transfers on in these circumstances similarly require specific agreement. Where the transfer is to a scheme subject to statutory override, it will be necessary to apply to IR SPSS for a formal direction on an individual case basis under regulation 11 SI 1988 No 1436 and/or regulation 8 SI 1990 No 2101 as appropriate. IR SPSS will generally be prepared to take a sympathetic view where:-

- a member, having transferred to a second scheme of an employer as in a) or b) above and retained continued rights in that scheme, transfers either to a third scheme of an employer as in a) or b) above as a result of, for example, promotion, or to a scheme of an employer as in b) above as a result, for example, of a sale or merger.

A3.6 Where the transfer is to a scheme not subject to statutory override, IR SPSS will consider the particular circumstances by analogy with regulation 11 and/or 8 as appropriate, and again as with statutorily overridden schemes, will be prepared to treat sympathetically, those cases falling within the circumstances described immediately above.

A3.7 The above conditions apply also where a member entitled to continued rights in his or her employer's scheme joins a second or subsequent supplementary scheme of the employer as in h) in paragraph A3.2 above.
Appendix IV. Split service

Split Service

A4.1 The benefits which may be provided for an employee who returns to service with the same employer after a break are as follows:

a) Where no benefits were provided in respect of the first period of service, subject to paragraph 3.5, benefits can be granted in respect of the aggregate of both periods of service and final remuneration from the second or last period.

b) Where benefits have been provided in respect of the earlier period of service but they have not yet come into payment, further benefits may be granted on one of the following bases:

   i) benefits may be increased to the maximum calculated by reference to aggregate service and final remuneration from the final period of service, or

   ii) the periods of service may be considered separately. In relation to the final period of service the benefits of the earlier period(s) should if necessary (see paragraph 7.4) be taken into account as retained benefits.

c) Where benefits in respect of the first period of service are in payment and those benefits were granted on an incapacity basis such that benefits in respect of notional service were given (see paragraph 6.2), then the pension benefits must be suspended if further benefits are to be provided. If this is done the total benefits on subsequent retirement must not exceed the greater of:

   i) those permitted by paragraph 7.4 for total service including the period when in receipt of the incapacity early retirement pension (in this respect pension instalments paid during the period of incapacity may be ignored but any lump sum retirement benefit paid on early retirement must be aggregated for the purpose of calculating maximum approvable total benefits, and

   ii) the amount of the early retirement pension originally granted but increased in accordance with paragraph 10.12.

A separate lump sum may be given in respect of the second period of service in accordance with the limits set out in Part 8.

In the case of partial recovery from incapacity the early retirement pension may be abated. If it is desired to provide further benefits in respect of the resumed service in these circumstances IR SPSS should be consulted.

d) Where benefits in respect of the first period of service are in payment and those benefits were not granted on an incapacity basis as in c) above, then further benefits may accrue. The position here depends on whether or not the early retirement pension is suspended. Where it is, benefits may be provided by reference to the aggregate of both periods of service in accordance with c) i) above. Where the early retirement pension is not suspended the continuing pension in payment and the annuity equivalent of any lump sum already taken are to be treated as aggregable benefits and the total benefit from both periods of service must not exceed 2/3rds of final remuneration on ultimate retirement. This will be so even if benefits in respect of the second period of service accrue at less than 1/60th of final remuneration. A separate lump sum may be given in respect of the second period of service in accordance with the limits set out in Part 8.

e) Where a refund of contributions (see paragraph 10.52) was taken by the employee in respect of the earlier period of service and is not repaid in accordance with paragraph 7.23,
the period of service to which they relate may not be included for the purposes of further benefit provision under the scheme.

f) Where in relation to b), c) and d) above, the employee is entitled to continued rights in respect of the first period of service but not in respect of the second or last period of service so that later period is subject to different Inland Revenue limits from the first period of service, provision of benefits by reference to aggregate service and final remuneration from the final period of service is not possible. In these circumstances the periods of service must be considered separately with the benefits in respect of the earlier period(s), if necessary (see paragraph 7.4) being taken into account as retained benefits.
Appendix V. Changes in part time working

Provision of Benefits Where Service Consists of Both Part Time and Full Time Service

A5.1 Whether part-time service precedes or follows full-time service, it is always permissible to compute the benefits for each period of service separately by reference to the remuneration of that period (for this purpose, the time restrictions on final remuneration to either earnings of one of the 5 years preceding the relevant date or to an average for a period ending within 10 years of the relevant date, may be set aside in respect of the earlier period of service, but each year's remuneration may only be increased (if the scheme rules allow) as set out in proviso (iv) to the definition of final remuneration, provided the years selected are within the time restrictions by reference to the date of change to part-time or full-time employment as the case may be).

A5.2 Alternatively where the full-time service follows the part-time, benefits may be based on final remuneration in the full-time job provided that the part-time service is converted into its full-time equivalent using the formula:

\[
\text{Years of part time service} \times \left( \frac{\text{Part time working hours}}{\text{Full time working hours}} \right)
\]

* This should be the number of hours on which final remuneration is based.

A5.3 A similar alternative is available where the part-time service follows the full-time. In this case, however, not only does the part-time service need to be converted to full-time service but also the final remuneration needs to be converted to its full-time equivalent (the permitted maximum, if appropriate, should apply to the amount after conversion). This alternative is not to be used for calculating benefits in respect of remuneration which includes emoluments as a director.

A5.4 Where the conversion method described in paragraphs 2 and 3 above is being used and the formula N/NS x P or N/NS x LS is being applied in respect of a member retiring (otherwise than on incapacity - see paragraph 6.2) before normal retirement date (see paragraphs 7.47 and 8.37) or leaving pensionable service (see paragraphs 10.10 and 10.17), then in calculating the NS element in the formula, the actual number of years between the date of early retirement/leaving pensionable service and normal retirement date must be taken into account. It is not acceptable in respect of a member leaving or retiring early from part-time employment to convert potential future part-time service to its full-time equivalent for the purpose of this calculation.

A5.5 Paragraph 7.4 describes circumstances where benefits must not exceed two-thirds of final remuneration less retained benefits. When applying this restriction to benefits for mixed full-time and part-time service, final remuneration should be calculated:

a) in conversion cases (i.e. where paragraphs 2 or 3 above apply) as the actual or notional full-time final remuneration used in the calculation, and

b) where separate period calculations are used, as follows:

\[
\left( \frac{\text{Years of part time service}}{\text{Years of total service}} \right) \times \text{Final Remuneration for part time service}
\]

plus

\[
\left( \frac{\text{Years of full time service}}{\text{Years of total service}} \right) \times \text{Final Remuneration for full time service}
\]
A5.6 Where benefits are to be calculated for employees with continued rights using either or both of the uplift tables in paragraphs 7.40 and 8.25, and either of the conversion methods set out in paragraphs 2 or 3 above, service, for the purpose of determining the maximum approvable fraction, should be taken as the total of notional full-time service (i.e. including the full-time equivalent of part-time service).

A5.7 Where the calculation of maxima has been based on separate periods of service in accordance with paragraph 1 above, full and part-time service may be aggregated for the purpose of determining the relevant rate of uplift which should then be apportioned pro rata.

Example

A5.8 A member of the scheme has been in both part-time and full-time service of the same employer, having completed 6 years part-time service with final remuneration of £6,000 followed by full-time service for 2 years finishing at normal retirement date on £14,000.

Total service is therefore 8 years and, if there are no retained benefits, maximum total pension benefit can be based on 24/60ths of final remuneration.

Calculation proceeds thus:

\[
\left( \frac{6 \text{ (years of part-time service)}}{8 \text{ (years of total service)}} \right) \times \frac{24}{60} \times £6,000 = £1,800
\]

\[
\left( \frac{2 \text{ (years of full-time service)}}{8 \text{ (years of total service)}} \right) \times \frac{24}{60} \times £14,000 = £1,400
\]

Total benefit = £3,200

A5.9 The calculation of the maximum approvable lump sum benefits for employees with continued rights and mixed part-time/full-time service must follow the method (conversion or separate calculations) used for calculating pension.

Benefits on death in service

A5.10 Maximum approvable pensions for widows, widowers, surviving civil partners or dependants should be calculated on the assumption that the terms of employment (i.e. full or part-time) at the time of death would have continued unchanged until normal retirement date.

A5.11 Final remuneration, for the purpose of calculating the maximum approvable lump sum death benefit (paragraphs 11.2 and 11.3) following a change from full-time to part-time employment, may be calculated as in paragraph 11.1c) by reference to a year ended not earlier than 36 months prior to the date of change.
A6.1 The text refers only to transferring schemes or occupational schemes and to administrator/trustees. Proposed overseas transfers from buy-out policies are also subject to these conditions. References to transferring schemes or occupational schemes should be read as including buy-out policies and references to administrator/trustees should be read as including Life Offices.

A. General conditions applying to all overseas transfers

A6.2 Where a member requests a transfer to an overseas scheme of non-contracted-out rights and/or non-safeguarded rights the transfer cannot be made if any of the following general conditions are not met:

- No part of the benefit under the UK scheme has come into payment or become due and payable (apart from the commencement of pension in the form of income drawdown from an additional voluntary contributions fund).

- The transfer is made directly from the administrator/trustees of the UK scheme to the administrator/trustees (or equivalent) of the overseas scheme. Cheques and other payments must specify that the money is being transferred to the administrator/trustees (or equivalent) in that capacity. Should that not be possible because of software limitations in the cheque production process the cheque or other payment must be accompanied by a letter specifying a similar instruction. In that case the administrator/trustees of the UK scheme must check that payment has been made in full to the administrator/trustees (or equivalent) of the overseas scheme in that capacity, and must notify IR SPSS if such confirmation is not obtained within three months of the transfer date. Where non-cash assets are being transferred, legal ownership of those assets must be transferred to the administrator/trustees (or equivalent) in that capacity.

- The transfer value and the value of other aggregable funds do not exceed the amount which is sufficient to provide the maximum approvable benefit for the transferee. Maximum approvable benefit means, for the purpose of an overseas transfer, the...
maximum permissible benefit at the date the member left pensionable service plus any appropriate increases in respect of the period from then until the date of transfer. Where the member's rights to benefits have been reduced by a pension sharing order, agreement or equivalent provision, this maximum approvable benefit must take account of any reduction required for the value of the negative deferred pension as at the date of transfer. A reduction will be required where the member was not a moderate earner (as defined in SI 2000 No 1085) at the date of the divorce/annulment.

- The transfer value does not include an asset which is a loan made by the UK scheme trustees to an employer that is participating, or has participated, in the scheme or to an associated employer.

- Where a member does not have a cash equivalent right to a transfer the rules of the transferring scheme must permit the transfer of his/her rights to an overseas scheme. A member has a cash equivalent right to a transfer provided his/her pensionable service ceases at least one year before normal pension age under the provisions of the Pension Schemes Act 1993.

Where any of these conditions is not met a transfer is not permissible. No transfer application should be submitted to IR SPSS.

Transfers of contracted-out rights and safeguarded rights must also meet the requirements of DWP Regulations. UK scheme trustees and administrators should notify the Inland Revenue National Insurance Contributions Office of transfers of contracted-out rights as follows

- GMP and/or post 97 COSR rights - complete form CA1890. See Termination of Contracted-out Employment Manual, CA14, for further information.


Completed forms CA 1890 and CA1895 should be sent to Inland Revenue National Insurance Contributions Office, Contracted-out Employment Group (COEG), Longbenton, Newcastle upon Tyne NE98 1ZZ.

The National Insurance Contributions Office does not need to be notified of transfers of safeguarded rights, but they can only be transferred if DDWP Regulatory requirements are met.

The telephone number for general enquiries on transfers of contracted-out rights and safeguarded rights is 0191 225 0150.

B. Overseas transfers meeting the conditions of the reciprocal agreements

A6.3 The Inland Revenue has reciprocal transfer agreements with Jersey, the Isle of Man, Guernsey and the Republic of Ireland. The texts of these agreements are set out in forms PS 119,120,121 and 122 respectively (see Appendix II).

A64Where the proposed transfer is permitted under the terms of the reciprocal agreement and the conditions in A above are satisfied, the transfer may be made without seeking the specific consent of IR SPSS. The transferring scheme administrator/trustees should arrange for the information evidencing the meeting of the conditions in the reciprocal agreement and those in A above to be kept for a period of six years from the date of transfer.

A6.5 Where the proposed transfer does not meet the requirements of the particular reciprocal agreement, the transfer must be considered under the procedure at either C or D below.

C. Transfers to certain schemes for staff of European Union institutions

A66There are special arrangements for transfers to:
• the pension scheme for the staff of the institutional bodies of the European Union
• the European Investment Bank staff pension scheme
• the pension scheme of the European Patent Office.

The conditions that apply to such transfers are with two exceptions, the same as those set out in A and in D.1 below. The transferee must have left the UK, but need not have done so on a permanent basis. And, although the scheme and the transferee have to be established/resident abroad, they do not have to be in the same European Union country.

A6.7 Where the conditions are met a transfer may be made without the specific approval of IR SPSS. The transferring scheme administrator/trustees should arrange for the information evidencing the meeting of those conditions to be kept for a period of six years from the date of the transfer. For further guidance about evidence requirements see D.1 below.

A68 Where any of the conditions is not met a transfer is not permissible. No transfer application should be submitted to IR SPSS.

D. Other overseas transfers

I. Further transfer conditions: evidence required for satisfaction of the conditions

A6.19 Where any of the following conditions is not met the transfer is not permissible. No transfer application should be submitted to IR SPSS.

• The transferee has left the UK on a permanent basis with no intention of returning to the UK to work or to retire.
  Evidence: written confirmation from the transferee.

• The transferee is already in employment or self-employment overseas. This condition is not met if the transferee is working for an overseas branch or representative office of a UK tax resident employer.
  Evidence: a letter from the overseas employer (or if self-employed a copy contract for services rendered or a copy of an invoice of services or goods provided)

• The transferee's employment arrangements have been severed completely, and the transferee does not exercise any self-employment within the UK.
  Evidence:
  - written confirmation from the transferee that he/she holds no current employment either in the UK or overseas with a UK tax resident employer, that he/she holds no current employment with the UK branch or representative office of an overseas employer, and that he/she does not exercise any self-employment in the UK, and
  - the payroll record showing when the transferee left the employment to which the scheme relates, and
  - if the transferee was in self-employment after he/she left the employment to which the transferring scheme relates, a copy of the cessation accounts of the transferee's business.

• The transferee and the receiving scheme are resident/established in the same country.
  Evidence: written confirmation of residence from the transferee, and written confirmation of the country of establishment of the overseas scheme from its administrator (or equivalent).
• The overseas scheme(s) has/have been authorised or recognised as a pension scheme by the relevant tax or supervisory authority of the country in which it is / they are established. The transferee’s rights can be transferred to more than one overseas scheme.

Evidence: a copy of the letter issued by the overseas tax or supervisory authority (either the overseas scheme’s letter of authorisation/recognition or a letter from the authority providing confirmation of authorisation/recognition).

• The overseas scheme is capable of receiving the transfer. This condition cannot be met if the overseas scheme is a book reserve scheme, an unfunded scheme or a “pay as you go scheme”. Transfers to US "qualified" retirement plans, including individual retirement arrangements (IRAs), cannot be made as such plans are not permitted to accept funds transferred or "rolled over" from UK schemes.

Evidence: written confirmation from the overseas scheme administrator (or equivalent).

II. Transfers not requiring the prior consent of IR SPSS

A6.10 If at the date of requesting a transfer the member is a controlling director or a high earner the transfer cannot be made without the prior consent of IR SPSS. Where that is the case, go to D.III below.

A6.11 Transfers of the rights of other members can be made without obtaining the prior consent of IR SPSS, provided all of the conditions in A and D.I are satisfied. The administrator/trustees should arrange for the information evidencing the meeting of the conditions in A and D.I to be kept for a period of six years from the date of transfer. A copy of the information evidencing that the member was not a controlling director or a high earner should be kept for a similar period.

A6.12 For members who are not controlling directors and for whom no evidence of remuneration is available the administrator/trustee may rely on a certificate provided by the member in the format at E.I below. The transfer can then be made provided all of the conditions in A and D.I are satisfied, but the administrator/trustees must send a copy of the E.I certificate to IR SPSS within 90 days of the transfer.

III. Transfers requiring the prior consent of IR SPSS

A6.13 In order for IR SPSS to consider whether the transfer is permissible the transferring scheme administrator/trustees will need to provide it with the following information:

• The evidence specified at D.I above and confirmation that the conditions in the first bullet point (and, if appropriate, the fifth bullet point) in A above are satisfied.

About the transferee

• His/her name and National Insurance number, and the last Schedule E District and reference number applicable to him/her.

• The name and IR SPSS reference of any other approved occupational scheme providing aggregable benefits (including Free standing Additional Voluntary Contribution Schemes). The name of the insurer, and the policy number, of any buy-out policy bought by an approved occupational scheme which was providing aggregable benefits. The name and IR SPSS reference number of any personal pension scheme which holds a transfer value from an approved occupational scheme which was providing aggregable benefits.

• A certificate (or letter on headed paper) from the tax authorities of the overseas country stating that the transferee is resident there for the purposes of income tax, or proof of the granting to the transferee of permanent resident status in the overseas country. If the documentation is not in English it should be accompanied by a translation.
acceptable format for the tax residence certificate is shown in E.II below (a letter should provide similar assurance).

About the transfer value

- The amount of the transfer value from the transferring scheme.
- A copy of the written actuarial advice or the calculations showing that the transfer amount does not exceed the amount required to provide the maximum approvable benefit.
- Full details of any part of the proposed transfer payment which is not in the form of cash, including a current open market valuation for each such asset.

E. Acceptable formats of certificates

A6.14

I. Certificate relating to high earner condition in D.II

Member's name:

Member's National Insurance number:

I certify that the total amount of remuneration paid to me in any year of assessment falling (wholly or partly) during the period of six years prior to the date on which the transfer request was made did not exceed [Ex – insert here the figure for the permitted maximum for the year of assessment in which the transfer request was made].

Member's signature:

Date:

Explanatory Note

"Remuneration" should be construed in accordance with section 612(1) of the Income and Corporation Taxes Act 1988. For the purposes of this certificate it is limited to remuneration in respect of any employment to which the proposed transfer payment relates. You should ignore any income that is not assessable to income tax under Schedule E.

Information to be provided by the administrator/trustees of the transferring scheme or, if the transfer is from a buy-out policy, by the insurance company

Name of transferring scheme or name of insurer of buy-out policy:

IR SPSS reference of transferring scheme or number of buy-out policy:

Name of overseas scheme:

Amount of transfer value:

Date of transfer request:

II. Certificate referred to in fourth bullet point in D.III

As an official representative of the Taxation Authorities of [name of overseas country] I certify that [name of transferee] is resident in [name of overseas country] for the purposes of income tax.

Signature:
F. Glossary

A6.15 The following definitions for use with this Appendix only (unless stated otherwise legislative references are to the Income and Corporation Taxes Act 1988)

Additional Voluntary Contributions are contributions by an employee other than Basic or Contractual Contributions i.e. over and above contributions (if any) required as a condition of membership and include any such contribution paid under a Free standing Additional Voluntary Contribution Scheme.

Administrator is defined in section 611AA.

Associated Employers are defined in section 590A(3) and (4) as companies where one is directly or indirectly controlled by the other or both or all are controlled by a third person. Control is construed in accordance with section 416 in relation to close companies or with section 840 for other corporate bodies.

Contracted-Out Rights are such rights, under or derived from an occupational pension scheme, or an appropriate scheme, as fall within the following categories:

- entitlement to payment of, or accrued rights to, guaranteed minimum pensions (section 8(2) of the Pension Schemes Act 1993 refers);
- section 9(2B) rights (section 9(2B) of the Pension Schemes Act 1993 refers);
- protected rights (section 10 of the Pension Schemes Act 1993 refers); or
- any of the rights above which themselves derive from any of those rights which have been the subject of a transfer payment.

Controlling Director is defined in paragraph 5(5) of Schedule 23 as a person who is a director and within paragraph (b) of section 417(5) of ICTA 1988 in respect of any employment to which the proposed transfer payment relates. For practical purposes this means a member who, at any time within 10 years of requesting a transfer of accrued pension rights to an overseas scheme, has been a director, and either on his own or with one or more associates has beneficially owned or been able to control, directly, indirectly or through other companies, 20% or more of the ordinary share capital of the company. For the purposes of this definition:

(i) "Associate" means in relation to a director, any relative (i.e. spouse, forebear, issue or sibling) or partner (within the meaning of the Partnership Act 1890), the trustees of any settlement in relation to which the director is, or any relative of his or her (living or dead) is or was, a settlor and, where the director is interested in any shares or obligations of the company which are subject to any trust, or are part of the estate of a deceased person, the trustees of the settlement concerned or, as the case may be, the personal representatives of the deceased, and

(ii) The expression "either on his own or with one or more associates" requires a person to be treated as owning or, as the case may be, controlling what any associate owns or controls even if he or she does not own or control share capital on his or her own.
DWP Regulations are the Contracting-out (Transfer and Transfer Payment) Regulations 1996, the Protected Rights (Transfer Payment) Regulations 1996 and the Pension Sharing (Pension Credit Benefit) Regulations 2000 as amended by the Contracting-out, Protected Rights and Safeguarded Rights (Transfer Payment) Amendment Regulations 2005.

Employment Arrangements means the arrangements whereby the transferee currently serves:

- in the UK or elsewhere for a UK tax resident employer as an employee within the meaning given in section 612, and/or
- in the UK as an employee within the meaning of section 612 for the UK branch or representative office of an overseas tax resident employer.

N.B. The references to ex-employees in section 612 are to be excluded for the purpose of this definition.

Equivalent Pension Benefit has the meaning given by section 57(1) of the National Insurance Act 1965.

Free standing Additional Voluntary Contribution Scheme means a retirement benefits scheme approved by virtue of section 591(2)(h), established by a pension provider or the trustees of an approved centralised scheme for non-associated employers to which the employer does not contribute and which provides benefits additional to those provided by a scheme to which the employer does contribute.

High Earner is a member whose total amount of remuneration in any year of assessment falling (wholly or partly) during the period of six years prior to the date on which the transfer request was made exceeded the permitted maximum for the year of assessment in which the transfer request was made.

Institutional Bodies of the European Union means, for the purposes of this Appendix, the Commission, the European Parliament, the Council, the Court of Justice, the Court of Auditors, the Economic and Social Committee and the Committee of the Regions, the European University Institute in Florence, as well as any other organisation devoted to furthering the European Communities’ interests whose personnel are subject to the Staff Regulations of the Officials of the European Communities.

Negative Deferred Pension is the current value in terms of pension of a pension debit as revalued under section 31 Welfare Reform and Pensions Act 1999.

Normal Pension Age is defined in section 180 of the Pension Schemes Act 1993.

Permitted Maximum is defined in section 590C. The figure for 2000/2001 is £91,800.

Pensionable Service means service for an employer in respect of which benefits (other than benefits payable solely on death before retirement) accrue under an approved scheme.

Personal Pension Scheme means a scheme approved under Chapter IV, Part XIV.

Remuneration should be construed in accordance with section 612(1), and for the purposes of this Appendix is limited to remuneration in respect of any employment to which the proposed transfer payment relates. Any income that is not assessable to income tax under Schedule E is to be ignored.

Member requests a transfer of accrued rights.

Are all of the conditions in A met?

Yes: Make transfer and keep records

No: No overseas transfer can be made

Is the transfer permitted under a reciprocal agreement?

Yes: Make transfer and keep records

No: No overseas transfer can be made

Are all of the conditions referred to in C met?

Yes: Make transfer and keep records

No: No overseas transfer can be made

Is the transfer to a scheme for staff of EU institutions?

Yes: Make transfer and keep records

No: No overseas transfer can be made

Are all of the conditions in D I met?

Yes: Make transfer and keep records

No: No overseas transfer can be made

Send transfer application to PSO with information specified in D III. PSO will advise whether or not the transfer can be made.

Is the transferee a controlling director or a high earner? (see D II)

Yes: Make transfer and keep records

No: No overseas transfer can be made
## Appendix VII. Reporting checklist

### Checklist of Reports Required by IR SPSS

<table>
<thead>
<tr>
<th>Subject</th>
<th>PN ref</th>
<th>Form (where available)</th>
<th>Time limit for notification (where applicable)</th>
</tr>
</thead>
<tbody>
<tr>
<td>All members</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Change of NRA for member with <em>continued rights</em></td>
<td>6.15</td>
<td>-</td>
<td><em>IR SPSS to be notified before</em> any action is taken</td>
</tr>
<tr>
<td>NRA less than 60</td>
<td>6.7</td>
<td>-</td>
<td><em>IR SPSS to be notified before</em> any action is taken</td>
</tr>
<tr>
<td>Temporary absence / secondment outside normal conditions</td>
<td>3.15</td>
<td>-</td>
<td><em>IR SPSS to be notified before</em> any action is taken</td>
</tr>
<tr>
<td>Secondment abroad outside normal conditions</td>
<td>15.9</td>
<td>-</td>
<td><em>IR SPSS to be notified before</em> any action is taken</td>
</tr>
<tr>
<td>Benefits</td>
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<td></td>
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<tr>
<td><em>Final Remuneration</em></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>- fluctuating emoluments in single year only</td>
<td>App 1</td>
<td>-</td>
<td><em>IR SPSS to be notified before</em> any action is taken</td>
</tr>
<tr>
<td>- benefits-in-kind not assessed to income tax</td>
<td>App 1</td>
<td>-</td>
<td><em>IR SPSS to be notified before</em> any action is taken</td>
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<tr>
<td>Commutation</td>
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<td></td>
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<tr>
<td>- tax charge on triviality (Reg 10)</td>
<td>16.6</td>
<td>1(SF) (4/01)</td>
<td>30 days after end of year of assessment</td>
</tr>
<tr>
<td>- tax charge on triviality (Reg 11)</td>
<td>16.7</td>
<td>2(SF) (4/01)</td>
<td>180 days after the end of the chargeable period of the insurance company</td>
</tr>
<tr>
<td>- tax charge on serious ill-health (Reg 10)</td>
<td>16.6</td>
<td>1(SF) (4/01)</td>
<td>30 days after the end of the year of assessment</td>
</tr>
<tr>
<td>- tax charge on serious ill-health (Reg 11)</td>
<td>16.7</td>
<td>2(SF) (4/01)</td>
<td>180 days after the end of the chargeable period of the insurance company</td>
</tr>
<tr>
<td>- individual commutation factors</td>
<td>7.59-56</td>
<td>-</td>
<td><em>IR SPSS to be notified before</em> any action is taken</td>
</tr>
<tr>
<td><em>Incapacity</em> - partial recovery</td>
<td>App IV</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>Former partner</td>
<td>3.5</td>
<td>-</td>
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<tr>
<td>Subject</td>
<td>PN ref</td>
<td>Form (where available)</td>
<td>Time limit for notification (where applicable)</td>
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<tr>
<td>--------------------------------</td>
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<td>------------------------</td>
<td>-----------------------------------------------</td>
</tr>
<tr>
<td>Change of Scheme particulars</td>
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</tr>
<tr>
<td>Name of scheme</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Trustees</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Principal employer – change of name or address (Reg 6)</td>
<td>21.5</td>
<td>PS 256 (4/01)</td>
<td>180 days after the end of the scheme year</td>
</tr>
<tr>
<td>Change of Principal Employer</td>
<td>16.8</td>
<td>PS 257 (4/01)</td>
<td>180 days after the end of the scheme year</td>
</tr>
<tr>
<td>Participating employer</td>
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</tr>
<tr>
<td>- admission (Reg 6)</td>
<td>21.5</td>
<td>PS 274 (4/01)</td>
<td>180 days after the end of the scheme year</td>
</tr>
<tr>
<td>- admission - Simplified Scheme (Reg 6)</td>
<td>22.34</td>
<td>PS 403 (4/01)</td>
<td>180 days after the end of the scheme year</td>
</tr>
<tr>
<td>- cessation</td>
<td>14.10</td>
<td>PS 199 (6/01)</td>
<td></td>
</tr>
<tr>
<td>- change of name or address (Reg 6)</td>
<td>21.5</td>
<td>PS 256 (4/01)</td>
<td>180 days after the end of the scheme year</td>
</tr>
<tr>
<td>- retention on change of circumstances (Reg 6)</td>
<td>21.5</td>
<td>PS 256 (4/01)</td>
<td>180 days after the end of the scheme year</td>
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<tr>
<td>- temporary participation</td>
<td>21.6</td>
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<td></td>
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<tr>
<td>Contributions</td>
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<tr>
<td>Employer contributions holiday for more than 2 years</td>
<td>5.4</td>
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<td></td>
</tr>
<tr>
<td>Special contributions - (Reg 7)</td>
<td>5.7-9</td>
<td>PS 251 (4/01)</td>
<td>180 days after the end of the scheme year</td>
</tr>
<tr>
<td>Refund of employee contributions (Reg 10)</td>
<td>4.14 &amp;16.6</td>
<td>1(SF) (4/01)</td>
<td>30 days after the end of the year of assessment</td>
</tr>
<tr>
<td>Refund of employee contributions (Reg 11)</td>
<td>16.7</td>
<td>2(SF) (4/01)</td>
<td>180 days after the end of the chargeable period of the insurance company</td>
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<tr>
<td>Refund of AVCs (Reg 10)</td>
<td>16.6</td>
<td>1(SF) (4/01)</td>
<td>30 days after the end of the year of assessment</td>
</tr>
<tr>
<td>Refund of employer contributions paid in error (where it is outside the criteria in PN 5.17)</td>
<td>5.17</td>
<td>-</td>
<td><em>IR SPSS to be notified before any action is taken</em></td>
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<tr>
<td>Subject</td>
<td>PN ref</td>
<td>Form (where available)</td>
<td>Time limit for notification (where applicable)</td>
</tr>
<tr>
<td>---------------------------------</td>
<td>--------</td>
<td>------------------------</td>
<td>-----------------------------------------------</td>
</tr>
<tr>
<td><strong>Controlling directors</strong></td>
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<tr>
<td>Admission (Reg 8)</td>
<td>3.8</td>
<td>PS 255 (4/01)</td>
<td>180 days after the end of the scheme year</td>
</tr>
<tr>
<td>Retention of member who becomes a controlling director (Reg 8)</td>
<td>3.8</td>
<td>PS 255 (4/01)</td>
<td>180 days after the end of the scheme year</td>
</tr>
<tr>
<td>SIH commutation (Reg 9)</td>
<td>8.22</td>
<td>-</td>
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<tr>
<td><strong>Incapacity</strong> retirement (Reg 9)</td>
<td>6.3</td>
<td>-</td>
<td><strong>IR SPSS to be notified before</strong> any action is taken</td>
</tr>
<tr>
<td>Continuous service</td>
<td>7.21</td>
<td>PS 155 (3/03)</td>
<td>Within 6 years of leaving the first employer on a change of employment.</td>
</tr>
<tr>
<td><strong>Discontinuance</strong></td>
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<tr>
<td>Particulars</td>
<td>14.3</td>
<td>PS 199 (6/01)</td>
<td></td>
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<tr>
<td>Winding-up at interim stage</td>
<td>14.11</td>
<td>PS 160 (4/01)</td>
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<tr>
<td>Paid-up at interim stage</td>
<td>14.11</td>
<td>PS 161 (4/01)</td>
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<td><strong>Non-associated Employers</strong></td>
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<tr>
<td>Establishment of scheme</td>
<td>21.21</td>
<td>-</td>
<td><strong>IR SPSS to be notified before</strong> any action is taken</td>
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<tr>
<td><strong>Repayment to Employer</strong></td>
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<tr>
<td>Particulars (Reg 10)</td>
<td>16.6</td>
<td>1(SF) (4/01)</td>
<td>30 days after the end of the year of assessment</td>
</tr>
<tr>
<td>Particulars (Reg 11)</td>
<td>16.7</td>
<td>2(SF) (4/01)</td>
<td>180 days after the end of the chargeable period of the insurance company</td>
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<tr>
<td>Refund of surplus assets or excess policy proceeds</td>
<td>13.19-25</td>
<td>-</td>
<td><strong>IR SPSS to be notified before</strong> any action is taken</td>
</tr>
<tr>
<td><strong>Rule changes</strong></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Rule amendments or Documentation Certificate</td>
<td>16.12 &amp; 18.14</td>
<td>PS 6 (4/01)</td>
<td></td>
</tr>
<tr>
<td><strong>Transfers</strong></td>
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<tr>
<td>Transfer from a scheme seeking approval</td>
<td>10.25</td>
<td>-</td>
<td><strong>IR SPSS to be notified before</strong> any action is taken</td>
</tr>
<tr>
<td>Subject</td>
<td>PN ref</td>
<td>Form (where available)</td>
<td>Time limit for notification (where applicable)</td>
</tr>
<tr>
<td>------------------------------------------------------------------------</td>
<td>--------</td>
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<td>------------------------------------------------</td>
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<tr>
<td>Transfer to a scheme seeking approval (exceptional circumstances)</td>
<td>10.24</td>
<td>-</td>
<td>IR SPSS to be notified before any action is taken</td>
</tr>
<tr>
<td>Until 6/4/2003 transfer to a SSAS or between SSAS where the transfer either alone or 365 day total is £250,000 or more.</td>
<td>10.24</td>
<td>PS 7050</td>
<td>IR SPSS to be notified before any action is taken</td>
</tr>
<tr>
<td>Until 6/4/2003 transfer from a SSAS where the transfer either alone or 365 day total is £250,000 or more.</td>
<td>10.24</td>
<td>PS 7050</td>
<td>IR SPSS to be notified before any action is taken</td>
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<tr>
<td>Block transfers</td>
<td>10.36</td>
<td>PS 295 (4/01)</td>
<td>IR SPSS to be notified before any action is taken</td>
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<tr>
<td>Overseas schemes - transfers from</td>
<td>10.40</td>
<td>-</td>
<td>IR SPSS to be notified before any action is taken</td>
</tr>
<tr>
<td>Overseas schemes - transfers to (in the case of high earners/controlling directors)</td>
<td>10.39 &amp; App VIB</td>
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<tr>
<td>Sec 615 Ch 1 Pt XIV ICTA 1988 schemes – from</td>
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<td>-</td>
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<tr>
<td>Second and subsequent transfers – continued rights members</td>
<td>App III (A3.5)</td>
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<tr>
<td>Transfer payments of £250,000 or more in aggregate (regs 11A &amp; 11B)</td>
<td>16.16a – 16.16b</td>
<td>7050</td>
<td>28 days</td>
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</table>

### Additional requirements for Insured Schemes

<table>
<thead>
<tr>
<th>Loans to employers</th>
<th>16.88</th>
<th>PS 8 (4/01)</th>
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<tbody>
<tr>
<td>Loans - foreclosure</td>
<td>16.89</td>
<td>-</td>
<td>30 days</td>
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<tr>
<td>Loans - interest / capital outstanding</td>
<td>16.90</td>
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<td>If outstanding 90 days after the due date for payment, report to IR SPSS within a further 30 days</td>
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<td>Loans - amendment to loan agreement</td>
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<td>PS 8 (4/01)</td>
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<td>Loans - cessation of contributions</td>
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<td>Subject</td>
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<td>Time limit for notification (where applicable)</td>
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<td><strong>Additional requirements for Self-administered Schemes</strong> - See below for Small Self-administered Schemes (SSASs)</td>
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<td>Common investment fund</td>
<td>17.12</td>
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<td>Actuarial Valuation Reports</td>
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<tr>
<td>- schemes covered by Pension Scheme Surpluses (Valuation) Regulations 1987</td>
<td>16.13</td>
<td>PS 162 (4/01)</td>
<td>2 years of &quot;as at&quot; date</td>
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<td>- other schemes</td>
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<td>Surplus</td>
<td>13.19</td>
<td>PS 290 (4/01)</td>
<td>6 months of signing AVR or PS162</td>
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<td><strong>Additional requirements for SSASs</strong></td>
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<tr>
<td>Actuarial Valuation Reports - Regs</td>
<td>16.13 &amp; 20.35</td>
<td>-</td>
<td>1 year of &quot;as at&quot; date</td>
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<tr>
<td>Reports under SSAS Regulations</td>
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<tr>
<td>Pensioneer Trustee</td>
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<tr>
<td>- cessation</td>
<td>20.11</td>
<td>-</td>
<td>30 days</td>
</tr>
<tr>
<td>- appointment</td>
<td>20.11</td>
<td>-</td>
<td>30 days</td>
</tr>
<tr>
<td><strong>Reports under Information Powers Regulations</strong></td>
<td></td>
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<tr>
<td>Transactions</td>
<td></td>
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<tr>
<td>- property (Reg 5)</td>
<td>20.49</td>
<td>PS 7012 (4/01)</td>
<td>90 days</td>
</tr>
<tr>
<td>- loans (Reg 5)</td>
<td>20.49</td>
<td>PS 7013 (4/01)</td>
<td>90 days</td>
</tr>
<tr>
<td>- shares in employer (Reg 5)</td>
<td>20.49</td>
<td>PS 7014 (4/01)</td>
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<td>- shares in unlisted Co. (Reg 5)</td>
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<td>PS 7014 (4/01)</td>
<td>90 days</td>
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<td>- borrowings (Reg 5)</td>
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<td>PS 7015 (4/01)</td>
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<tr>
<td>- miscellaneous (Reg 5)</td>
<td>20.49</td>
<td>PS 7016 (4/01)</td>
<td>90 days</td>
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</table>

Appendix VIII. Part A. Amended ABI Funding Guidelines

INTRODUCTION

a8a.1.1 These notes set out the funding method known as the:

Maximum Permissible Funding Rates on Insured Money Purchase Schemes (ABI 1996 Method as amended 31 March 1998 and 21 December 2001)

This method has been agreed with 'IR Savings, Pensions, Share Schemes' (*IR SPSS*), which the office previously known as the Pension Schemes Office is now part of, to calculate maximum joint regular contributions by employer and employee to fully insured money purchase schemes from 1 June 1996 for approvable retirement benefits, as subsequently amended ("the ABI 1996 method as amended 31 March 1998 and 21 December 2001"). The method updates and replaces the funding basis introduced in 1994 ("the ABI 1994 method"), which was included as Appendix VIII to the Practice Notes IR12 (2001) and schemes where contributions were limited by the ABI 1994 method could move to the original (ie prior to the 31 March 1998 amendments) ABI 1996 method from 1 June 1996. Allowance is made for the earnings cap (the 'Permitted Maximum') where applicable.

a8a.1.2 The 31 March 1998 amendments concern the de minimis limit and are described in paragraphs a8a.3.1 – a8a.3.8

a8a.1.3 The 21 December 2001 amendments relate primarily to the introduction of pension sharing on divorce. There are a few other amendments which update references.

a8a.1.4 The method for calculating maximum special contributions to insured money purchase schemes is described in paragraphs a8a.7.1 – a8a.7.4.

*Terms appearing in italics are defined in the glossary of the Practice Notes IR12 (2001).

TRANSITIONAL ARRANGEMENTS FOR MARCH 1998 AMENDMENTS

a8a.2.1 These transitional arrangements ceased to apply to any contract from 1 September 1999, but reference is included here for information.

a8a.2.2 Contracts in force prior to 1 September 1994 were not required to comply fully with the ABI 1996 method as amended 31 March 1998 until 1 September 1999, at which time the maximum joint regular contributions by employer and employee should have been no higher than the maximum allowed under the new method. There were, however, three events under the transitional arrangements which would have triggered the ABI 1996 method as amended 31 March 1998:

- any proposal for an increase in contributions before 1 September 1999, whether by increment or new contract, meant that the whole contract had to be tested against this method as at the date the increase was due to be made. If the proposed contribution was more than the maximum, then the increase should not have been made, but the existing contribution did not have to be reduced at that time. If the existing contribution was less than the maximum under the ABI 1996 method as amended 31 March 1998, but the proposed increase would have taken it over, then a partial increase up to the maximum could be made

- payment of a special contribution
undisclosed *retained benefits* coming to light which, when expressed in terms of pension, exceeded £260 in aggregate, or (for Class C members only) lump sums of £2,500 in aggregate.

a8a.2.3 It should be noted that a “trigger event” applied only to the particular member to whom it related, and did not mean that other members of the scheme (if any) had to be tested at that time against the ABI 1996 method as amended 31 March 1998.

a8a.2.4 If contributions ceased or were temporarily reduced, a funding test under the ABI 1996 method as amended 31 March 1998 should have been applied immediately if the resumed contributions were at a higher level than before the interruption or reduction.

a8a.2.5 A replacement contract would have remained under these transitional arrangements if, and only if, one of the reasons for continuation set out in Practice Notes IR12 (2001), Appendix III, applied. This was irrespective of which maximum limits basis applied to the member.

a8a.2.6 Separate transitional arrangements applied to insured schemes which converted to small self-administered schemes (SSASs) before 1 June 1996 and to pre-September 1994 insured schemes which converted to SSASs after 1 June 1996. These arrangements are described in the guidance notes relating to the SSAS 1996 method which are included as Appendix IX to the Practice Notes IR12 (2001).

**DE MINIMIS LIMIT**

a8a.3.1 This limit does not apply if any defined benefit schemes are involved.

a8a.3.2 No check against the maximum funding rate is required where the annual aggregate contributions to all schemes, excluding contributions for death in service benefits and contributions to personal pension / stakeholder contracts which are subject to the "concurrency" rules in section 632B ICTA 1988, for the same employment do not exceed 17½% of *Remuneration* (within the *Permitted Maximum* in all cases), subject to contributions (including special contributions) not having been at a higher amount than the figure determined from this limit in any earlier year. Contributions to *free standing additional voluntary contribution schemes* must be taken into account for this purpose.

a8a.3.3 For the purpose of this limit, age-related rebates (that is, the excess over the flat-rate percentage rebate) made under the Social Security (Reduced Rates of Class 1 Contributions and Rebates) (Money Purchase Contracted-out Schemes) Order 1996 (SI 1996/1055) and minimum contributions to appropriate personal pensions may be ignored.

a8a.3.4 There is no corresponding de minimis limit for *special contributions*.

a8a.3.5 Prior to 31 March 1998 a different de minimis limit applied, linked principally to a flat contribution of £5,000 or £6,000 per annum. This was withdrawn by the Inland Revenue because of abuse.

**Transitional Arrangements for March 1998 amendments**

a8a.3.6 For individuals for whom a scheme was established before 31 March 1998, or who joined a scheme before that date, the previous de minimis test could be applied.

a8a.3.7 Providing there was no increase in the contribution rate (and subject to the following paragraph) three year reassessments for such individuals which fell due prior to 31 March 2001 could also be carried out by reference to the previous de minimis test. However, if contributions were to be increased, the new test had to be applied at the reassessment date.

a8a.3.8 All pension arrangements for individuals to which the previous de minimis test was applied before 31 March 1998 had to, in any event, satisfy the new test by 31 March 2001, or had instead to be subject to a full funding check by reference to the ABI 1996 Method as amended 31 March 1998.
CURRENT VALUATION OF EXISTING ASSETS (V)

a8a.4.1 If the maximum funding rate is being assessed as at the anniversary of the commencement of the policy or as at a 'specified date' for which a cash equivalent has been disclosed in accordance with the Disclosure of Information Regulations -SI 1996/1655 Schedule 2 paragraph 6) the value of the contract is to be taken as the transfer value which would be available if the contract ceased on that day.

a8a.4.2 If the maximum funding rate is being assessed on a date other than the policy anniversary or a 'specified date' then the value of the contract is taken as the transfer value at that date. If this is not readily available the value of the assets may be taken as the transfer value at the policy anniversary or 'specified date', increased by the premiums received between that date and the date of assessment, all accumulated at the rate of 8.5% per annum compound.

a8a.4.3 Where the maximum funding rate is being reassessed part way through the scheme year, policy year or company accounting year etc (as the case may be) in respect of which maximum contributions are determined and monitored, V may be reduced by the amount of annual contributions already paid in that year. Only the balance of the revised maximum contribution then calculated may be paid in the remainder of that year, with the revised maximum funding rate applying from the next year.

a8a.4.4 Assets under other money purchase (including self-administered) schemes relating to the same employment are to be brought into account. This includes age-related rebates made under the Social Security (Reduced Rates of Class 1 Contributions and Rebates) (Money Purchase Contracted-Out Schemes) Order 1996 (SI 1996/1055). In addition, for Class A members, the value of benefits from all connected schemes and associated employments must be brought into account as explained in PN 7.26. Assets under free standing additional voluntary contribution schemes (but not in-house additional voluntary contributions) and under personal pension / stakeholder schemes subject to the "concurrency" rules in section 632B ICTA 1988, may be ignored. Concurrent benefits from defined benefit schemes are dealt with in paragraphs a8a.6.20 – a8a.6.22 below.

a8a.4.5 Any pension debit arising as a result of the member's pension rights being shared on divorce, must also be brought into account, unless the member falls within the administrative easement described in PN 7.7, in which case the pension debit can be ignored. Appendix XIII to the Practice Notes IR 12 (2001) demonstrates the methodology to be used to calculate "pension debits".

a8a.4.6 Where PN 7.10 applies in determining maximum benefits, the value of retirement annuities or personal pension benefits is to be taken as the transfer value at the date of assessment (or if exceptionally a transfer value is not available, the present value of the projected benefits at retirement calculated on a basis consistent with the financial assumptions specified in paragraph a8b.2.1 of Part B to these notes).

SPECIAL CONTRIBUTIONS(S)

a8a.5.1 The amount of any special contribution which is to be paid at the time of calculation is also to be taken into account as indicated in paragraphs a8a.6.20 – a8a.6.22 below. The method for calculating the maximum special contribution is described in paragraphs a8a.7.1 – a8a.7.4.

METHOD OF CALCULATION

a8a.6.1 The actuarial formulae corresponding to Factors [1] to [5] are attached as Part B to these notes.

Value of Retained Benefits (R)

a8a.6.2 The figures represented by R1 and R2 in paragraphs a8a.6.8 – a8a.6.19 below are arrived at as follows.
a8a.6.3 R1 = transfer value of the retained benefits at the assessment date / Factor [1] and

a8a.6.4 R2 = transfer value of the retained benefits at the assessment date / Factor [3].

a8a.6.5 Retained benefits should include any pension debit applied against those benefits (unless
the administrative easement in PN 7.7 applied at the date of divorce).

a8a.6.6 Retained benefits may be ignored (ie R1 and R2 taken as zero) in the circumstances
described in PN 7.5 and 7.6. If the retained benefit is already in payment, then it should be taken
at its current value (and including the amount of any lump sums already paid - PN 16.38).

Value of the pension debit (if any) (D)

a8a.6.7 This is calculated as follows:

- Calculate the notional deferred pension equivalent of the pension debit at the time of
divorce. This is the actual pension debit divided by the appropriate value of Factor [5]
for the age at the date of divorce.

- Increase the notional deferred pension at the time of divorce by the actual rate of
statutory revaluation which has applied between that date and the date of the
maximum contribution rate calculation.

- Multiply the notional deferred pension, revalued as in (b) above, by factor [5] for the
age at the date of the maximum contribution rate calculation.

Calculation of the Maximum Permissible Pension at the Normal Retirement Date

a8a.6.8 The calculation varies depending on which basis of Revenue limits applies ie post 1989
(Class A), pre 1 June 1989 (Class B), or pre 17 March 1987 (Class C) members. For Class A
members it is necessary to calculate separately the maximum permissible pension on the basis of
current remuneration (P1) and the current Permitted Maximum (P2).

a8a.6.9 Either "final remuneration" (as described in PN Appendix 1) or current remuneration can
be used for the calculations. There is no requirement to use just one approach where funding
checks are required for more than one member of a particular scheme.

a8a.6.10 Final remuneration should be used in every case for funding checks carried out in the
three year period immediately prior to normal retirement date.

a8a.6.11 Where contributions are to be fixed as level amounts for the period (to be no longer than
three years) until the next funding check, that can be reflected in the calculation of Factor [2] and
Factor [4] (which are defined in Part B). Otherwise, those contribution factors should allow for
remuneration to increase every year in line with the assumptions specified in that Part. It must be
noted that contributions may be fixed as level amounts only if "final remuneration" is used in the
calculation. If current remuneration is used, the maximum contribution must be expressed as a
percentage of current remuneration.

a8a.6.12 The maximum total benefits at normal retirement date derived from this calculation
applies to the aggregate benefits from all schemes relating to the current employment and for
Class A members associated employments / connected schemes.

Class A Members

a8a.6.13 (This basis will apply to virtually all new schemes and new entrants to existing schemes.)

a8a.6.14 P1 = The greater of

(a) NS (maximum 40)/60 x Remuneration¹ and
(b) the lesser of
   
   (i) NS (maximum 20)/30 x Remuneration\(^1\) and
   
   (ii) 2/3 x Remuneration\(^1\) - R1.

a8a.6.15 P2 = The greater of

(a) NS (maximum 40)/60 x Permitted Maximum and

(b) the lesser of

   (i) NS (Maximum 20)/30 x Permitted Maximum and
   
   (ii) 2/3 x Permitted Maximum - R2.

**Class B Members**

a8a.6.16 The calculation of P1 is the same as for Class A members.

a8a.6.17 The calculation of P2 is not required.

**Class C Members**

a8a.6.18 P1 = the greater of

(a) NS (maximum 40)/60 x Remuneration\(^1\) and

(b) the lesser of

   (i) the uplifted scale (PN 7.40) x Remuneration\(^1\) and
   
   (ii) 2/3 x Remuneration\(^1\) - R1.

a8a.6.19 The calculation of P2 is not required.

**Allowance for Concurrent Benefits under a Defined Benefit Scheme**

a8a.6.20 If the employee is a concurrent member of a defined benefit scheme in respect of the same employment then V must be increased by one of the following:-

- Where the maximum permissible pension at normal retirement date in accordance with paragraphs a8a.6.8 – a8a.6.19 is P1, by the value of the prospective pension under the defined benefit scheme (inclusive of any pension debit applied against that prospective pension under the defined benefit scheme, unless the PN 7.7 easement applied at the date of divorce) at normal retirement date based on current pensionable earnings under that scheme, or

- Where the maximum permissible pension at normal retirement date is P2, by the value of the prospective pension under the defined benefit scheme (inclusive of any pension debit applied against that prospective pension under the defined benefit scheme, unless the PN 7.7 easement applied at the date of divorce) at normal retirement date based on the current Permitted Maximum.

a8a.6.21 The value must be assessed on a basis consistent with that used for calculating the maximum contribution C below.

a8a.6.22 The pension equivalent of lump sum retirement benefits may be calculated using the 12:1 factor, regardless of the tax approval regime which applies and the escalation rate of the pension given up.
Calculation of the Maximum Regular Contribution (C)

a8a.6.23 For Class A members, the maximum regular contribution (C) is the lesser of the amounts calculated on the basis of Remuneration\(^1\) (C1) and the current Permitted Maximum (C2).

a8a.6.24 For Class B and C members, C1 always applies and C2 is not calculated.

\[
C1 = \frac{P1 \times \text{Factor [1]} - V - S - D}{\text{Factor [2]}} \times 1.05
\]

\[
C2 = \frac{P2 \times \text{Factor [3]} - V - S - D}{\text{Factor [4]}} \times 1.05
\]

a8a.6.25 For the purposes of C1, V should include money purchase assets and the value of prospective pensions from defined benefit schemes relating to the same employment (inclusive of any pension debit applied against that prospective pension under the defined benefit scheme, unless the PN 7.7 easement applied at the date of divorce).

a8a.6.26 For the purposes of C2 (Class A members only), V should include money purchase assets and the value of prospective pensions from defined benefit schemes relating to the same employment and from connected schemes and associated employments (inclusive of any pension debit applied against that prospective pension under the defined benefit scheme, unless the PN 7.7 easement applied at the date of divorce).

a8a.6.27 The amount calculated above for C is the maximum annual figure to all money purchase schemes relating to the current employment. The corresponding maximum monthly, quarterly and half-yearly amounts are 1/12, 1/4 and 1/2 of this figure respectively.

a8a.6.28 S is the actual special contribution paid, if any, as referred to in paragraph a8a.5.1 above.

a8a.6.29 This cannot exceed the maximum calculated as described in paragraphs a8a.7.1 – a8a.7.4, which, it should be noted, cannot be negative.

Calculation of the Maximum Future Contribution Rate (F)

a8a.6.30 Where the maximum future contribution is to be expressed as a percentage remuneration\(^1\) (but not where contributions are to be fixed amounts, until the next reassessment, where these paragraphs a8a.6.30 – a8a.6.32 do not apply) this is calculated as:

\[
100 \times \frac{C}{\text{Current Remuneration}^1}
\]

a8a.6.31 The contribution that can be paid in subsequent years will be F% of that year's remuneration\(^1\). If remuneration\(^1\) has decreased from the previous year then the maximum contribution that can be paid will reduce.

a8a.6.32 The maximum future contribution rate (F) applies to all insured money purchase schemes (including in-house additional voluntary contributions) relating to the current employment.
METHOD OF CALCULATION OF MAXIMUM SPECIAL CONTRIBUTIONS

a8a.7.1 *Special Contributions* should not be made to fund benefits in advance of the maximum justifiable by reference to service to date.

a8a.7.2 For a post 1989 (Class A) member the maximum is the lesser of $S_1$ and $S_2$ where

$$S_1 = \left( \frac{N}{NS} \times P_1 \times \text{Factor}[1] \right) - V - D$$

$$S_2 = \left( \frac{N}{NS} \times P_2 \times \text{Factor}[3] \right) - V - D$$

For Class B and C members $S_1$ always applies.

$P_1$ and $P_2$ are calculated as described in paragraphs a8a.6.1 - a8a.6.32.

a8a.7.3 If the employee is a concurrent member of a defined benefit scheme in respect of the same employment then $V$ must be increased by one of the following (in the same way as applies under paragraphs a8a.6.20 – a8a.6.22):

- Where the maximum permissible pension at *normal retirement date* in accordance with paragraphs a8a.6.8 - a8a.6.19 is $P_1$, by the value of the prospective pension under the defined benefit scheme (inclusive of any *pension debit* applied against that prospective pension under the defined benefit scheme, unless the PN 7.7 easement applied at the date of divorce) at *normal retirement date* based on current pensionable earnings under that scheme, or

- Where the maximum permissible pension at *normal retirement date* is $P_2$, by the value of the prospective pension under the defined benefit scheme (inclusive of any *pension debit* applied against that prospective pension under the defined benefit scheme, unless the PN 7.7 easement applied at the date of divorce) at *normal retirement date* based on the current *Permitted Maximum*.

a8a.7.4 It should also be noted that, for the purpose of paragraphs a8a.7.1 - a8a.7.4, any part of $V$ which originates from paragraphs a8a.6.20 - a8a.6.22 (ie that relates to concurrent benefits under a defined benefit scheme) can be reduced in proportion to $N/NS$.

REASSESSMENT OF MAXIMUM CONTRIBUTION LEVEL

3 Year Reassessment

a8a.8.1 The contribution rate must be reassessed within 3 years of the effective date at which C or F (as appropriate) has been established, or within 3 years of a de minimis check, unless it has been previously amended in accordance with paragraphs a8a.8.3 - a8a.8.5 or paragraph a8a.8.6 below (in which case the 3 year period runs from the date of the most recent change in C or F). Reassessment is not required when a member gets divorced but at the next reassessment date, any *pension debit* applied against that member's benefits must be brought into account, unless the member falls within the administrative easement described in PN 7.7, in which case the *pension debit* can be ignored.

a8a.8.2 The revised value of C or F must apply from the effective date of the test (increase or decrease) and, if necessary, future regular contributions reduced. A new 3 year period will then commence.
Increases in Regular Contribution

a8a.8.3 Reassessment is only required if the proposed total contribution rate exceeds F% based on the current Remuneration at the time of increase.

a8a.8.4 If the calculation indicates that F should be lower, the previously assessed value of F may be retained until a three year reassessment is made as described in paragraphs a8a.8.1 and a8a.8.2 above. If the calculation indicates that F is increased the revised value may be used immediately (and a new three year period will then commence for the purpose of paragraphs a8a.8.1 and a8a.8.2 above).

a8a.8.5 This section does not apply to the fixed amount basis.

Special Contributions

a8a.8.6 A reassessment of the maximum contribution must be made whenever a special contribution outside that allowed for at the time of the latest funding check is paid. The revised value of C or F as appropriate must apply immediately (increase or decrease) and, if necessary, future regular contributions reduced. A new 3 year period will commence for the purpose of paragraphs a8a.8.1 and a8a.8.2 above.

DEATH IN SERVICE BENEFITS

a8a.9.1 Contributions towards insurance of approvable death-in-service benefits may be paid in addition to the contributions being paid for post-retirement benefits.

BENEFIT ILLUSTRATIONS

a8a.10.1 Once the maximum contribution level has been determined it may be used in illustrations based on the normal FSA/PIA requirements. There is no additional requirement that the benefits illustrated should be restricted by Revenue limits.

REVIEW OF ASSUMPTIONS

a8a.11.1 The financial and demographic assumptions underlying the Factors in the Appendices to these notes will be reviewed from time to time by IR SPSS in consultation with the Government Actuary’s Department.

OTHER POINTS

In-House Additional Voluntary Contribution Contracts

a8a.12.1 Contracts for additional voluntary contributions written on a money purchase basis and held within final salary (defined benefit) schemes other than small self-administered schemes, are not subject to the ABI 1996 method as amended 31 March 1998 and 21 December 2001. The extent to which additional voluntary contributions can be paid, to augment the final salary scheme benefits within approvable limits, will be determined by the scheme actuary.

a8a.12.2 Additional voluntary contributions in conjunction with money purchase schemes or small self-administered schemes do come within the ABI 1996 method as amended 31 March 1998 and 21 December 2001, and form part of the maximum overall contribution. However, having established the maximum overall contribution based on funding to the normal retirement date, there is no objection to further additional voluntary contributions being paid to the extent that they can be justified for the provision of approvable benefits at an anticipated earlier retirement date.

Use of Additional Voluntary Contributions to Fund for Early Retirement

a8a.12.3 IR SPSS have agreed that, where additional voluntary contributions are paid to fund for early retirement, a suitable approach to determine the maximum additional voluntary contributions would be to substitute the early retirement date in the maximum funding calculation for the normal
retirement date, to use the appropriately adjusted Revenue limits in paragraphs a8a.6.8 - a8a.6.19 and the prospective benefits at the early retirement date in paragraphs a8a.6.20 - a8a.6.22. Other bases of calculation may, however, be acceptable but should be cleared with IRSPS in advance.

a8a.12.4 The extra contribution may be paid only to the extent that it does not exceed the employee's contribution limit of 15% of pay. On no account may the balance be paid by the employer.

a8a.12.5 All employee contributions to the scheme for other purposes should be taken into account in calculating what the employer can pay to fund for retirement at normal retirement date.

Retained Benefits

a8a.12.6 If on a member's admission to a scheme the administrator or pensions practitioner acting for the administrator is told that there are no retained benefits which PN require to be taken into account, contributions may be calculated and accepted on that basis.

a8a.12.7 But if subsequent enquiries establish that such retained benefits do exist, a further funding check should be made at the time the new information comes to light and future contributions reduced or suspended accordingly if necessary. Where the discovery of hitherto undisclosed retained benefits and a complete stop on contributions would still leave the scheme overfunded under the ABI 1996 method as amended 31 March 1998 and 21 December 2001 for more than a year, an appropriate repayment of contributions already paid will be required. In the case of a refund of employer contributions the prior agreement of IRSPS will be required. The refund of contributions paid in error procedure detailed in PN 5.17 is not applicable in these circumstances.

Transfer Payments

a8a.12.8 When a transfer payment is received by a scheme the contribution rate should be retested on the ABI 1996 method as amended 31 March 1998 and 21 December 2001 at that time except where the transfer represents

- retained benefits which may be ignored under PN 7.5 and 7.6 or
- concurrent or retained benefits which have already been taken into account in setting the scheme contribution level, or
- benefits under a personal pension / stakeholder scheme subject to the "concurrency" rules in section 632B ICTA 1988.

This applies to schemes set up under pre and post-September 1994 and post-June 1996 contracts. The funding test need not be carried out if the aggregate contributions are below the de minimis limit in paragraphs a8a.3.1 - a8a.3.8 of the Guidance Notes.

Schemes Approved Under S590 ICTA 1988

a8a.12.9 The ABI 1996 method as amended 31 March 1998 and 21 December 2001 should be applied to money purchase insured schemes approved under S590 ICTA 1988 with appropriate adjustments to reflect the following limitations:

(i) benefits may be funded for only on the basis that they do not exceed N/60ths
(ii) no allowance may be made for benefits to increase in payment except to the extent required by Section 51 Pensions Act 1995
(iii) no salary roll-up is permitted
(iv) allowance must not be made for benefits to be payable for a guaranteed period
(v) complete years of service only to count.

a8a.12.10 Point (i) can be allowed for by calculating P1 and P2 as set out in paragraphs a8a.6.14, a8a.6.15 or a8a.6.18 (as appropriate) of the ABI 1996 method as amended 31 March 1998 and 21 December 2001 and the underlying actuarial formulae should be adjusted to allow for points (ii), (iii) and (iv).

a8a.12.11 Retesting every three years (or more frequently if desired) will enable salary growth in the intervening period to be reflected in the calculation of the maximum funding level.

**Simplified Defined Contribution Schemes**

a8a.12.12 For the avoidance of doubt it is confirmed that the ABI 1996 method as amended 31 March 1998 and 21 December 2001 does not apply to Simplified Defined Contribution Schemes.

21 December, 2001
Ref
I/330/002
I/330/013
I/330/014
DEFINITIONS

a8b.1.1  $T$ means the number of complete years between the *Normal Retirement Date* of the member and the date of calculation.

a8b.1.2  NRA means the age of the member at the *Normal Retirement Date*.

a8b.1.3  aNRA means a life annuity calculated using PA(90) ultimate minus two years of age - see Notes.

FINANCIAL ASSUMPTIONS

a8b.2.1

Rate of investment return .................................. 8.5% pa
Rate of future salary growth ................................ 6.9% pa
Rate of post retirement pension increases ................. 5.3% pa
Rate of price inflation .................................... 5.3% pa

FACTORS

a8b.3.1

Factor [1]  \[ V_T (@ 1.5\% pa) \times a_{NRA} (@ 3.0\% pa) \]

Factor [2]  
- \[ 0.97443 \times a_T (@ 1.5\% pa) \]
- \[ 0.91352 \times a_T (@ 1.5\% pa) \]

Factor [3]  \[ V_T (@ 3.0\% pa) \times a_{NRA} (@ 3.0\% pa) \]

Factor [4]  
- \[ 0.98883 \times a_T (@ 3.0\% pa) \]
- \[ 0.94052 \times a_T (@ 3.0\% pa) \]

Factor [5]  \[ V_T (@ 4.0\% pa) \times a_{NRA} (@ 3.0\% pa) \]

For Factors [2] and [4] the annuities are certain.

Notes

a8b.4.1  The annuity factors in the above formulae assume payment annually in arrears. A suitable adjustment to factors [1] and [3] may be made for actual payment frequency and for pension payment to be guaranteed for 5 years.

a8b.4.2  A contingent post-retirement spouse's pension may be included in calculating aNRA if the member is married (excluding a divorced member, unless that member has remarried) at the date of calculation or if there is a nominated financial dependant. The actual age of the spouse may be used where known; otherwise it may normally be assumed that in the case of a male employee he is married to a wife three years younger than himself, and in the case of a female employee that she is married to a husband three years older than herself.

a8b.4.3  The constants of 0.97443, 0.91352, 0.98883 and 0.94052 which are used in arriving at factors [2] and [4] are adjustments to allow for the timing of contributions, which are assumed to be
paid half way through the year. Different figures should not be used for other frequencies.

21 December, 2001
Ref
L/330/002
L/330/013
L/330/014
Appendix VIII. Part C. Worked Example

DATA

a8c.1.1

- Male aged 40 next birthday - joined service age 30 next birthday
- Married
- *Normal Retirement Date*: 65th birthday
- Current *Remuneration*: £65,000
- *Permitted Maximum* for 2001/02: £95,400
- Post 1989 (Class A) regime applies
- No *special contributions*
- No *pension debit*

a8c.1.2 The current valuation of existing assets (V) is £250,000. This represents the aggregate of the value of existing money purchase scheme assets at the date of assessment and the value of the prospective pension under a concurrent defined benefit scheme. These values are £50,000 and £200,000 respectively.

a8c.1.3 Current value at the date of assessment of *retained benefits* from earlier employment is £30,000 (R).

FACTORS

a8c.2.1

\[ A_{\text{ora}} = a_{63}^m + \frac{1}{3}(a_{60}^f - a_{63:60}^m) \]

\[ = 11.520 + \frac{1}{3}(15.262 - 9.999) = 15.5287 \]

**Factor [1]**  
\[ = (1.015)^{25} x 15.5287 = 10.7025 \]

**Factor [2]**  
\[ = 0.97443 x a_{25} @ 1.5\% = 20.1898 \]

**Factor [3]**  
\[ = (1.03)^{25} x 15.5287 = 7.4166 \]

**Factor [4]**  
\[ = 0.98883 x a_{25} @ 3\% = 17.2186 \]

Calculations

a8c.3.1

R1 = 30,000 / 10.7025 = 2803.08

R2 = 30,000 / 7.4166 = 4044.98

P1 = The greater of
(a) 35/60 \times 65000 = 37916.67 and
(b) the lesser of
   (i) 20/30 \times 65000 = 43333.33
   (ii) 2/3 \times 65000 - 2803.08 = 40530.25

\[ P2 = \text{The greater of} \]
(a) 35/60 \times 95,400 = 55,650.00 and
(b) the lesser of
   (i) 20/30 \times 95,400 = 63,600.00
   (ii) 2/3 \times 95,400 - 4044.98 = 59,555.02

\[ C1 = \frac{40530.25 \times 10.7025 - 250000}{20.1898} \times 1.05 = 9557.49 \]

\[ C2 = \frac{59555.02 \times 7.4166 - 250000}{17.2186} \times 1.05 = 11689.72 \]

\[ F = \frac{100 \times 9557.49}{65000} = 14.70\% \]

**Results**
a8c.3.2

- Maximum contribution to insured money purchase schemes = £9557.49.
- Maximum annual contribution rate to insured money purchase schemes = 14.70%
WORKED EXAMPLE - MAXIMUM CONTRIBUTION FOLLOWING DIVORCE AND REMARRIAGE

Data

a8d.1.1

- Male aged 45 next birthday – joined service age 30 next birthday
- Marriage (second marriage)
- Normal Retirement Date: 65th birthday
- Current Remuneration: £80,000
- Permitted Maximum for 2001/02: £95,400
- Post 1989 (Class A) regime applies
- No special contributions
- Pension debit at date of divorce (age 40) £100,000

a8d.1.2 The current valuation of existing assets (V) is £200,000. This represents the aggregate of the value of existing money purchase scheme assets at the date of assessment and the value of the prospective pension under a concurrent defined benefit scheme. These values are £50,000 and £150,000 respectively.

a8d.1.3 Current value at the date of assessment of retained benefits from earlier employment is £40,000 (R).

Factors

a8d.2.1

\[ A_{nra} = a_{63}^m + \frac{2}{3} (a_{60}^f - a_{63:60}^{m:f}) \]

\[ = 11.520 + \frac{2}{3} (15.262 - 9.999) = 15.5287 \]

Factor [1] = \((1.015)^{-20} \times 15.5287 = 11.5296\)

Factor [2] = \(0.97443 \times a_{20} @ 1.5\% = 16.7297\)

Factor [3] = \((1.03)^{-20} \times 15.5287 = 8.5978\)

Factor [4] = \(0.98883 \times a_{20} @ 3\% = 14.7113\)

Factor [5] = \((1.04)^{-25} \times 12.020 = 4.5089\)

(at date of divorce)

Factor [5] = \((1.04)^{-20} \times 12.020 = 5.4857\)

(currently)

(These factors are all tabulated in the Appendix to PSO Update 84)
Calculations

a8d.3.1 Value of *retained benefits*

\[ R_1 = \frac{40,000}{11.5296} = 3469.33 \]
\[ R_2 = \frac{40,000}{8.5978} = 4652.35 \]

a8d.3.2 Value of *pension debit*

(i) Pension amount at date of divorce
\[ \frac{100,000}{4.5089} = £22,178.36 \text{ pa} \]

(ii) Statutory revaluation for 5 years to date of maximum contribution calculation (taken as 3.0% pa)
\[ £22,178.36 \div (1.03)^5 = £25,710.71 \]

(iii) Current value
\[ £25,710.71 \times 5.4857 = £141,041.24 \]

a8d.3.3 Maximum gross pension

\[ P_1 = \text{The greater of} \]
\[ (a) \quad \frac{35}{60} \times 80,000 = 46,666.68 \text{ and} \]
\[ (b) \quad \text{The lesser of} \]
\[ (i) \quad \frac{20}{30} \times 80,000 = 53,333.33 \]
\[ (ii) \quad \frac{2}{3} \times 80,000 - 3,469.33 = 49,864.00 \]

\[ P_2 = \text{The greater of} \]
\[ (a) \quad \frac{35}{60} \times 95,400 = 55,650.00 \text{ and} \]
\[ (b) \quad \text{The lesser of} \]
\[ (i) \quad \frac{20}{30} \times 95,400 = 63,600.00 \]
\[ (ii) \quad \frac{2}{3} \times 95,400 - 4,652.35 = 58,947.65 \]

a8d.3.4 Maximum contribution

\[ C_1 = \frac{(49,864.00 \times 11.5296 - 200,000 - 141,041.24)}{16.7297 \times 1.05} = 14,678.34 \]
\[ C_2 = \frac{(58,947.65 \times 8.5978 - 200,000 - 141,041.24)}{14.7113 \times 1.05} = 11,832.25 \]
\[ F = \frac{11,832.25}{80,000} = 14.79\% \]

Results

a8d.3.5

- Maximum contribution to insured money purchase schemes = £11,832.25
- Maximum annual contribution rate to insured money purchase schemes = 14.79%
Appendix IX. Amended SSAS Funding Guidelines

Introduction

A9.1 These notes set out the method (the SSAS 1996 Method) fixed by IR SPSS to calculate maximum contributions to SSASs from 1 June 1996 for approveable retirement benefits, as subsequently amended on 11th March 2003. The method makes allowance for the earnings cap (the "permitted maximum") where applicable and applies to money purchase and defined benefit SSASs. It is known as:


The method for calculating maximum special contributions to SSASs is described in PN A9.12.

A9.2 The 11th March 2003 amendments relate primarily to the introduction of pension sharing on divorce. There are a few other amendments which update references. Also, the transitional arrangements which applied from 1 June 1996 to 1 June 2002 have now been deleted from the notes.

De minimis limit

A9.3 No check against the maximum funding rate is required for a member where:

a) the annual aggregate contributions to all schemes, excluding contributions for death in service benefits (and contributions to personal pension schemes / stakeholder pension scheme contracts which are subject to the “concurrency” rules in section 632B ICTA 1988) for the same employment do not exceed 17.5% of remuneration (within the permitted maximum), and

b) contributions (including special contributions) have not been at a higher amount than the figure determined from this limit in any earlier year. (Contributions to free standing additional voluntary contribution schemes) must be taken into account for this purpose.

For the purpose of this limit, age-related rebates (that is, the excess over the flat-rate percentage rebate) made under the Social Security (Reduced Rates of Class 1 Contributions and Rebates) (Money Purchase Contracted-out Schemes) Order 1996 (SI 1996/1055) and minimum contributions to appropriate personal pensions may be ignored.

There is no corresponding de minimis limit for special contributions.

Current Valuation of Existing Assets (V)

A9.4 The value of assets (V) is to be taken as the market value, as shown in the scheme accounts in respect of the member concerned.

A9.5 If the maximum funding rate is being assessed on a date other than the scheme’s accounting date, then the value of the assets should be taken at market value. If this is not readily available the assets may be taken as the value at the most recent accounting date increased (or decreased, as appropriate) by the monies received by the scheme between that date and the date of assessment, all accumulated at the rate of 8.5% per annum compound.

A9.6 Assets under any other "Money Purchase" schemes relating to the same employment are to be brought into account. This includes age-related rebates made under the Social Security (Reduced Rates of Class 1 Contributions and Rebates) (Money Purchase Contracted-Out Schemes) order 1996 (SI 1996/1055). In addition, for Class A members, the value of benefits from all connected schemes and associated employments must be brought into account as explained in
PN 7.26. Assets under Free standing Additional Voluntary Contribution Schemes (but not in-house Additional Voluntary Contributions) and under personal pension schemes / stakeholder pension schemes subject to the “concurrency” rules in section 632B ITCB 1988, may be ignored. Concurrent benefits in respect of the same employment from defined benefit schemes are dealt with in 7C below.

A9.7 Any pension debit arising as a result of the member’s pension rights being shared on divorce must also be brought into account, unless the member falls within the easement described in PN 7.7, in which case the pension debit can be ignored. Appendix XIII to the PN demonstrates the methodology to be used to calculate “pension debits”

A9.8 Where PN 7.10 applies in determining maximum benefits, the value of retirement annuity contracts or personal pension scheme benefits is to be taken as the transfer value at the date of assessment (or if exceptionally a transfer value is not available, the present value of the projected benefits at retirement calculated on a basis consistent with the financial assumptions specified in paragraph 2 of the Appendix to these notes).

Special contributions

A9.9 The amount of any special contribution (S) which is to be paid at the time of calculation is also to be taken into account as indicated in 6D below. The method of calculating the maximum special contribution is described in PN A9.12.

Expenses

A9.10 Where a scheme meets its own expenses, these should be justified and clearly identified in the actuary’s report. A reserve for such expenses excluding investment-related expenses may be incorporated in the calculations equal to the capitalised value of all expected future administration costs to be borne by the scheme.

Method of Calculation

A9.11 Factors [1] to [5] are described in the Appendix to these notes.

- A - Value of Retained Benefits (R)

The figures represented R1 and R2 in section - B - below are arrived at as follows:

R1 = transfer value of the Retained Benefits at the assessment date ÷ Factor [1]

R2 = transfer value of the Retained Benefits at the assessment date ÷ Factor [3].

Retained Benefits should include any pension debit applied against those benefits (unless the administrative easement in PN 7.7 applied at the date of divorce).

Retained benefits may be ignored (i.e. R1 and R2 taken as zero) in the circumstances described in PN 7.5 and 7.6. If the Retained Benefits are already in payment, then it should be taken at its current value (and including the amount of any lump sums already paid - PN 16.38).

Value of the pension debit (if any) (D)

This is calculated as follows:

- Calculate the notional deferred pension equivalent of the pension debit at the time of divorce. This is the actual pension debit divided by the appropriate value of Factor [5] for the age at the date of divorce.

- Increase the notional deferred pension at the time of divorce by the actual rate of statutory revaluation which has applied between that date and the date of the maximum contribution rate calculation.
Multiply the notional deferred pension, revalued as above, by Factor [5] for the age at the date of the maximum contribution rate calculation.

- B - Calculation of the Maximum Permissible Pension at the Normal Retirement Date

The calculation varies depending on which basis of Revenue limits applies i.e. Post 1989 (Class A), pre 1 June 1989 (Class B), or pre 17 March 1987 (Class C) members. For Class A members it is necessary to calculate separately the maximum permissible pension on the basis of current remuneration (P1) and the current permitted maximum (P2).

"Either 'final remuneration' (as defined in PN Appendix 1) or 'current remuneration' can be used for the calculations. There is no requirement to use just one approach for all members of a particular SSAS.

'Final remuneration' should be used in every case for the three year period immediately prior to NRA.

Where contributions are to be fixed as level amounts for the period (to be no longer than three years) until the next valuation, that can be reflected in the calculation of Factor [2] and Factor [4] (which are defined in the Appendix to this Note). Otherwise, those contributions factors should allow for remuneration to increase every year in line with the assumptions specified in that Appendix." It must be noted that contributions may be fixed as level amounts only if “final remuneration” is used in the calculation. If current remuneration is used, the maximum contributions must be expressed as a percentage of current remuneration.

The maximum total benefits at normal retirement date derived from this calculation applies to the aggregate benefits from all schemes relating to the current employment and for Class A members Associated Employments / connected schemes.

I. Class A Members

P1 = The greater of

(a) NS (maximum 40)/60 x remuneration and

(b) the lesser of

(i) NS (maximum 20)/30 x remuneration and

(ii) 2/3 x remuneration - R1

P2 = The greater of

(a) NS (maximum 40)/60 x remuneration and

(b) the lesser of

(i) NS (maximum 20)/30 x permitted maximum and

(ii) 2/3 x permitted maximum - R2

II. Class B Members

The calculation of P1 is the same as for Class A members.

The calculation of P2 is not required.

III. Class C Members

P1 = the greater of
(a) NS (maximum 40)/60 x remuneration and

(b) the lesser of

   (i) The uplifted scale (PN 7.40) x remuneration and

   (ii) 2/3 x remuneration - R1

The calculation of P2 is not required.

- C - Allowance for Concurrent Benefits under a Defined Benefit Scheme

If the employee is a concurrent member of a defined benefit scheme in respect of the same employment scheme then V must be increased either by

- the value of the prospective pension under that scheme (inclusive of any pension debit applied against that prospective pension under that scheme, unless the PN 7.7 easement applied at the date of divorce) at the normal retirement date based on current pensionable earnings in that scheme or,

- by the value of the prospective pension under that scheme (inclusive of any pension debit applied against that prospective pension under that scheme, unless the PN 7.7 easement applied at the date of divorce) at the normal retirement date based on the current permitted maximum.

The value must be assessed on a basis consistent with that used for calculating the maximum contribution C below.

The pension equivalent of lump sum retirement benefits may be calculated using the 12:1 factor, regardless of the tax approval regime which applies and the escalation rate of the pension given up.

- D - Calculation of the Maximum Regular Contribution (C)

For Class A members, the maximum regular contribution (C) is the lesser of the amounts calculated on the basis of remuneration (C1) and the current permitted maximum (C2).

For Class B and C members, C1 always applies and C2 is not calculated.

\[
C_1 = \left( \frac{P1 \times \text{Factor}[1] - V - S - D}{\text{Factor}[2]} \right) \times 1.05
\]

\[
C_2 = \left( \frac{P2 \times \text{Factor}[3] - V - S - D}{\text{Factor}[4]} \right) \times 1.05
\]

The value V used in these calculations must be adjusted to allow for concurrent defined benefit scheme membership (see 8C).

The amount calculated above in C is the maximum annual figure to all schemes relating to the current employment.

It should be noted that the value of S cannot be negative.

**Method of Calculation of Maximum Special Contributions**

A9.12 Special contributions should not be made to fund benefits in advance of the maximum justifiable by reference to service to date.

For a post 1989 (Class A) member the maximum is the lesser of \( S_1 \) and \( S_2 \) where
For Class B and C members $S_1$ always applies.

If the employee is a concurrent member of a defined benefit scheme in respect of the same employment then $V$ must be increased by one of the following:

- Where the maximum permissible pension at normal retirement date in accordance with PN A9.11 is $P_1$, by the value of the prospective pension under the defined benefit scheme (inclusive of any pension debit against that prospective pension under the defined benefit scheme, unless PN 7.7 easement applied at the date of divorce) at normal retirement date based on current pensionable earnings under that scheme, or

- Where the maximum permissible pension at normal retirement date in accordance with PN A9.11 is $P_2$, by the value of the prospective pension under the defined benefit scheme (inclusive of any pension debit against that prospective pension under the defined benefit scheme, unless PN 7.7 easement applied at the date of divorce) at normal retirement date based on current Permitted Maximum.

It should be noted that, for the purposes of the paragraphs under PN A9.12, any part of $V$ which relates to concurrent benefits under a defined benefit scheme can be reduced in proportion to $N/NS$.

**Reassessment of Maximum Contribution Level**

**A9.13**

**A. 3 Year Reassessment**

The contribution limit must be reassessed within 3 years of the date that the maximum contribution $C$ has been established unless it has been previously amended in accordance with 9B below (in which case the 3 year period runs from the date of the most recent change in 9B). Reassessment is not required when a member gets divorced but at the next reassessment date, any pension debit applied against that member’s benefits must be brought into account, unless the member falls within the administrative easement described in PN 7.7, in which case the pension debit can be ignored.

The revised value of $C$ must apply from the effective date of the assessment. A new 3 year period will then commence.

**B. Special Contributions**

A reassessment of the maximum contributions must be made whenever a special contribution outside that shown in an actuarial report is paid. The revised value of $C$ must apply immediately (increase or decrease) and, if necessary, future regular contributions reduced. A new 3 year period will commence for the purpose of 9A above.

**Death in Service Benefits**

A9.14 Contributions towards insurance of approvable death-in-service benefits may be paid in addition to the contributions being paid for post retirement benefits.
Review of Assumptions

A9.15 The financial and demographic assumptions underlying the Factors in the Appendices to these notes will be reviewed from time to time by IR SPSS in consultation with the Government Actuary’s Department and the Association of Pensioneer Trustees.

Additional Voluntary Contributions

A9.16 Additional Voluntary Contributions in conjunction with SSASs form part of the maximum overall contribution. However, having established the maximum overall contribution based on funding to the normal retirement date, there is no objection to further Additional Voluntary Contributions being paid to the extent that they can be justified for the provision of approvable benefits at an anticipated earlier retirement date. A suitable approach to determine the maximum Additional Voluntary Contributions would be to substitute the early retirement date in the maximum funding calculation for the normal retirement date with appropriately adjusted Revenue limits. Other bases of calculation may, however, be acceptable but should be cleared with IR SPSS in advance.

Retained benefits

A9.17 If on a member’s admission to a scheme the administrator is told that there is no retained benefits which PN require to be taken into account, contributions may be calculated and accepted on this basis.

If subsequent enquires establish that such retained benefits do exist, a further funding check should be made at the time the new information comes to light and future contributions reduced or suspended accordingly if necessary. In the case of a refund of employer contributions the prior agreement of IR SPSS will be required.

Transfer Payments

A9.18 When a transfer payment is received by a scheme the contribution rate should be retested at that time except where the transfer represents

- Retained benefits which may be ignored under PN 7.5 and 7.6 or
- Concurrent or retained benefits which have already been taken into account in setting the scheme contribution level, or
- Benefits under a personal pension scheme / stakeholder pension scheme subject to the “concurrency” rules in section 632B ICTA 1988.

The funding test need not be carried out if the aggregate contributions are below the de minimis limit in PN A9.3 above.

Schemes Approved Under S590 ICTA 1988

A9.19 The guidelines set out in this note should be applied to money purchase SSASs approved under S590 ICTA 1988 with appropriate adjustments to reflect the following limitations:

(i) benefits may be funded for only on the basis that they do not exceed N/60ths
(ii) no allowance may be made for benefits to increase in payment except to the extent required by Section 51 Pensions Act 1995
(iii) no salary roll-up is permitted
(iv) allowance must not be made for benefits to be payable for a guaranteed period
(v) complete years of service only to count.
Point (i) can be allowed for by calculating P1 and P2 appropriately and the underlying actuarial formulae should be adjusted to allow for points (ii), (iii) and (iv).

Retesting every three years (or more frequently if desired) will enable salary growth in the intervening period to be reflected in the calculation of the maximum funding level.
Definitions Assumptions and Factors

A9.1.1
Maximum Permissible Funding Rates for Small Self-Administered Schemes (SSASs) (SSAS 1996 Method)

Annex

1. Definitions

T means the period between the normal retirement date of the member and the date of calculation.

NRA means the age of the member at the normal retirement date.

2. Financial Assumptions

Rate of investment return 8.5% pa
Rate of future salary growth 6.9% pa
Rate of post retirement pension increases 5.3% pa
Rate of price inflation 5.3% pa
Rate of statutory revaluation to deferred pension credit on divorce 4.3% pa

3. Factors

FACTOR [1] is the present value at the date of calculation of a pension of £1 pa payable at NRA allowing for future salary increases up to NRA.

FACTOR [2] is the present value at the date of calculation of a future contribution of £1 pa until NRA increasing in line with earnings. The frequency of the increases is to be in accordance with paragraph 7B.

FACTOR [3] is the present value at the date of calculation of a pension of £1 pa payable at NRA allowing for future price inflation to NRA.

FACTOR [4] is the present value at the date of calculation of a future contribution of £1 pa until NRA increasing in line with prices. The frequency of the increases is to be in accordance with paragraph 7B.

FACTOR [5] is the present value at the date of calculation of a pension of £1 pa payable at NRA allowing for future increases up to NRA in line with statutory revaluation.

The annuity factors may be calculated as a life annuity guaranteed five years and payable in accordance with the likely payment frequency using mortality PA(90) ultimate minus two years of age. A contingent post-retirement spouse's pension may be included if the member is married at the date of calculation, or if there is a nominated financial dependant. The actual age of the spouse may be used where known: otherwise it may normally be assumed that in the case of a male employee he is married to a wife 3 years younger than himself, and in the case of a female employee, that she is married to a husband 3 years older than herself.
### Index of Inland Revenue Statutory Instruments Applying to Occupational Pension Schemes

**A.10.1**

(Copies can be obtained from HM Stationery Office)

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<td>Section 591(6)</td>
<td>Retirement Benefits Schemes (Restriction on Discretion to Approve) (Small Self-administered Schemes) (Amendment) Regulations</td>
<td>2000</td>
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<td>Pension Scheme Surpluses (Valuation) Regulations</td>
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<td>Schedule 22 ICTA 1988</td>
<td>Pension Scheme Surpluses (Valuation) (Amendment) Regulations</td>
<td>1989</td>
<td>1989 No 2290</td>
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<td>Retirement Benefits Schemes (Indexation of Earnings Cap) Order</td>
<td>1990</td>
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<td>1991</td>
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<td>1992</td>
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<td>Retirement Benefits Schemes (Indexation of Earnings Cap) (No 2) Order</td>
<td>1993</td>
<td>1993 No 2950</td>
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<td>Retirement Benefits Schemes (Indexation of Earnings Cap) Order</td>
<td>1994</td>
<td>1994 No 3009</td>
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TRANSFERS FROM APPROVED RETIREMENT BENEFIT SCHEMES, RELEVANT STATUTORY SCHEMES AND BUY OUT POLICIES TO PERSONAL PENSION SCHEMES

This Appendix gives details of how to:

1) calculate the maximum amount that may be transferred from an approved retirement benefit scheme, a relevant statutory scheme or a buy-out policy to a personal pension scheme under regulation 8(3) of The Personal Pension Schemes (Transfer Payments) Regulations 2001

and

2) calculate the prescribed amount referred to in regulation 7(4) of The Personal Pension Schemes (Restriction on Discretion to Approve and Conversion of Retirement Benefits Schemes) Regulations 2001.

Terms which appear in bold type have specific meanings in relation to this Appendix, which are explained in the text or defined in the attached Annex. The terms as defined are for use with this Appendix only.

NB Where the individual is entitled to a statutory minimum level of transfer value calculated in accordance with the Minimum Funding Requirement (MFR) under the Pensions Act 1995, this amount may be transferred, even if greater than the amount permitted under Step 4.

STEP 1

Calculate The Total Current Value of The Existing Assets (VT)

The value of the assets is to be taken as the market value of the funds held for the purpose of providing benefits, for service with the current employer, for the member and any dependants under:

- the transferring scheme, excluding any funds which are being transferred to a scheme or policy which is not a personal pension scheme (V1)
- where benefits have not yet come into payment, any other approved schemes (or any schemes seeking approval) relating to the current employer (including Free standing AVC schemes) of which the individual is, or has been, a member, regardless of whether a transfer is being made from these schemes, plus any funds in the transferring scheme which are being transferred to a scheme or policy which is not a personal pension scheme (V2)
- where benefits have not yet come into payment, any retirement annuity contract, personal pension arrangement or buy-out policy which must be treated as providing benefits in respect of service with the current employer (V3) - see Note 1.

For a defined contributions scheme, market value is to be taken as the actual market value of the assets as at the transfer valuation date. For a defined benefits scheme, market value is to be taken as the notional transfer value of the accrued benefits as at the transfer valuation date, assessed using the assumptions set out in Step 3. The transfer valuation date may be any date within 2 months of the proposed transfer date.

The market value of retirement annuities and personal pensions is to be taken as the transfer value at the transfer valuation date.
VT is the sum of $V1 + V2 + V3$.

The transfer should be made within 2 months of the transfer valuation date. If the transfer is not made within this period, a fresh valuation must be made.

**NB** The asset valuation above should exclude any funds held under the schemes at $V1$ or $V2$ which are treated as **retained benefits** under those schemes.

**STEP 2**

**Calculate the maximum permissible accrued benefit**

The calculation varies depending on which basis of Revenue limits applies to the member under the transferring scheme i.e. post 1989 (Class A), pre 1 June 1989 (Class B) or pre 17 March 1987 (Class C).

For all 3 Classes of member -

N means the number of actual years of service (maximum 40 years) with the **current employer** up to the earlier of the date of leaving **pensionable service** or the proposed transfer date. Fractions of a year may be included in N. (In the case of a buy-out policy, see the definition of **current employer**).

NS means the number of years of potential service to **normal retirement date** (maximum 40 years) with the **current employer**. Fractions of a year may be included in NS. (In the case of a buy-out policy, see the definitions of **current employer** and **normal retirement date**).

**CLASS A MEMBERS**

The benefit limit for a Class A member is the lesser of the primary limit and the secondary limit. The secondary limit is relevant only where the member has benefits or rights to benefits for service in **associated employments** or under **connected schemes**. The primary limit is calculated as follows:

Leaving **pensionable service** condition.

Where, at the date of the transfer, the member has not reached the retirement age specified in the scheme rules (or, in the case of a buy-out policy, the retirement age specified in the rules of the scheme which was the direct or indirect source of the capital fund used to purchase the policy) and the member is still in service with the **current employer**, make the calculation immediately below.

$$P = \text{the greater of}$$

a) $\frac{N}{60} \times \text{final remuneration}$ and  
b) the lesser of

i) $\frac{N}{30}$ (maximum 20/30) $\times \text{final remuneration}$ and  
ii) $\frac{2}{3} \times \text{final remuneration} - \text{retained benefits}$ (see Note 2).

Multiply P by $\frac{N}{NS}$. The result of $\frac{N}{NS} \times P$ should be increased by 5% pa compound for the period between leaving **pensionable service** and the transfer valuation date (where the member's benefits include GMPs, these should be revalued in accordance with the appropriate method specified in scheme rules rather than 5% pa).
Alternative condition:

Where the member does not satisfy the “leaving pensionable service condition”, make the calculation immediately below.

\[ P = \text{the greater of} \]

a) \( \frac{N}{60} \times \text{final remuneration} \) and

b) the lesser of

i) \( \frac{N}{30} \times \text{final remuneration} \) and

ii) \( \frac{2}{3} \times \text{final remuneration} \) – retained benefits (see Note 2).

\( P \) should be increased by 5% pa compound for the period between leaving pensionable service and the transfer valuation date (where the member’s benefits include GMPs, these should be revalued in accordance with the appropriate method specified in scheme rules rather than 5% pa).

The secondary limit is calculated as follows:

\[ \frac{1}{30} \times \text{permitted maximum} \times \text{years of service (maximum 20)} \]

less

\[ \text{(the associated employer fund benefit plus the associated employer pension benefit).} \]

For this purpose, service is the aggregate of all service with the current employer and associated employers in connected schemes and associated employments, with no period of concurrent service to count more than once.

Benefit limit adjustment (to take account of benefits already in payment and pension debits):

The amount of the benefit limit must be reduced by the amount of any pension or annuity in payment at the transfer valuation date, where that pension/annuity relates to service with the current employer.

If such a pension is in payment under income drawdown, the amount of the pension should be taken as the maximum amount capable of being paid under income drawdown, at that time.

Where a lump sum retirement benefit which relates to service with the current employer (see Note 1) has already been paid, its pension value (determined by dividing the amount of the lump sum by 12) should also be deducted from the benefit limit.

Where the member’s rights to benefits relating to service with the current employer and/or the member’s benefits relating to service with the current employer have been reduced by a pension sharing order, agreement or equivalent provision and the member was not a moderate earner (as defined in S1 2000 No 1085) at the date of the divorce/annulment, then the negative deferred pension must also be deducted from the benefit limit.

CLASS B MEMBERS

\[ P = \text{the greater of} \]
a) NS/60 x final remuneration and

b) the lesser of

i) NS/30 (maximum 20/30) x final remuneration and

ii) 2/3 x final remuneration – retained benefits (see Note 2).

Multiply P by N/NS. The result of N/NS x P should be increased by 5% pa compound for the period between leaving pensionable service and the transfer valuation date (where the member's benefits include GMPs, these should be revalued in accordance with the appropriate method specified in scheme rules rather than 5% pa).

The benefit limit adjustment is the same as for Class A members except that the pension value of any lump sum retirement benefit should be determined using the appropriate divisor specified in the rules of the transferring scheme or a divisor approved by the Inland Revenue for use by the transferring scheme. The divisor used should be appropriate to the member's age at the transfer valuation date.

CLASS C MEMBERS

P = the greater of

a) NS/60 x final remuneration and

b) the lesser of

i) the uplifted scale (see Note 3) x final remuneration and

ii) 2/3 x final remuneration – retained benefits (see Note 2).

Multiply P by N/NS. The result of N/NS x P should be increased by 5% pa compound for the period between leaving pensionable service and the transfer valuation date (where the member's benefits include GMPs, these should be revalued in accordance with the appropriate method specified in scheme rules rather than 5% pa).

The benefit limit adjustment is the same as for Class A members except that the pension value of any lump sum retirement benefit should be determined using the appropriate divisor specified in the rules of the transferring scheme or a divisor approved by the Inland Revenue for use by the transferring scheme. The divisor used should be appropriate to the member's age at the transfer valuation date.

STEP 3

Calculate the maximum transferable fund

The maximum transferable fund (MTF) is the present value of the benefit limit assessed in Step 2 above from normal retirement age using the following assumptions.

<table>
<thead>
<tr>
<th>Assumption</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rate of investment return</td>
<td>8.5%</td>
</tr>
<tr>
<td>Rate of post retirement pension increases</td>
<td>5.3%</td>
</tr>
<tr>
<td>Rate of pre retirement indexation</td>
<td>5.0%</td>
</tr>
</tbody>
</table>

The annuity factors may be calculated as a life annuity guaranteed for five years and using PA(90) minus two years of age. A contingent post-retirement spouse's or dependant's pension of 2/3rds of
the member’s pension may be included if, and only if, the member is either married or has an adult financial dependant at the date of the calculation. The actual age of the spouse or dependant may be used where known: otherwise male members should be assumed to be 3 years older and female members 3 years younger than their spouse or dependant, and where members and dependants are the same sex, it should be assumed that they are the same age.

In order to assess a notional transfer value in respect of accrued benefits under a defined benefit scheme, post-retirement pension increases should be valued in line with the increases actually guaranteed. For LPI increases with a ceiling of 5% pa, pension increases should be taken at 4.3% pa, which should also be assumed for revaluation in deferment of non-GMPs. For GMPs, it should be assumed that revaluation in deferment will be at the fixed rate as at the date of leaving.

The various assumptions are subject to periodic review.

**STEP 4**

**Compare the results of Steps 1 and 3**

1) If \( MTF \) is equal to or higher than \( VT \), then \( V1 \) may be transferred. **Retained benefits** held under the transferring scheme may also be transferred.

2) If \( MTF \) is lower than \( VT \), then \( MTF - (V2 + V3) \) may be transferred subject to cash equivalent requirements (see below). **Retained benefits** held under the transferring scheme may also be transferred. The transfer may not take place unless the relevant asset value is reduced to the permitted amount.

Where

- \( MTF - (V2 + V3) \), plus
- any retained benefits held under the transferring scheme, plus
- the value of any rights to benefit in the transferring scheme which are being transferred to a scheme or policy which is not a personal pension scheme

is less than the member’s cash equivalent calculated in accordance with DSS legislation, no transfer may take place.

**Note 1.**

Benefits are treated as being provided by the current employer, and therefore aggregable,

- firstly, in the case of a controlling director not entitled to continued rights (a Class A member), where the benefits from retirement annuity contracts or personal pension arrangements arise from premiums or contributions paid out of relevant earnings from the current employer, and
- secondly, where the emerging benefits from a personal pension arrangement or buy-out policy arise as the result of a transfer from a retirement benefit scheme of the current employer, but only to the extent that they relate to service with the current employer.

**Note 2.**

Valuation of retained benefits.

For certain members joining the first scheme of an employer after August 1991 **retained benefits**
can be ignored in the calculation of benefit limits. For certain members joining the first scheme of an employer before August 1991, retained benefits can be ignored in the calculation of benefit limits if the scheme accrual rate for pension benefits (excluding any benefits from additional voluntary contributions) does not exceed 1/60th of final remuneration for each year of service. For all such members the value of retained benefits should be taken as zero.

For all other members, retained benefits must be valued as follows:

- where the benefits are not yet in payment:
  - the funds held for the purpose of providing benefits for the member and any dependants should be valued on the same basis as in Step 1. A deferred annuity rate should then be applied to the fund i.e. the annuity rate appropriate to the member's normal retirement age should be adjusted by allowing for increases of 5% pa and discounting at 8.5% pa for the period between the transfer valuation date and the normal retirement date.

- where the benefits are already in payment:
  - the value is the amount of the pension or annuity currently in payment. If the pension is in payment under income drawdown, the amount of the pension should be taken as the maximum amount capable of being paid under income drawdown, at that time. Where a lump sum retirement benefit has already been paid, its value is the pension value determined by dividing the amount of the lump sum by 12 for Class A members, or the divisor specified in the rules of the transferring scheme or a divisor approved by the Inland Revenue for use by the transferring scheme for members of Classes B and C. For members of Classes B and C the divisor used should be appropriate to the member’s age at the transfer valuation date.

- where the member’s rights to receive retained benefits and/or the member’s retained benefits have been reduced by a pension sharing order, agreement or equivalent provision and the member was not a moderate earner (as defined in S1 2000 No 1085) at the date of the divorce/annulment, then the negative deferred pension must also be included in the value of retained benefits.

Note 3.

The uplifted scale means:

<table>
<thead>
<tr>
<th>Years of service to normal retirement date</th>
<th>Maximum pension fraction of final remuneration</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 – 5</td>
<td>1/60 for each year</td>
</tr>
<tr>
<td>6</td>
<td>8/60</td>
</tr>
<tr>
<td>7</td>
<td>16/60</td>
</tr>
<tr>
<td>8</td>
<td>24/60</td>
</tr>
<tr>
<td>9</td>
<td>32/60</td>
</tr>
<tr>
<td>10 or more</td>
<td>40/60</td>
</tr>
</tbody>
</table>

Fractions of a year may be interpolated into this scale.
ANNEX TO APPENDIX XI

These definitions are for use with this Appendix only.

(Legislative references to a numbered section are references to Income and Corporation Taxes Act 1988, unless otherwise indicated)

Associated employer fund benefit is the benefit income of:

A. Any funds held for the purpose of providing benefits for the member and any dependants under the transferring scheme for service in associated employments, plus

B. Where benefits have not yet come into payment, the total of any funds held for the purpose of providing benefits for the member and any dependants under a connected scheme, inclusive for this purpose of any such funds transferred out of a connected scheme to a policy or scheme, other than the transferring scheme.

The market value of the funds at A and B should be determined in the same way as the funds at Step 1.

The benefit income of the funds at A and B is calculated using a deferred annuity rate i.e. the annuity rate appropriate to the member’s normal retirement age should be adjusted by allowing for increases of 5% pa and discounting at 8.5% pa for the period between the transfer valuation date and the member’s normal retirement date.

Associated employer pension benefit is the total of all pensions/annuities currently in payment (including the pension value of any lump sum benefit already paid) from connected schemes and from any scheme or buy-out policy which has received a transfer from a connected scheme.

If the benefit is in payment under income drawdown, the amount should be taken as the maximum amount capable of being paid under income drawdown, at that time. Where a lump sum benefit has already been paid, its value is the pension value determined by dividing the amount of the lump sum by 12.

Associated employers are defined in section 590A(3) and (4) as companies where one is directly or indirectly controlled by the other or both or all are controlled by a third person. Control is construed in accordance with section 416 in relation to close companies or with section 840 for other corporate bodies.

Associated employments means in relation to a member in the transferring scheme any employment held concurrently with the member’s employment with the employer where benefits in respect of each employment are payable under the scheme in respect of a period while the employments were or are concurrent and, during that period, the employers in question were or are associated.

Connected scheme is defined in section 590A in relation to an employee. Schemes are connected if they are approved or seeking approval under Chapter I Part XIV and:

(a) there is a period during which the member has been the employee of 2 associated employers, and

(b) the period counts under both schemes as a period in respect of which benefits are payable, and

(c) the period counts under one scheme for service with one employer and under the other for service with the other employer.

Controlling director means a member who is, or has been at any time during the period of 10
years prior to the date of the proposed transfer, a director (as defined in section 612) and within paragraph (b) of section 417(5) in relation to the current employer.

**Current employer** means the employer with which the member is or was most recently in service (the present employer) under the rules of the transferring scheme. In the case of a buy-out policy, the current employer is deemed to be the current employer in the scheme which was the direct or indirect source of the capital fund used to purchase the policy.

Current employer also means any employer where service with that employer is aggregable with service for the present employer for the purpose of benefit provision (as distinct from any limitation on benefit) under the transferring scheme.

Where the member has held 2 or more concurrent employments and both/all of the employers have participated in the transferring scheme, **final remuneration**, service and benefits cannot be aggregated. Benefits for such concurrent employments must be calculated independently. Where independent calculations are required, Steps 1 to 4 must be performed with each separate employment treated as an independent “current employer”. For independent calculations, Step 2 must take into account retained benefits in respect of the other concurrent employments (as well as any other retained benefits). The member’s permissible transfer fund will be the sum of the results of the independent calculations.

**Final remuneration** from the current employer means an amount not greater than either:

(a) the highest remuneration upon which tax liability has been determined for any one of the 5 years preceding the date of leaving pensionable service being the aggregate of:

(i) the basic pay for the year in question, and

(ii) the yearly average over 3 or more consecutive years* ending with the expiry of the corresponding basic pay year, of any fluctuating emoluments provided that fluctuating emoluments of a year other than the basic pay year may be increased in proportion to the increase in the Retail Prices Index from the last day of that year up to the last day of the basic pay year, or

(b) the yearly average of the total emoluments from the employer which are assessable to income tax under Case I or II of Schedule E and upon which tax liability has been determined for any 3 or more consecutive years ending not earlier than 10 years before the date of leaving pensionable service.

Provided that-

(i) remuneration and total emoluments do not include any amounts which arise from the acquisition or disposal of shares or any interest in shares or from a right to acquire shares (except where the shares or rights etc which give rise to such an amount liable to tax under Schedule E had been acquired before 17 March 1987) or anything in respect of which tax is chargeable by virtue of section 148

(ii) in relation to a controlling director, final remuneration shall be the amount ascertained in accordance with (b), and (a) above shall not apply

(iii) in relation to any other employee whose remuneration in any year subsequent to 5 April 1987 used for the purpose of calculating benefits has exceeded £100,000 (or such other figure as may be prescribed by the Treasury), final remuneration shall not exceed the amount ascertained in accordance with (b) above, and (a) above shall not apply, unless the individual chooses to adopt £100,000 (or such other figure as may be prescribed by the Treasury)
(iv) where final remuneration is computed by reference to any year other than the last complete year ending on the date of application for the transfer, the member's remuneration or total emoluments of any year may be increased in proportion to any increase in the Retail Prices Index from the last day of that year up to the date of the transfer application.

(v) final remuneration shall not exceed the permitted maximum except in relation to Class B or C members.

(vi) the total amount of any profit related pay (whether relieved from income tax or not) may be classed as pensionable remuneration and treated as a fluctuating emolument.

(vii) an early retirement pension in payment from the employer may not be included in final remuneration.

* Where fluctuating emoluments have not been paid for the full 3 years, they should be averaged over the period from the commencement of their entitlement to payment (or the beginning of the 3 year period, if later) to the end of the relevant basic pay year. Where, however, it is proposed to include in final remuneration a fluctuating emolument which was payable in a single year only the agreement of the Pension Schemes Office must be sought.

Fluctuating emoluments are any part of an employee's earnings which are not paid on a fixed basis and are additional to the basic wage or salary. They include overtime, commission, bonuses and benefits in kind as long as they are assessable to tax under Case I or II of Schedule E.

Negative deferred pension is the current value in terms of pension of the pension debit as revalued under section 31 Welfare Reform and Pensions Act 1999 (WRP). For this purpose, where statutory revaluation under WRP ceases, the value of the pension debit must be increased by 4.3% pa for the period up to the transfer valuation date.

Normal retirement age means the age specified in the scheme rules as the age at which a member should normally retire or the member's actual age if already past the specified age. In the case of a buy-out policy, it is deemed to be the retirement age specified in the rules of the scheme which was the direct or indirect source of the capital fund used to purchase the policy, or the member's actual age if already past the specified age.

Normal retirement date means the date of attainment by the member of the age specified in the scheme rules as the age at which a member should normally retire or the transfer valuation date if already past the specified date. In the case of a buy-out policy, it is deemed to be the date of attainment by the member of the retirement age specified in the rules of the scheme which was the direct or indirect source of the capital fund used to purchase the policy, or the transfer valuation date if already past the specified date.

Pensionable service shall have the meaning in section 70(2) Pension Schemes Act 1993. In the case of a buy-out policy, pensionable service means the period of pensionable service under the scheme which was the direct or indirect source of the capital fund used to purchase the policy.

Permitted maximum is defined in section 590C(2).

Relevant earnings are defined in section 644.

Remuneration from the current employer means (unless qualified in the definition of final remuneration) any emoluments which are chargeable to tax under Case I or II of Schedule E other than those items which are specifically excluded by section 612(1) (e.g. share option gains or golden handshakes).
Retained benefits are generally a member’s benefits and rights to benefits from pension schemes or contractual pension arrangements (which have benefited from tax privileges) built up in previous employments other than the employment(s) with the current employer, or in periods of self-employment. They include benefits from:

- retirement benefit schemes approved or seeking approval under Chapter I Part IV
- relevant statutory schemes
- schemes to which section 608 applies
- retirement benefit schemes which have been accepted as corresponding for the purposes of section 596(2)(b)
- retirement annuity contracts or trust schemes approved under section 620. Additionally, benefits must be included where they arise from contributions paid out of relevant earnings from the current employer and the member is a Class B or C member or is a Class A member who is not a controlling director.
- personal pension schemes approved under section 631, excluding any fund or benefit arising from contributions paid under section 632B or section 638(8). Additionally, benefits must be included (apart from benefits arising from contributions paid under section 632B) where they arise from contributions paid out of relevant earnings from the current employer and the member is a Class B or C member or is a Class A member who is not a controlling director.

Benefits from these sources which have been transferred to another scheme or bought out continue to be retained benefits.

For the avoidance of doubt, this includes a lump sum benefit already paid and benefits being paid in the form of a pension/annuity purchased with funds which came directly or indirectly from any of the above sources.

Benefits for service in employments or for periods of self-employment which started after the start of service with the current employer should be ignored.

Benefits for service in employments or for periods of self-employment which started at the same time as service with the current employer should be ignored.

Benefits for service in employments or for periods of self-employment which started before and continued after the start of service with the current employer are retained benefits only in part. The retained benefit consists of that proportion of the total benefit which accrued in the period prior to the start of service with the current employer. However, benefits for Class A members arising from service with associated employers in respect of associated employments and connected schemes are not retained benefits.

Benefits for service in employments or for periods of self-employment which started and finished before service with the current employer started are retained benefits in their entirety.
Appendix XII. Annuity purchase deferral and drawdown

INTRODUCTION TO APPENDIX XII DATE CODED 08/2001

Content of This Appendix

A12.001 Parts I, II and III of this Appendix set out full details of the benefit options permitted in schemes and buy-out contracts which adopt the flexibility provisions for annuity purchase deferral and drawdown. Part IV contains a worked example showing the calculation of a lump sum benefit where drawdown is operated.

A12.002 The flexibility provisions can be adopted only by schemes providing benefits on a money purchase basis or buy-out contracts. Where the money purchase benefits are contracted-out the flexibility provisions cannot be applied. If a scheme provides separate money purchase and defined benefit elements the flexibility provisions cannot be applied where one element underpins the other.

A12.003 The provisions are not compulsory. Scheme trustees and Life Offices are free to decide whether to adopt them.

A12.004 Parts I, II and III are written in a style that is consistent with the format of scheme documentation (or at least with the format of model documents agreed with IR SPSS).

A12.005 Part I deals with the flexible payment of employer funded benefits.

A12.006 The flexibility provisions for additional voluntary benefits are in Parts II and III. Part II permits additional voluntary contribution benefits to be taken from age 50 before benefits funded by the employer come into payment. Part III deals with additional voluntary contribution benefits taken simultaneously with or subsequent to the payment of employer funded benefits. Additional voluntary contribution benefits may be taken before the member’s 50th birthday if the employer funded benefits come into payment due to Incapacity or due to the member’s attainment of a low normal retirement age.

A12.007 Parts I to IV contain certain defined terms which appear either in bold type or in capitals and are listed in Part V.

A12.008 Parts I, II and III contain the full range of the flexibility provisions. Trustees may choose to implement one or more of the permitted options, e.g. they may choose to permit only the option of annuity deferral for benefits from additional voluntary contribution funds. Trustees must issue announcements to members stating which options have been chosen.

How to Adopt The Flexibility Provisions

A12.009 If they wish scheme trustees can adopt the provisions by executing the following model rule amendment:

“Notwithstanding anything to the contrary in the scheme documentation the options in Parts I, II and III of Appendix XII dated 08/2001 of IR 12 (2001) may be applied to the benefits of scheme members with the consent of the Trustees.”

A12.010 Trustees must issue announcements that specify the options which will be available to scheme members.

A12.011 It is the responsibility of scheme trustees to ensure that the execution of the model rule amendment is compatible with the scheme’s existing powers of amendment.

A12.012 Where schemes with standard documentation execute this model rule amendment IR SPSS should be notified using the documentation certificate (PS 5, PS 6 or PS 176 as
A12.013 Where schemes with non-standard documentation adopt the model rule amendment trustees should notify IR SPSS in writing.

A12.014 Scheme trustees are free to draft their own rule amendments to implement these provisions. The draft rule amendments should be submitted to IR SPSS for approval before execution.

A12.015 Buy-out contracts can be endorsed where it is desired to take advantage of the flexibility provisions by using the following endorsement:

"Notwithstanding anything to the contrary in the buy-out contract the options in Parts I, II and III of the Appendix XII dated 08/2001 of IR 12 (2001) may be applied to the benefits arising under the contract with the consent of the Life Office."

A12.016 It is the responsibility of Life Offices to ensure that they have the necessary powers to endorse a buy-out contract in this way. IR SPSS does not need to be informed when a buy-out contract is endorsed to give effect to the provisions in Appendix XII and we do not wish to see copies of the endorsement.

Limitations on Usage

A12.017 The following schemes should not use the model rule amendment procedure:

- Large self-administered schemes which do not contain a requirement to secure benefits for members by the purchase of an annuity
- Simplified Defined Contribution Schemes (Parts I and III refer to benefit limits which do not apply to such schemes).

These schemes must use non-standard rule amendments to adopt the flexibility provisions.

A12.018 Trustees of SSASs have the choice of continuing with their existing method of annuity purchase deferral or adopting the flexibility provisions in this Appendix. Whichever method is chosen it must apply to all members whose benefits are not yet in payment. Where the flexibility provisions of this Appendix are to be adopted the trustees of the SSAS may continue to apply the scheme’s existing arrangements for annuity purchase deferral to those Members or Dependents currently in receipt of a pension from the scheme. The trustees may also offer the flexibility provisions to a Member or Dependant who is already in receipt of a pension from the scheme. Once a scheme has adopted the provisions described in this Appendix it will not be possible to revert to scheme’s earlier method of deferral of annuity purchase.

A12.019 Trustees of SSASs adopting the flexibility provisions in this Appendix must ensure that their scheme documentation already contains the requirements of Regulations 4,6 and 7 of S.I.1991 No 1614, as amended, concerning assets franking pensions in payment. If the documentation does not contain these requirements then the documentation must be amended at the same time that the flexibility provisions in this Appendix are adopted.

A12.020 Similarly trustees of insured self-managed schemes (see paragraph 16.93) who adopt the flexibility provisions in this Appendix must ensure that the requirements for assets franking pensions in payment, mentioned in the paragraph above, are incorporated into the scheme documentation. Again, if the documentation does not contain these requirements then the documentation must be amended at the same time that the flexibility provisions in this Appendix are adopted.

PART I INCOME DRAWDOWN FOR EMPLOYER FUNDED BENEFITS

A12.101 Whenever employer funded benefits in pension or annuity form are due and payable to
the Member, or Dependant, under the rules of the scheme, they may with the consent of the Trustees elect to receive a pension in the form of income drawdown. The Member or Dependant may also with the consent of the Trustees elect to take an immediate annuity and to receive pension in the form of income drawdown.

* [A Member or Dependant who is already in receipt of an employer funded pension directly from the scheme having deferred the purchase of an annuity may with the consent of the Trustees elect to receive pension in the form of income drawdown. If so at the time of the election there must be an immediate calculation of the maximum annual amount of pension payable in the form of income drawdown.]

Conditions governing pension in the form of income drawdown for the Member

A12.102 On the date that employer funded benefits in pension or annuity form become due and payable the Member's Gross Scheme Fund must be tested to determine if there is a surplus. For the purposes of this test the Member must select a nominal form of benefit i.e. level or escalating pension and with or without guarantee. A current annuity rate appropriate to the selected form of the benefits must be determined either by the actuary advising the scheme Trustees or by current availability on the open market. The specific annuity rate should then be applied to the Member's Gross Scheme Fund. The result of this calculation is the nominal pension prospectively payable from the Member's Gross Scheme Fund. Where this nominal pension, plus the total pension and any pension equivalent of other benefits under the scheme and any Associated Scheme exceeds the Member's maximum permissible Aggregate Retirement Benefit the Member's Gross Scheme Fund includes an element of surplus. The surplus in the Member's Gross Scheme Fund is the proportion of the Member's Gross Scheme Fund which corresponds to the proportion by which the nominal pension must be reduced to prevent the total benefits exceeding the maximum permissible Aggregate Retirement Benefit. The surplus in the Member's Gross Scheme Fund should be dealt with immediately as if it were a surplus arising on the Member's retirement.

A12.103 Only the Member's Income Drawdown Fund can be used to provide pension in the form of income drawdown to the Member. No part of the Member's Income Drawdown Fund may be allocated to provide Dependents' benefits unless all or part of the fund is used to purchase an immediate annuity which provides contingent benefits for Dependents.

A12.104 The annual amount of pension paid in the form of income drawdown from the Member's Income Drawdown Fund forms part of the Member's Aggregate Retirement Benefit. The Aggregate Retirement Benefit cannot at any time exceed 1/60th times Final Remuneration times years of Service (not exceeding 40 years) or such greater amount as will not prejudice Approval. The annual amount of pension paid in the form of income drawdown from the Member's Income Drawdown Fund must be restricted as necessary to ensure that the Member's Aggregate Retirement Benefit is not excessive at any time.

A12.105 Subject to the restriction in paragraph A12.104, the maximum annual amount of pension payable under income drawdown will be determined using the GAD Tables by reference to the Member's Income Drawdown Fund available at that time to provide pension. Each year the Member may choose to take between 100% and 35% of the amount of the maximum pension determined by the GAD Tables provided this does not exceed the amount permitted in paragraph A12.104. The amount permitted in paragraph A12.104 must be paid where it is less than the pension at the 35% level determined by the GAD Tables. At intervals not exceeding 3 years the maximum annual pension must be recalculated using the GAD Tables. An immediate recalculation must be made whenever an Employer makes an additional contribution to the Member's Income Drawdown Fund for the benefit of the Member. An immediate recalculation must be made if the Trustees increase the Member's Income Drawdown Fund by re-allocating reversionary funds upon the predecease of a prospective Dependant. The Member must choose afresh the amount of pension taken in the form of income drawdown, after each recalculation. The requirement to take a pension of at least 35% of the maximum will not apply in the year in which the remaining fund is utilised for annuity purchase or upon the Member’s death.

A12.106 Once commenced pension in the form of income drawdown must be paid until the
Member’s death or until the whole of the Member's Income Drawdown Fund is utilised for annuity purchase.

A12.107 Once the Member has begun to receive pension in the form of income drawdown from the Member's Income Drawdown Fund no transfer in or out will be permitted in respect of that Member without the specific approval of the Inland Revenue.

A12.108 Up to the age of 75 the Member may require the Trustees to purchase an annuity or a tranche of annuity using all or part of the Member's Income Drawdown Fund. An annuity purchased using all or part of the Member's Income Drawdown Fund forms part of the Member’s Aggregate Retirement Benefit. Any guarantee period attaching to any annuity purchased from the Member's Income Drawdown Fund must be reduced by the length of time that pension in the form of income drawdown has been in payment from the Member's Income Drawdown Fund. Where both an annuity and a pension in the form of income drawdown are in payment concurrently, the maximum annual amount of pension must be immediately recalculated after the purchase of any tranche of annuity. The restriction in paragraph A12.104 applies after taking into account the amount of the annuity.

A12.109 The purchase of an annuity or of the final tranche of an annuity cannot be delayed beyond the Member’s 75th birthday.

A12.110 Any Member’s Income Drawdown Fund remaining after the completion of the final or sole annuity purchase should be dealt with as if it were a surplus arising on the Member’s retirement.

A12.111 Where the Member dies within 5 years of the date that pension in the form of income drawdown first became due and payable from the Member's Income Drawdown Fund a lump sum death benefit may be paid. The payment can be made irrespective of the type of guarantee (if any) which was selected by the Member under paragraph A12.102. The lump sum death benefit may be paid to any person at the discretion of the Trustees. The permissible lump sum death benefit should be calculated by subtracting the total of all instalments of pension paid in the form of income drawdown from the Member's Income Drawdown Fund from the total of 5 times the annual pension. For this purpose the annual pension means the maximum permissible annual pension that was first payable from the Member's Income Drawdown Fund determined in accordance with paragraph A12.105. Where part of the Member’s benefits have been secured by the purchase of a tranche of annuity from the Member's Income Drawdown Fund prior to the Member’s death, the value of the permissible lump sum death benefit must be further reduced by the amount of any lump sum guarantee payment attaching to the annuity, and also by the total amount paid under the annuity. Additionally the lump sum death benefit payable cannot exceed the value of the residue of the Member's Income Drawdown Fund.

A12.112 Subject to the requirements of contracting-out legislation where the Member dies within 10 years of the date that pension in the form of income drawdown first became due and payable from the Member's Income Drawdown Fund and no lump sum death benefit is paid (excluding any lump sum payable under continued life cover), a pension or annuity may be paid. The payment can be made irrespective of the type of guarantee (if any) which was selected by the Member under paragraph A12.102. This pension or annuity may be paid to any individual at the discretion of the Trustees. The pension or annuity may be paid until the tenth anniversary of the date that pension in the form of income drawdown first became due and payable from the Member's Income Drawdown Fund. The amount of the pension or annuity must not exceed the maximum permissible annual pension that was first payable from the Member's Income Drawdown Fund determined in accordance with paragraph A12.105. Where part of the Member’s benefits have been secured by the purchase of a tranche of annuity from the Member's Income Drawdown Fund prior to the Member’s death, the amount of the pension or annuity to be paid must be reduced by the amount of the annuity already in payment. Additionally the pension or annuity payable cannot exceed the value of the benefit which can be paid from or purchased with the residue of the Member's Income Drawdown Fund.

A12.113 Where the Member dies whilst in receipt of a pension under income drawdown a
Dependant's or Dependants' pension(s) or annuity(ies) may be provided. The pension or annuity may not be paid to a Dependant before the cessation of any pension or annuity payable to that Dependant under the terms of paragraph A12.112. After the payment of any lump sum or any pension under paragraphs A12.111 or A12.112 respectively, the residue, if any, of the Member’s Income Drawdown Fund should be dealt with as if it were a surplus on the Member’s retirement.

A12.114 Any initial pension or annuity payable to a Dependant, when aggregated with any other pension or annuity received in that capacity under the scheme and under all Associated Schemes shall not exceed an amount equal to 2/3rds of the maximum permissible Aggregate Retirement Benefit payable to the Member immediately before the Member’s death.

The aggregate amount of the pension or annuity payable to a Dependant may be increased once in payment up to the level of the maximum initial pension or annuity and additionally by 3% for each complete year or if greater, in proportion to any increase in the Index since the pension or annuity commenced.

Where benefits are to be paid to more than one Dependant the total of all the initial pensions/annuities cannot exceed the full amount of Member’s maximum permissible Aggregate Retirement Benefit.

A12.115 The residue of any Dependants’ fund after any lump sum death benefit and pension or annuity death benefits have been provided should be dealt with as if it were a surplus arising on the Member’s retirement.

Conditions governing pension in the form of income drawdown for Dependents

A12.116 On the date that employer funded benefits in pension or annuity form become due and payable the Dependant’s Gross Scheme Fund must be tested to determine if there is a surplus. For the purposes of this test the Dependant must select a nominal form of benefit i.e. level or escalating pension. For the purposes of this test it should be assumed that the pension is payable for life to the Dependant. A current annuity rate appropriate to the selected form of the benefits must be determined either by the actuary advising the scheme Trustees or by current availability on the open market. The specific annuity rate should then be applied to the Dependant’s Gross Scheme Fund. The result of this calculation is the nominal pension prospectively payable from the Dependant’s Gross Scheme Fund. Where this nominal pension when aggregated with any other pension or annuity provided under the scheme and all Associated Schemes exceeds the limit at paragraph A12.114 the Dependant’s Gross Scheme Fund includes an element of surplus. The surplus in the Dependant’s Gross Scheme Fund is the proportion of the Dependant’s Gross Scheme Fund which corresponds to the proportion by which the nominal pension must be reduced to prevent the total benefits exceeding the limit at paragraph A12.114.

Where benefits are to paid to more than one Dependant the nominal pensions plus the aggregate of any other pension or annuity provided under the scheme and all Associated Schemes are subject to the limit at paragraph A12.114. The actuary advising the scheme Trustees should determine the amount of any surplus in the Dependant’s Gross Scheme Fund.

The surplus in the Dependant’s Gross Scheme Fund should be dealt with immediately as if it were a surplus arising on the Member’s retirement.

A12.117 The annual amount of pension paid in the form of income drawdown from the Dependant’s Income Drawdown Fund forms part of the Dependant’s benefit which is limited in paragraph A12.114. The annual amount of pension in the form of income drawdown from the Dependant’s Income Drawdown Fund must be restricted as necessary to ensure that the limit in paragraph A12.114 is not exceeded.

A12.118 Subject to the restriction in paragraph A12.114, the maximum annual amount of pension payable under income drawdown will be determined using the GAD Tables by reference to the Dependant’s Income Drawdown Fund available at that time to provide pension. Each year the Dependant may choose to take between 100% and 35% of the amount of the maximum pension...
determined by the GAD Tables provided that this does not exceed the amount permitted in paragraph A12.114. The amount permitted in paragraph A12.114 must be paid where it is less than the pension at the 35% level determined by the GAD Tables. At intervals not exceeding 3 years the maximum annual pension must be recalculated using the GAD Tables. An immediate recalculation must be made whenever an Employer makes an additional contribution to the Dependant’s Income Drawdown Fund. The Dependant must choose afresh the amount of pension taken in the form of income drawdown, after each recalculation. The requirement to take a pension of 35% of the maximum will not apply in the year in which the remaining fund is utilised for annuity purchase or upon the Dependant’s death.

A12.119 Once commenced pension in the form of income drawdown must be paid until the Dependant’s death or until the whole of the Dependant’s Income Drawdown Fund is utilised for annuity purchase or until the Dependant ceases to be eligible to receive a pension under the scheme rules.

A12.120 Where the Dependant dies whilst in receipt of pension in the form of income drawdown the residual Dependant’s Income Drawdown Fund should be dealt with as if it were a surplus arising on the Member’s retirement.

A12.121 Once the Dependant has begun to receive pension in the form of income drawdown from the Dependant’s Income Drawdown Fund no transfer in or out will be permitted in respect of that Dependant without the specific approval of the Inland Revenue.

A12.122 Up to the age of 75 the Dependant may require the Trustees to purchase an annuity or a tranche of annuity using all or part of the Dependant’s Income Drawdown Fund. An annuity purchased using all or part of the Dependant’s Income Drawdown Fund forms part of the Dependant’s benefit which is limited in paragraph A12.114. Where both an annuity and a pension in the form of income drawdown are in payment concurrently, the maximum annual amount of pension under income drawdown must be immediately recalculated after the purchase of a tranche of annuity. The restriction in paragraph A12.114 applies after taking into account the amount of the annuity.

A12.123 The purchase of an annuity or the final tranche of an annuity cannot be delayed beyond the Dependant’s 75th birthday or if earlier the date that the deceased Member would have attained the age of 75.

A12.124 Any Dependant’s Income Drawdown Fund remaining after the completion of the final or sole annuity purchase should be dealt with as if it were a surplus arising on the Member’s retirement.

* Drafting note: The wording in brackets will only be required for SSASs with Members who are already in annuity deferral and those Members are to be given the chance to opt for the new income drawdown system.

**PART II INCOME DRAWDOWN FOR AVC BENEFITS PAID BEFORE THE DATE BENEFITS FUNDED BY THE EMPLOYER BECOME DUE AND PAYABLE**

A12.201 From the age of 50 onwards and with the consent of the Trustees the Member may take benefits from the Member’s AVC Fund before the date benefits funded by the Employer come into payment.

A12.202 The following conditions apply in the period before benefits funded by the Employer become due and payable.

A12.203 Benefits from the Member’s AVC Fund must be taken as a pension in the form of income drawdown.

A12.204 The maximum annual amount of pension payable under income drawdown will be determined using the GAD Tables, by reference to the Member’s AVC Fund available at that time to provide pension. Each year the Member may choose to take between 100% and 35% of the
maximum pension. At intervals not exceeding 3 years the maximum annual amount of pension under income drawdown must be recalculated using the GAD Tables. The Member must choose afresh the amount of pension they take in the form of income drawdown, after each recalculation.

A12.205 If the Member's AVC Fund is augmented by means of a transfer from another scheme, the maximum annual pension taken under income drawdown must be recalculated immediately.

A12.206 The requirement to take a pension of at least 35% of the maximum will not apply in the year in which the remainder of the Member's AVC Fund is utilised for annuity purchase or upon the Member's death.

A12.207 The scheme rules on death in service should be applied where a Member dies whilst in receipt of pension under income drawdown before the date benefits funded by the Employer become due and payable.

A12.208 Where the scheme rules permit, a Class B Member or a Class C Member in receipt of pension in the form of income drawdown may elect to become a Class A Member up to the date that the benefits funded by the Employer become due and payable.

A12.209 Any Lump Sum Retirement Benefit from the Member's AVC Fund, which is permitted by the scheme rules, cannot be taken until the date benefits funded by the Employer become due and payable.

A12.210 Once commenced pension in the form of income drawdown must be paid until the Member’s death or until at least the date benefits funded by the Employer become due and payable or until the remaining AVC fund is transferred out of the scheme as part of a general transfer of the Member's benefits.

PART III INCOME DRAWDOWN FOR AVC BENEFITS PAID AT OR AFTER THE DATE BENEFITS FUNDED BY THE EMPLOYER BECOME DUE AND PAYABLE

Benefit limits

A12.301 When the Member's maximum permissible Aggregate Retirement Benefit is being calculated and the Member's AVC Fund will continue to exist because either:

(a) the Member is to draw or to continue to draw pension in the form of income drawdown from the Member's AVC Fund or

(b) the Member is to defer taking annuity and pension benefits from the Member's AVC Fund.

the pension equivalent of the benefits from the Member's AVC Fund (excluding any Lump Sum Retirement Benefit) should be calculated as follows.

A12.302 The amount of the pension equivalent should be taken as the maximum annual pension determined by applying the GAD Tables to the Member's AVC Fund available at that time to provide pension. The Member's AVC Fund should be taken at its value after the payment of any Lump Sum Retirement Benefit or the purchase of any tranche of annuity which is to be payable from the date that the benefits funded by the Employer become due and payable.

A12.303 Where the Member has already received a pension in the form of income drawdown the following additional condition must be observed if the Member is either a Controlling Director or a Member whose Remuneration in any complete year of assessment after attaining the age of 50 has exceeded ½ of the Permitted Maximum for the year in question. The amount of all pension instalments taken under income drawdown under this scheme and under any Associated Scheme from which a transfer of an AVC fund has been received must be added to the value of the Member's AVC Fund. The maximum annual pension should then be determined by applying the GAD Tables to the aggregate of the Member's AVC Fund value plus the pension instalments.
A12.304 Any annuity purchased from the AVC fund and any Lump Sum Retirement Benefit paid from the *Member’s AVC Fund* will form part of the Member’s Aggregate Retirement Benefit and Lump Sum Retirement Benefit respectively.

**Options for benefits from the Member’s AVC Fund**

A12.305 At the time that the benefits funded by the Employer become due and payable the Member, with the consent of the Trustees, has the following options.

- To take a Lump Sum Retirement Benefit where scheme rules permit
- An immediate annuity may be purchased
- A pension in the form of income drawdown may be paid (see paragraphs A12.306 to A12.316 below)
- A combination of an immediate annuity and a pension in the form of income drawdown may be paid (see paragraphs A12.306 to A12.316 below)
- To defer the taking of annuity and pension benefits (see paragraphs A12.317 to A12.321). Where pension in the form of income drawdown is subsequently paid see paragraphs A12.307 to A12.316 below. (References in paragraphs A12.311 and A12.312 to the death of the Member within 5 years and 10 years respectively of the date benefits funded by the Employer became due and payable should be read as references to the death of the Member within 5 years and 10 years respectively of the date of the start of pension paid in the form of income drawdown from the *AVC fund*.)

**Conditions governing pension in the form of income drawdown and deferral of pension/annuity benefits**

A12.306 Where the Member has already received pension in the form of income drawdown there should be a recalculation of the maximum annual pension payable, using the GAD Tables, at the date benefits funded by the Employer became due and payable.

A12.307 The maximum annual amount of pension payable under income drawdown will be determined using the GAD Tables, by reference to the *Member’s AVC Fund* available at that time to provide pension. Each year the Member may choose to take between 100% and 35% of the maximum pension. At intervals not exceeding 3 years the maximum annual amount of pension under income drawdown must be recalculated using the GAD Tables. The Member must choose afresh the amount of pension they take in the form of income drawdown, after each recalculation. The requirement to take a pension of at least 35% of the maximum will not apply in the year in which the remainder of the *Member’s AVC Fund* is utilised for annuity purchase or upon the Member’s death.

A12.308 Once commenced pension in the form of income drawdown must be paid until the Member’s death or until the whole AVC fund is utilised for annuity purchase.

A12.309 Up to the age of 75 the Member may require the Trustees to purchase an annuity or a tranche of annuity using all or part of the AVC fund. Any guarantee period attaching to any annuity purchased from the AVC fund must be reduced by the length of time that pension under income drawdown has been in payment since the date benefits funded by the Employer became due and payable. When a tranche of annuity is purchased and a residual *Member’s AVC Fund* continues to exist the maximum annual amount of any pension under income drawdown must be immediately recalculated using the GAD Tables.

A12.310 The purchase of an annuity or of the final tranche of an annuity cannot be delayed beyond the Member’s 75th birthday.

A12.311 Where the Member dies within 5 years of the date that benefits funded by the Employer
became due and payable a lump sum death benefit may be paid. The lump sum death benefit may be paid to any person at the discretion of the Trustees. The permissible lump sum death benefit should be calculated by subtracting the total of all instalments of pension paid under income drawdown since the date benefits funded by the Employer became due and payable from the total of 5 times the annual pension. For this purpose the annual pension means the maximum annual pension determined in accordance with paragraph A12.307 at the date benefits funded by the Employer became due and payable. Where part of the Member’s benefits have been secured by the purchase of annuity from the AVC fund prior to the Member’s death, the value of the permissible lump sum death benefit must be further reduced by the amount of any lump sum guarantee payment attaching to the annuity, and also by the total amount paid under the annuity. Additionally the lump sum death benefit payable cannot exceed the value of the residue of the Member’s AVC Fund.

A12.312 Where the Member dies within 10 years of the date that benefits funded by the Employer became due and payable and no lump sum death benefit is paid a pension or annuity may be paid to any individual at the discretion of the Trustees. The pension or annuity may be paid until the tenth anniversary of the date that benefits funded by the Employer became due and payable. The amount of the pension or annuity must not exceed the maximum annual pension determined in accordance with paragraph A12.307 at the date benefits funded by the Employer became due and payable. Where part of the Member’s benefits have been secured by the purchase of a tranche of annuity from the AVC fund prior to the Member’s death, the amount of the pension or annuity to be paid must be reduced by the amount of the annuity already in payment. Additionally the pension or annuity payable cannot exceed the value of the benefit which can be paid from or purchased with the residue of the Member’s AVC Fund.

A12.313 Where the Member dies whilst in receipt of a pension in the form of income drawdown a Dependant’s or Dependants’ pension(s) or annuity(ies) may be provided. The pension or annuity may not be paid to a Dependant before the cessation of any pension or annuity payable to that Dependant under the terms of paragraph A12.312.

A12.314 Any initial pension or annuity payable to a Dependant, when aggregated with any other pension or annuity received in that capacity under the scheme and under all Associated Schemes shall not exceed an amount equal to 2/3rds of the maximum permissible Aggregate Retirement Benefit payable to the Member immediately before the Member’s death.

The aggregate amount of the pension or annuity payable to a Dependant may be increased once in payment up to the level of the maximum initial pension or annuity and additionally by 3% for each complete year or if greater, in proportion to any increase in the Index since the pension or annuity commenced.

Where benefits are to be paid to more than one Dependant the total of all the initial pensions/annuities cannot exceed the full amount of Member’s maximum permissible Aggregate Retirement Benefit.

A12.315 With the consent of the Trustees a Dependant may choose to take the benefit from the AVC fund in the circumstances stated in paragraph A12.313 as pension in the form of income drawdown. This benefit option will be permitted only where that Dependant is to simultaneously receive other benefits from the scheme as pension in the form of income drawdown. The payment of such a pension will be governed by paragraphs A12.116 to A12.124.

A12.316 Any residue in the AVC fund remaining after the provision of any lump sum death benefit and any death benefits in pension/annuity form should be paid to the Member’s legal personal representative.

A12.317 The taking of pension/annuity benefits cannot be deferred if the Member has already taken pension in the form of income drawdown before the date that benefits funded by the Employer became due and payable.

A12.318 Where the Member is to defer taking benefits in pension/annuity form a Lump Sum
Retirement Benefit may be paid from the **Member's AVC Fund** if the scheme rules permit. No Lump Sum Retirement Benefit may be paid when pension/annuity benefits subsequently come into payment.

A12.319 Where the Member dies after the date that benefits funded by the Employer became due and payable, and pension/annuity benefits from the **Member's AVC Fund** remain in deferment, a second surplus **AVC** check must be made as prescribed in the *Retirement Benefits Schemes (Restriction on Discretion to Approve)(Additional Voluntary Contributions) Regulations 1993 – S I 1993 No 3016*, as amended from time to time. Any surplus **AVCs** must be repaid in accordance with the rules of the scheme.

A12.320 The Member may choose to take their deferred benefits totally in annuity form or as pension in the form of income drawdown or as a combination of the two. The purchase of an annuity or of the final tranche of an annuity cannot be delayed beyond the Member’s 75th birthday. Pension in the form of income drawdown cannot be paid after the Member’s 75th birthday.

A12.321 When the sole annuity or the final tranche of the annuity is to be purchased and the **AVC** fund includes funds to provide **Dependant**’s benefits but the Member has no prospective **Dependants** at that point in time, the whole of the **AVC** fund may be used to purchase a single life annuity for the Member.

**PART IV**

**Lump sum retirement benefit**

A12.401 For scheme members whose lump sum retirement benefit is not calculated by reference to the amount of pension payable, the use of income drawdown will not affect the amount of the lump sum benefit. However, members whose lump sum retirement benefit is based on their pension (see paragraph 8.7 and paragraph 8.28) will only be able to draw a lump sum as measured by the amount of initial pension payable before commutation and any allocation.

A12.402 For illustrative purposes, detailed below are two examples of a calculation of a Finance Act 1989 regime member’s lump sum under income drawdown:

**Example 1**

1st stage: value **Member’s Gross Scheme Fund** and check for surplus over maximum benefits

- **Member’s Gross Scheme Fund** value: £200,000
- open market annuity rate (RPI + 10 yr gte) 18: 1
- member’s maximum approvable benefit: £20,000 pa
- maximum permissible fund is £360,000 (£20,000 x 18)

therefore

the whole of the **Member’s Gross Scheme Fund** of £200,000 can be brought forward into the drawdown process.

2nd stage: calculate maximum lump sum under drawdown

- **Member’s Income Drawdown Fund** value £200,000
- annuity rate from **GAD Tables** 12: 1
  
  * gross pension value is (£200,000/12) i.e. £16,667
  
  * [£16,667 is within approvable limits (£20,000)]
maximum lump sum is \(2.25 \times (\£200,000/12)\) i.e. £37,500 [assuming maximum drawdown]

drawdown fund is (£200,000 - £37,500) i.e. £162,500

drawdown pension is (£162,500/12) i.e. £13,542 @ 100% of income drawdown

therefore

the permissible lump sum is £37,500 if income drawdown of £13,542 pa is taken.

**Example 2**

1st stage: value member’s fund and check for surplus over maximum benefits

**Member’s Gross Scheme Fund** value: £200,000

open market annuity rate (RPI + 10 yr gte) 18: 1

member’s maximum approvable benefit: £10,000 pa

therefore

maximum permissible fund is £180,000 and £20,000 is surplus and cannot be brought forward into the drawdown process – the £20,000 will stay in the scheme if it is a CTF or be refunded to the employer otherwise

2nd stage: calculate maximum lump sum under drawdown

**Member’s Income Drawdown Fund** value £180,000

annuity rate from **GAD Tables** 12: 1

* gross pension value is (£180,000/12) i.e. £15,000

* (£15,000 is greater than approvable limits (£10,000), so £10,000 must be used)

maximum lump sum is \(2.25 \times £10,000\) i.e. £22,500 [assuming maximum drawdown]

drawdown pension is (£10,000 - £1,875 [£22,500/12 {12: 1 is the commutation factor}])

i.e. £8,125

therefore

the permissible lump sum is £22,500 if income drawdown of £8,125 is taken and

£8,125 is permissible under drawdown because it is within 100%-35% range

drawdown fund is (£180,000 - £22,500) i.e. £157,500

drawdown range is (£157,500/12) i.e. £13,125 @ 100%; £4,594 @ 35%.

* Where the **GAD Tables** annuity rate differs from the commutation factor (which is 12: 1 for ‘89 members), the comparison with maximum approvable benefits is more complex.
N.B. The fund values above do not include any AVC funds.

**PART V DEFINED TERMS**

A12.501 All the terms which are in bold type or in capitals in Parts I to IV are defined terms.

A12.502 The terms in bold type are unique to this Appendix and are defined individually (see below).

A12.503 The terms in capitals are assumed to be defined already in scheme documentation.

A12.504 The terms “Dependant”, “Employer”, “Member” and “Trustee” are terms of general use in documentation.

A12.505 The terms “Aggregate Retirement Benefit”, “Approval”, “Associated Scheme”, “Class A Member”, “Class B Member”, “Controlling Director”, “Lump Sum Retirement Benefit”, “Final Remuneration”, “Index” and “Permitted Maximum” are all terms defined in the model limit rules for schemes, the PS 123 (7/94). References in this Appendix to these terms should be read as references to the definitions in the PS 123. The PS 123 is available on request from IR SPSS (Sylvia Porter on 0115 974 1646 or Stella Jones on 0115 974 1621).

**AVC**: Additional Voluntary Contribution.

**Dependant's Gross Scheme Fund**: the money purchase fund to provide benefits for the Dependant(s) which is derived from employer contributions and the Member’s compulsory contributions.

**Dependant’s Income Drawdown Fund**: the Dependant’s Gross Scheme Fund after any required reduction of surplus, which is available at any time to pay pension in the form of income drawdown to the Dependant. Where there is more than one Dependant each Dependant will have a separate income drawdown fund and the drawdown process should be operated independently for each Dependant.

**GAD Tables**: the Government Actuary’s Department Tables on a single life basis.

**Member’s AVC Fund**: that proportion of the total AVC fund which is held solely to provide benefits for the Member, as distinct from the fund (if any) held to provide benefits for the Dependents of the Member.

**Member’s Gross Scheme Fund**: the money purchase fund to provide benefits for the Member which is derived from employer contributions and the Member’s compulsory contributions. This fund is the residue after the payment of any Lump Sum Retirement Benefit and the purchase of any immediate annuity at the date benefits in pension/annuity form first become payable to the Member.

**Member’s Income Drawdown Fund**: the Member’s Gross Scheme Fund after any required reduction of surplus, which is available at any time to pay pension in the form of income drawdown.
Appendix XIII. Pension debits

Calculation of Pension Debts

A13.1 Where:

- a member’s benefits are subject to a pension sharing order, and
- the member does not fall within the administrative easement described in paragraph 7.7

the pension debit must be taken into account as an aggregable benefit when calculating the maximum total benefits that can be paid to the member or to the widow, widower, surviving civil partner or dependants of the member. The maximum total benefits (pension and lump sum) that could have been paid to the member had the pension sharing order not occurred must be reduced by the pension debit (see paragraph 7.2). The maximum pension for the widow, widower, surviving civil partner or dependants of the member must be calculated by reference to the maximum pension that could have been paid to the member, after reduction to take account of the pension debit (see paragraphs 11.7 and 12.2).

A13.2 The pension debit is the amount of benefit rights given up by a scheme member and allocated to the ex spouse or former civil partner of the member at the time of a pension sharing order. Once the pension sharing order has taken place there is no link between what were previously the member’s benefits rights (the pension debit) and the corresponding benefit rights acquired by the ex spouse or former civil partner (the pension credit). This is because an underlying fundamental principle of pension sharing orders is to achieve a “clean break” between the divorcing couple in relation to pension matters. However, since no special tax reliefs are given for divorcing couples, it is still necessary to take into account the pension debit for the purposes of establishing the maximum approvable benefits for or in respect of a member at the relevant date, i.e the date of retirement, leaving pensionable service or death as the case may be. This is achieved by converting the pension debit into a notional deferred pension at the time of the pension sharing order. The notional amount of pension is then revalued from the time of the pension sharing order to the relevant date.

A13.3 The revalued pension equivalent of the pension debit is a “negative deferred pension” as it is the amount by which the member’s maximum total benefits (based on the amount that could be paid had the pension sharing order not occurred) must be reduced.

A13.4 The following examples give guidance on how to value the pension debit for the purpose of calculating maximum total benefits when:

- the member’s benefits are in payment
- the member’s benefits crystallize on leaving pensionable service
- the member’s benefits are paid
- the member dies, and
- the member’s benefits are transferred.

A13.5 The examples and notes are based on guidance issued by the Department of Social Security (DSS) in December 2000 – “Pension Sharing on Divorce or Nullity – Illustrative Examples of the Treatment of a Pension Debit”. The DSS guidance is available on the DSS website www.dss.gov.uk

Please note that enquiries about the effect of the pension debit in relation to contracting-out issues should be referred to the DSS.
Notes

1. The cash equivalent transfer value of the pension rights to which a member would be entitled (the “relevant benefits” in section 29 of the Welfare Reform and Pensions Act 1999) forms the basis of the pension debit and of the pension credit.

2. In implementing a pension debit a key consideration is which benefits are included as the “relevant benefits” in the calculation of the cash equivalent transfer value. These will form the “qualifying benefits” referred to in section 31 of the Welfare Reform and Pensions Act. Since allowance should be made, either explicitly or implicitly, in the calculation for benefits such as any lump sums payable on death for deferred or pensioner members, and benefits to dependants following death, such benefits should be reduced appropriately by the pension debit.

3. Except for a member in active pensionable service the “relevant benefits” are broadly all the benefits to which the member is entitled. For a member who is in pensionable service the relevant benefits are those which the member would receive if he or she had left service immediately before the day on which the pension sharing order had come into effect. Hence for a member in pensionable service the debit will be a proportion of the deferred benefits that she or he would have received if she or he had become a deferred pensioner at the time of the divorce (the “qualifying benefit”). This means that the situation for implementing pension debits against members in active pensionable service may have features where the pension debit and the main scheme benefit behave in slightly different ways – this is covered in example 3.

4. A divorce under Scottish law will see the pension sharing order made in terms of an amount rather than a percentage value of the cash equivalent transfer value. It is expected that schemes may wish to calculate the initial amount of the pension debit by turning the amount into a percentage value by comparing it with the cash equivalent transfer value of the relevant benefits on which the pension share was based. Once this has been done the pension debit can be enforced in the manner shown in these examples. For Scottish divorces where the pension benefits included in the matrimonial property on which the cash equivalent transfer value, and therefore the pension sharing order, was based are not the whole of the pension rights under the scheme the pension debit should similarly apply only to the rights included in cash equivalent transfer value.

5. The examples assume that rights in the State Earnings-Related Pension Scheme will generally not be shared where shareable rights exist in a non-state pension arrangement. Where rights in a pension arrangement that is or has been contracted-out on a salary-related basis are shared, the Guaranteed Minimum Pension (GMP) from the non-state arrangement (after sharing) and the State Earnings-Related Pension Scheme net of contracted-out deduction will probably no longer equal the State Earnings-Related Pension Scheme had the member not been contracted-out. Although this is not covered with a numerical example, scheme administrators may like to be aware of this feature in case their members raise queries about their total benefits.

6. The examples all assume that the member who is subject to the pension sharing order is male. The same principles apply in enforcing a pension debit against a female member’s pension rights.
A pensioner aged 68 with a pension of £10,000 a year is made subject to a pension sharing order. The share to be given to the member’s former spouse is 40%. Of the £10,000 a year pension, £1,000 a year represented pre-88 GMP and £500 a year represented post-88 GMP. Other than the GMP elements the whole pension is subject to increases in line with limited-price indexation. Taking the valuations of these different components into account should produce the following result.

At the time of the pension sharing order (age 68)

<table>
<thead>
<tr>
<th>Total gross pension</th>
<th>£10,000 a year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pension debit</td>
<td>£4,000 a year</td>
</tr>
<tr>
<td>Pension net of debit</td>
<td>£6,000 a year</td>
</tr>
</tbody>
</table>

Splitting the debit and residual pension into GMP and non-GMP

The total gross pension was split

| Pre-88 GMP | £1,000 a year |
| Post-88 GMP | £500 a year |
| Thus excess over GMP (≤ £10,000 – £1,000 – £500) | £8,500 a year |

The debit can be split in the same proportions

| Pre-88 GMP included in debit (≤ £4,000 x £1,000 / £10,000) | £400 a year |
| Post-88 GMP included in debit (≤ £4,000 x £500 / £10,000) | £200 a year |
| Excess over GMP included in debit (≤ £4,000 – £400 – £200) | £3,400 a year |

Hence the residual pension after the pension debit is made up of

| Pre-88 GMP (≤ £1,000 – £400) | £600 a year |
| Post-88 GMP (≤ £500 – £200) | £300 a year |
| Excess over GMP (≤ £6,000 – £600 – £300) | £5,100 a year |
| or (≤ £8,500 – £3,400) | |

In the first year after the pension sharing order, assume that the LPI increase is 3.5%. Thus the increase which the scheme must pay on post-88 GMPs is 3.0% a year. The increase on the pension net of debit as follows:

| Increase on pre-88 GMP | £0 a year |
| Increase on post-88 GMP (≤ £300 x 0.03) | £9 a year |
| Increase on excess over GMP (≤ £5,100 x 0.035) | £179 a year |
| Total increase | £188 a year |
Example 1A. Death of a Pensioner Member with a Pension Debit

Now suppose that the pensioner in example 1 remarries almost immediately after the divorce, but
dies aged 70. *Retail Prices Index* (RPI) increases were 3.5% in the first year (as above) and 2.5% in
the second year.

By the time of death, the pension net of the *pension debit* has increased to

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pre-88 GMP (no increases paid by scheme)</td>
<td>£ 600 a year</td>
</tr>
<tr>
<td>Post-88 GMP (increases up to 3% paid by scheme)</td>
<td>£ 317 a year</td>
</tr>
<tr>
<td>Excess (LPI increases paid)</td>
<td>£ 5,411 a year</td>
</tr>
</tbody>
</table>

Under the scheme rules the spouse inherits a 2/3 rate pension, i.e.

\[
\text{Total pension net of debit at time of death} = (\text{ (£300 + £9) x (1 + 0.025)})
\]

\[
\text{£ 6,328 a year}
\]

Under the scheme rules the spouse inherits a 2/3 rate pension, i.e.

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>(= £6,328 x 2/3)</td>
<td>£ 4,219 a year</td>
</tr>
</tbody>
</table>

of which a portion is GMP (ignored in this example)

The widow’s pension is also affected by the *pension debit* because
benefits to widows were included in the valuation of the total benefit at the
time of the pension share, of which the specified proportion was awarded
to the former spouse.

As a check, consider the position of the member if there had been no
*pension debit*.

The pension at time of death would have been

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pre-88 GMP (no increases paid by scheme)</td>
<td>£ 1,000 a year</td>
</tr>
<tr>
<td>Post-88 GMP (£500 x (1 + 0.03) x (1 + 0.025))</td>
<td>£ 528 a year</td>
</tr>
<tr>
<td>Excess over GMP (£8,500 x (1 + 0.035) x (1 + 0.025))</td>
<td>£ 9,017 a year</td>
</tr>
<tr>
<td>Total</td>
<td>£10,545 a year</td>
</tr>
</tbody>
</table>

And the spouse’s pension with no debit, two-thirds of this, is

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ratio of spouse’s pension paid after debit (£4,219) to this amount is 60%</td>
<td>60%</td>
</tr>
<tr>
<td>(£4,219 / £7,030), as to be expected following a 40% debit.</td>
<td>£ 7,030 a year</td>
</tr>
</tbody>
</table>

Any lump sum benefit related to the level of the pension (e.g. “balance” payments or “guarantees”
in early years of retirement) should be adjusted to reflect the rate of the *pension debit* on the same
basis, even if they have not explicitly been included in the valuation of pensions in payment.
Example 2. Pension Debit for Deferred Pensioner of a Defined Benefits Scheme

A13.8
A deferred pensioner of a defined benefits scheme aged 50 has a deferred pension, including revaluation to date of divorce, of £10,000 a year. The scheme has a normal retirement date of 60. Based on the cash equivalent transfer value (whose value is unimportant in this context), the member is made subject to a pension debit of 40%, which directly represents a pension debit of a deferred pension of £4,000 a year.

At divorce at age 50 total gross deferred pension

\[ \text{Pension debit} = \frac{40\% \times £10,000}{1.041^{10}} = £4,000 \text{ a year} \]

At normal retirement date (60)

Increases to deferred benefit in line with statutory revaluation, say 4.1% a year on average (50% over 10 years – used in all examples)

Thus total gross pension (\( = £10,000 \times 1.041^{10} \))

\[ \text{Pension debit} (= £4,000 \times 1.041^{10}) \]

Net pension put into payment (\( = £15,000 - £6,000 \))

\[ £9,000 \text{ a year} \]

If the deferred pension contained a GMP, anti-franking will apply at GMP payment age (65 if member is male, 60 for a woman)

Assume that of the £10,000 pension at age 50, £2,000 was GMP.

Increases to GMP at statutory fixed rate revaluation of 6.25% a year

Gross GMP (\( = £2,000 \times 1.0625^{14} \))

\[ £4,673 \text{ a year} \]

Gross excess over GMP (\( = £8,000 \times 1.041^{10} \times 1.035^{5} \))

\[ £14,252 \text{ a year} \]

Total anti-franking minimum gross of debit (\( = £4,673 + £14,252 \))

\[ £18,925 \text{ a year} \]

This will generally be higher than the scheme pension at GMP payment age – for example this could be (\( = £15,000 \times 1.035^{5} \))

\[ £17,815 \text{ a year} \]

Therefore anti-franking will require a one-off increase in the pension-in-payment at GMP payment age.

The calculation of the cash equivalent transfer value on which the pension sharing order was based should take into account anti-franking. Thus the debit, calculated as a proportion of that cash equivalent transfer value, is also bound by anti-franking requirements (subject in due course to the new requirements in the Child Support Pensions and Social Security Act 2000 where applicable).

The debit can be split into GMP and excess elements

GMP in debit at age 50 (\( = 40\% \times £2,000 \))

\[ £800 \text{ a year} \]

Excess over GMP in debit at age 50 (\( = 40\% \times £8,000 \))

\[ £3,200 \text{ a year} \]

At GMP payment age (65)

GMP in debit (\( = £800 \times 1.0625^{14} \))

\[ £1,869 \text{ a year} \]

Excess over GMP in debit (\( = £3,200 \times 1.041^{10} \times 1.035^{5} \))

\[ £5,701 \text{ a year} \]

Total debit after allowing for anti-franking (\( = £1,869 + £5,701 \))

\[ £7,570 \text{ a year} \]

The total debit is still 40% of the gross pension after the effects of complying with the anti-franking requirements.

The net pension after allowing for anti-franking at age 65 is thus

\( = £18,925 - £7,570 \)

\[ £11,355 \text{ a year} \]

Note that where the scheme revalues GMPs at a fixed rate, the same fixed rate should be used for the GMP element of the debit for a deferred pensioner as for the gross benefit. This is because the transfer value, and thus the pension debit, should have been calculated on this basis.
Example 2A. Commuting Pension for Lump Sum at Retirement

A13.9
At retirement the member in example 2 may wish to commute part of his pension in order to provide a lump sum (if the scheme rules allow this). The maximum lump sum will depend on whether or not the member has pre 17 March 1987 continued rights.

For a member without continued rights
Maximum pension at age 60 without debit £15,000 a year
Maximum lump sum (= 2.25 x £15,000) £33,750
If maximum lump sum taken, then maximum residual pension using the divisor 12 (see paragraph 7.2) is
(= £15,000 – (£33,750 / 12)) £12,188 a year

Maximum pension at age 60 with debit £9,000 a year
Maximum lump sum (= 2.25 x £9,000) £20,250
If maximum lump sum taken, then maximum residual pension using the divisor 12 (see paragraph 7.2) is
(= £9,000 – (£20,250 / 12)) £7,313 a year

The maximum lump sum and the maximum pension where the maximum lump sum has been taken are 60% of the amount without the debit.

For a member with pre 17 March 1987 continued rights the maximum lump sum is not directly linked to the pension payable
Maximum lump sum without debit, say £39,000
Maximum residual pension if maximum lump sum taken without debit
(= £15,000 – (£39,000 / 12)), £11,750 a year
assuming that the scheme has adopted a 12:1 commutation factor for all members.

Where the pre 17 March 1987 continued rights member has a debit, the maximum lump sum can be calculated on the better of two bases
Approach one: maximum lump sum
(= £39,000 – (2.25 x £6,000)) £25,500
And maximum pension if maximum lump sum is taken is
(= £9,000 – (£25,500 / 12)) £6,875 a year

Approach two: maximum lump sum
(= 2.25 x £9,000) £20,250
And maximum pension if maximum lump sum is taken is, as before
(= £9,000 – (£20,250 / 12)) £7,313 a year
Example 2B. Death during Deferment

A13.10

If the pension scheme member remarries and dies at age 55
Assume that deferred pension revalued to date of death gross of debit is
(=£10,000 x 1.0415) £12,225 a year
Further assume that the scheme pays a 2/3 spouse’s pension (and ignore anti-franking in this case)
Then gross pension payable to widow is (= £12,225 x 2/3) £8,150 a year
Using the same rules for calculating the amount of the debit as for the main scheme pension gives a debit at death of
(= £4,000 x 1.0415 x 2/3) £3,260 a year
And thus a net pension for the widow of (= £8,150 – £3,260) £4,890 a year
The debit from the widow’s pension is still 40% of the scheme benefit, as expected.

Any benefits to other dependants (e.g. to children) should also be reduced by the debit in the appropriate proportion if they are included in the cash equivalent transfer value on which pension sharing was based.

Example 2C. Deferred Pensioner Choosing to Take Pension after Normal Retirement Date

A13.11

Under regulation 8 of the Occupational Pension Schemes (Preservation of Benefit) Regulations 1991 [SI 1991 No 167], a preserved pension can come into payment after scheme normal pension age provided that the value of the late retirement pension is at least as great as the value of the pension payable from scheme normal pension age. This implies that schemes must offer increases (enhancements) to deferred pensioner members who wish to receive their pension after scheme normal pension age, if such postponement is permitted by the scheme. Such a postponement of pension payment will not be possible in all cases (see paragraph 10.8).

The following example is based on the assumption that the scheme offers an increment of 10% a year for each year after the scheme normal pension age that the benefit is deferred, with allowance for LPI increases as well (at an average of 3.5% a year over the period in question). Also, that the member in the example 2 chooses to defer his pension so that it commences at age 65.

Gross pension before debit (for simplicity this does not take into account anti-franking requirements)
(= £10,000 x 1.04110 x 1.0355 x (1 + 5 x 0.10)) £26,723 a year
The pension debit, which must be calculated and brought into account whenever the main scheme benefits are first put into payment, should receive similar enhancements
So the pension debit which comes into payment at 65 is
(= £4,000 x 1.04110 x 1.0355 x (1 + 5 x 0.10)) £10,689 a year
The pension net of pension debit is thus (= £26,723 – £10,689) £16,034 a year

Example 2D. Other Contingencies for Deferred Pensioners (Ill-Health or Incapacity Pension, Voluntary Early Retirement)

A13.12

Please see corresponding examples for active members (examples 3D and 3E that follow).
Example 2E. Deferred Pensioner Subsequently Re-admitted to Active Membership

A13.13
At age 52 the deferred pensioner in example 2 is readmitted to active scheme membership, and the 20 years' service on which his deferred pension was based is reinstated. His new salary is £35,000. By scheme normal retirement date, 60, his salary has increased to £48,000. He now has 28 years' service.

Gross pension at scheme normal retirement date is
\[
(\frac{28}{60} \times £48,000) \quad £22,400 \text{ a year}
\]
The pension debit, however, behaves exactly as if he had remained a deferred pensioner, i.e. from normal retirement date it is
\[
(\text{as in example 2 above}) \quad £6,000 \text{ a year}
\]
Leaving a net pension of (= £22,400 – £6,000) £16,400 a year

Both scheme pension and debit may receive an increase at GMP payment age (65) as result of the application of anti-franking rules.

The pension debit is calculated as if he remained a deferred pensioner, because its treatment must be consistent with the calculation of the cash equivalent transfer value on which it was based.

Any cost to the scheme experienced as a result of a deferred pensioner rejoining and having past service counting in full is unaffected by the pension debit.
Example 3. Pension Debit for Active Member

A13.14
A 50-year-old male active member of a defined benefits scheme with a 1/60ths accrual rate has 20 years’ service and a salary of £30,000 a year, giving an accrued (deferred) pension of £10,000 a year. The scheme has a normal retirement date of 60. Based on the cash equivalent transfer value, the member is subject to a pension debit of 40%, which leads directly to a pension debit of a deferred pension equivalent of £4,000 a year.

At age 50
Total gross deferred pension as if service terminated at divorce on which cash equivalent transfer value for pension sharing was based
Pension debit

At scheme normal retirement date (60)
Salary, say
Service
Thus gross pension at scheme pension age (= £48,000 x 30/60) Increases to debit in line with statutory revaluation as if it were a deferred benefit, say 4.1% a year on average (50% over 10 years)
Pension debit (= £4,000 x 1.041^{10})
Net pension put into payment (= £24,000 – £6,000)
Both scheme pension and debit may need to be increased at, GMP payment age, 65 in the case of a man, to meet the anti-franking requirements – the treatment of the debit would be same as in the case of the deferred member in example 2.

Revaluation of GMP element of debits for active members

In the private sector, schemes will generally choose to revalue the GMP element of a deferred pension in line with fixed rate revaluations. However, there is the option for schemes to revalue the GMP element of deferred pensions in line with section 148 (Social Security Administration Act 1992) orders as with GMPs for those who remain in active service (see section 16 of the Pension Schemes Act 1993). The fixed rate for GMP revaluations is set to approximate the level of future section 148 orders that may be expected.

Schemes may decide to revalue the GMP element of debits in line with section 148 orders for those continuing in active service.
Example 3A. Commuting Pension for Lump Sum at Retirement

At retirement the member in example 3 may wish to commute part of his pension in order to provide a lump sum (if the scheme rules allow this). The maximum lump sum will depend on whether or not the member has pre 17 March 1987 continued rights.

For a member without continued rights

<table>
<thead>
<tr>
<th>Pension Type</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Maximum pension at age 60 without debit</td>
<td>£24,000 a year</td>
</tr>
<tr>
<td>Maximum lump sum (= 2.25 x £24,000)</td>
<td>£54,000</td>
</tr>
<tr>
<td>If maximum lump sum taken, then maximum residual pension using divisor 12 (see paragraph 7.2) is</td>
<td>£19,500 a year</td>
</tr>
<tr>
<td>(= £24,000 – (£54,000 / 12))</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Pension Type</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Maximum pension at age 60 with debit</td>
<td>£18,000 a year</td>
</tr>
<tr>
<td>Maximum lump sum (= 2.25 x £18,000)</td>
<td>£40,500</td>
</tr>
<tr>
<td>If maximum lump sum taken, then maximum residual pension using divisor 12 (see paragraph 7.2) is</td>
<td>£14,625 a year</td>
</tr>
<tr>
<td>(= £18,000 – (£40,500 / 12))</td>
<td></td>
</tr>
</tbody>
</table>

For a member with pre 17 March 1987 continued rights

<table>
<thead>
<tr>
<th>Pension Type</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Maximum lump sum without debit (= 1.5 x £48,000)</td>
<td>£72,000</td>
</tr>
<tr>
<td>Maximum residual pension if maximum lump sum taken without debit (= £24,000 – (£72,000 / 12)), assuming the scheme has adopted a 12:1 commutation factor for all members.</td>
<td>£18,000 a year</td>
</tr>
</tbody>
</table>

Where the pre 17 March 1987 continued rights member has a debit, the maximum lump sum can be calculated on the better of two bases

**Approach one:**

<table>
<thead>
<tr>
<th>Calculation</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Maximum lump sum (= (1.5 x £48,000) – (2.25 x £6,000))</td>
<td>£58,500</td>
</tr>
<tr>
<td>and maximum pension if maximum lump sum is taken is (= £18,000 – (£58,500 / 12))</td>
<td>£13,125 a year</td>
</tr>
</tbody>
</table>

**Approach two:**

<table>
<thead>
<tr>
<th>Calculation</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Maximum lump sum (= 2.25 x £18,000)</td>
<td>£40,500</td>
</tr>
<tr>
<td>And maximum pension if maximum lump sum is taken is, as before, (= £18,000 – (£40,500 / 12))</td>
<td>£14,625 a year</td>
</tr>
</tbody>
</table>
Example 3B. Death of Active Member with Pension Debit

A13.16

The member (now earning £39,000 a year) dies at age 55, with 25 years’ service. If the scheme pays a lump sum of 4 times salary on death in service, this would be paid as (= 4 x £39,000) £156,000 with no reduction arising from the pension debit.

If the pension scheme member has remarried or is otherwise eligible for a surviving dependant’s pension: assuming that the scheme pays a spouse’s pension of 2/3 of the pension that the member would have received if he had retired at the date of death, based on actual service and salary (ignore anti-franking in this case) - the gross spouse’s pension is (= £39,000 x 25 / 60 x 2/3) £10,833 a year

Using the same rules for calculating the amount of the pension debit as for the deferred pensioner member in example 2, gives a debit of (= £4,000 x 1.0415 x 2/3) £3,260 a year

And thus a net pension for the widow of (= £10,833 – £3,260) £7,573 a year

Any benefits to other dependants (e.g. to children) should also be reduced by the debit in the appropriate proportion.

Example 3C. Active Member Choosing to Postpone Retirement Until After Scheme Normal Retirement Date

A13.17

Assume the member decides to remain at work until age 65. Assume further that the scheme allows service beyond normal retirement date to count as pensionable and to base the final pension on salary at eventual retirement.

At age 65 the member’s salary is £60,000 and he now has 35 years’ service, the gross scheme pension will be £35,000 a year

Allowing for increments on the pension debit from age 60 as if it were a deferred pension (say 10% a year) as well as the increases that it would have had if it been in payment (averaging 3.5% a year) gives a pension debit of (= £4,000 x 1.04115 x 1.0355 x (1 + 5 x 0.10)) £10,689 a year

Giving a net pension from age 65 of (= £35,000 – £10,689) £24,311 a year

If the scheme adopted the more usual approach of ceasing pension accrual at scheme normal pension age and enhancing the pension until it came into payment as if it were a deferred pension, then this example would look just like the deferred pensioner postponing retirement at example 2C.
Example 3D. Active member taking voluntary early retirement

A13.18 Assume that at 55, when the member has 25 years’ service and a salary of £39,000 a year, he wishes to take voluntary early retirement.

Formally the member leaves with a deferred benefit (short service benefit) payable from scheme normal retirement date, 60, of (= £39,000 x 25 / 60) £16,250 a year

The pension debit revalued until age 55 is (= £4,000 x 1.0415) £4,890 a year

The scheme in fact applies early retirement factors to this pension amount to allow for early payment. These factors are constructed so that the provisions of regulation 8 of the Occupational Pension Schemes (Preservation of Benefit) Regulations 1991 are complied with – i.e. ensuring that the value of the immediate early retirement benefit exceeds the value of the short service benefit/deferred pension. In this case assume that the factor is a 4% reduction for each year before scheme normal pension age. In addition a check may be needed to ensure that the GMP is covered at GMP payment age, which may lead to early retirement not being an option at some ages (other than this anti-franking is disapplied in the case of such early retirements).

Hence the pension that is put into payment at age 55 is
(= £16,250 x (1 – (5 x 0.04))) £13,000 a year

The pension debit, which is a “negative deferred pension”, should be reduced in the same proportion, i.e. to (= £4,890 x (1 – (5 x 0.04))) £3,912 a year

Thus the net early retirement pension is (= £13,000 – £3,912) £9,088 a year
Example 3E. Active Member Awarded Pension Early on Ill-health/Incapacity

A13.19
Benefits on ill-health retirement are generally at the discretion of the scheme trustees. In the example below the trustees have decided that the pension debit is to be applied with no reduction for early payment as would apply in the case of a voluntary early retirement (see example 3D above). Where the trustees of the scheme felt that applying an unreduced pension debit in such cases resulted in the member experiencing a debit of a considerably higher value than that intended, they may conclude that the appropriate course of action would be to reduce the debit. This might apply particularly to ill-health retirements at young ages where there was no impairment of life expectation. Trustees may consider that the maximum reduction in the pension debit should ideally be no more than the reduction that would be applied in the case of a voluntary early retirement at the same age.

Assume that at 55, when the member has 25 years’ service and a salary of £39,000 a year, the member has to take early retirement on ill-health grounds. The scheme provides a pension based on actual service and salary.

Hence the gross ill-health retirement pension from age 55 is
\[ \text{£39,000 \times 25 / 60} \]
£16,250 a year

The scheme member's pension debit on ill-health retirement should be
\[ \text{£4,000 \times 1.0415} \]
£4,890 a year

And the net ill-health retirement pension after allowing for the debit is
\[ \text{£16,250 - £4,890} \]
£11,360 a year

The same pension debit could apply where the scheme chooses to pay a higher ill-health retirement pension based, say, on full potential service to scheme normal retirement date, with the same flexibility for the debit as described above.
Example 3F. Active member subsequently becomes deferred pensioner member

A13.20
Assume that at 55, when the member has 25 years’ service and a salary of £39,000 a year, he leaves service with a deferred pension (short service benefit) payable from scheme normal retirement date, 60.

The deferred benefit payable from scheme normal retirement date, 60, is (£39,000 x 25 / 60) £16,250 a year

The pension debit, which is treated as a negative deferred pension, is (£4,000 x 1.0415) £4,890 a year

Both the actual gross deferred pension and the pension debit are revalued using rules for deferred pensions until age 60.

At age 60
The gross pension is now (£16,250 x 1.0415) £19,939 a year
The pension debit is (£4,890 x 1.0415) £6,000 a year

Note that the pension debit is the same as if the member had been an active member until age 60, or indeed had been a deferred pensioner member for the whole period for 50 to 60

Thus the net early retirement pension is (£19,939 – £6,000) £13,939 a year

This ignores the effect of anti-franking which will apply at 65 if the member is male (at 60, scheme normal retirement age, if the member is female).

In order to avoid any problems with the GMP element of the debit growing disproportionately compared with the gross GMP, trustees might decide to revalue the GMP element of the debit in line with section 148 (Social Security Administration Act 1992) orders while the member remains in active service and by the same fixed rate as the gross GMP in subsequent deferment (i.e. based on the date of leaving contracted-out employment). Although this may well not be the practice that schemes follow for deferred pensions (and in most cases the pension debit is treated as a negative deferred pension) trustees might conclude that it should be broadly consistent with the valuation of the pension debit.

For consideration of further contingencies following leaving service, see example 2.
Example 4. Pension Debit for Active Member of a Money-purchase Scheme

A13.21
A 40-year-old male active member of a defined contribution scheme has a fund of £80,000. The scheme has a normal retirement date of 60. His salary is £30,000 a year and he has 10 years’ service. For simplicity, any retained benefits and the permitted maximum are ignored. The pension target is taken as £20,000 a year (2/3rds of £30,000 a year). The member is subject to a pension debit of 50%, which leads directly to a reduction of £40,000 in the value of the fund.

At age 40
Total fund at divorce £80,000
Pension debit (transferred to his (ex-)wife for her to use to provide a pension in a form largely of her own choosing) £40,000
Notional deferred pension equivalent of pension debit (= £40,000 / 6.405), £6,245 a year
where 6.405 is Factor [5] (see paragraph a8a.6.7 of Appendix VIII or paragraph A9.11 of Appendix IX) for a male aged 40

At scheme normal retirement date (60)
Salary, say £80,000 a year
Service 30 years

Thus maximum gross pension at normal retirement date (= £80,000 x 2/3) £53,333 a year
The notional deferred pension equivalent of the pension debit established at the date of divorce, £6,245, is revalued between the date of divorce and the member’s normal retirement date by the rate of statutory revaluation that applies for a deferred, non-GMP, defined benefit - for the purpose of this example only, the rate is 4.1% a year compound.
Pension debit for deduction from maximum (= £6,245 x 1.04120) £13,949 a year
Net maximum pension that could be put into payment (= £53,333 – £13,949) £39,384 a year

Example 4A. Commuting Pension for Lump Sum at Retirement

A13.22
The same principles apply here as in the example for defined benefits schemes at example 3A – i.e. the maximum lump sum is effectively reduced by 2.25 x the (revalued) pension debit.
Example 4B. Death of Active Member with a Pension Debit

A13.23
In some cases the scheme will pay a death-in-service lump sum and pensions to *dependants* (if any) based on salary and service at the time of the member’s death. In this case, as with the corresponding example for members of defined benefits schemes, a death-in-service lump sum will be unaffected by the *pension debit*, but the maximum *dependants’* pensions should take account of the *pension debit* revalued between the date of divorce and the date of the member’s death.

Example 4C. Active Member Choosing to Postpone Retirement until After Scheme Normal Retirement Date

A13.24
Assume the member decides to remain at work until age 65. Assume further that the scheme allows service beyond *normal retirement date* to count as pensionable and to base the final pension on salary at eventual retirement.

The maximum permissible pension can be calculated on one of two bases. The effect of the *pension debit* on the maximum permissible pension must be consistent with the approach used for the gross maximum benefit. (Some members of pension schemes may be restricted as to which of the two approaches can apply to them – see, for example, paragraph 7.45.)

Approach 1 – late retirement factor applied to pension as at scheme *normal retirement date*

Suppose a factor of 1.42 is used by the scheme to increase the scheme pension at *normal retirement date* to allow for late retirement

The maximum scheme pension would be (= £53,333 x 1.42) £75,733 a year
The *pension debit* would be (= £13,949 x 1.42) £19,807 a year
And hence the maximum pension net of debit would be

(= £75,733 – £19,807) £55,926 a year

Approach 2 – recalculate the maximum based on salary (and service) at eventual retirement

At age 65 the member’s salary is £100,000, say, so the maximum gross scheme pension will be (= £100,000 x 2/3) £66,667 a year
The *pension debit* to be taken into account should be that from age 60 increased in line with statutory revaluation (= £13,949 x 1.0415) £17,053 a year
Giving a net pension from age 65 of (= £66,667 – £17,053) £49,614 a year
Example 4D. Active member taking voluntary early retirement

A13.25
Assume that at 50, when the member has 20 years’ service and a salary of £50,000 a year, he chooses to take early retirement voluntarily.

The maximum gross retirement pension from age 50 is (£50,000 x 2/3) £33,333 a year

The pension debit as it affects the maximum pension should be (£6,245 x 1.041^{10} x (1 – 0.065)^{10}) £4,766 a year

Note that in calculating the maximum pension the pension debit is brought into play with an actuarial reduction as if it were a pension paid before normal retirement age in a defined-benefit scheme.

And the net maximum pension after allowing for the debit is (£33,333 – £4,766) £28,567 a year

Money purchase schemes would not generally have cause to use early retirement factors. So in the circumstances the factor of 0.065 (compound) should be used to calculate the pension debit for the purposes of determining the maximum benefits.

Example 4E. Active Member Awarded Pension Early on Ill-health/Incapacity

A13.26
Assume that at 50, when the member has 20 years’ service and a salary of £50,000 a year, he has to take early retirement on ill-health grounds. The same approach is used here as in voluntary early retirement, with the same 6.5% a year compound reductions factors coming into play.

The maximum gross ill-health retirement pension from age 50 is (£50,000 x 2/3) £33,333 a year

The pension debit as it affects the maximum pension should be (£6,245 x 1.041^{10} x (1 – 0.065)^{10}) £4,766 a year

Note, it is appropriate to treat the person retiring early on ill-health no less favourably than the person retiring early voluntarily, with the pension debit reduced for early payment. For this reason the reduction in the pension debit should be the same reduction that would be applied in the case of a voluntary early retirement at the same age.

And the net maximum pension after allowing for the debit is (£33,333 – £4,766) £28,567 a year

Example 4F. Active member leaving pensionable service

A13.27
Assume at age 50, when the member has completed 20 years service and has a salary of £50,000 a year, he leaves pensionable service.

The maximum gross deferred retirement pension is £22,222 (£50,000 x 2/3 x 20/30)

The debit as it affects the maximum pension should be £9,333 (£6,245 x 1.041^{10})

If in the above example, the member subsequently took benefits early at, say, age 55, the maximum immediate benefit would be based on the maximum net deferred pension for an early leaver as appropriately increased during the period of deferment. Since the pension debit has already been reflected in the earlier calculation of maximum benefits, it would not be revisited at this later stage.

Example 4G. Pension Debit for a Pensioner Member of a Money-purchase Scheme

A13.28
For pensioner members, the principles of the application of a pension debit are similar to those for
pensioner members of defined benefit schemes, and many aspects of examples 1 and 1A are relevant.

**Example 5. Transfer of Pension Rights from Defined Benefit or Money Purchase Schemes for Members with a Pension Debit**

A13.29 Where a pension debit must be taken into account in relation to a member’s benefits (ie the administrative easement in paragraph 7.7 does not apply) and those benefits are transferred to:

- another tax approved occupational pension scheme of the same employer, an associated employer, an employer where continuous service applies, or a non-associated employer
- a personal pension scheme, or
- a buy-out contract

details of the pension debit applied to the member’s transferred benefits must be passed to the receiving scheme or provider to ensure that the necessary restrictions on the member’s total maximum benefits are maintained in the receiving scheme.

A13.30 Details of the pension debit do not have to accompany the transfer when it is made to a simplified defined contribution scheme.

A13.31 The details of the pension debit that must be passed to the receiving scheme or provider is a figure representing the notional deferred pension equivalent of the pension debit which has been appropriately revalued between the date of the pension sharing order and the date of the transfer. The receiving scheme or provider must continue to revalue the pension debit amount from the date of receipt (of the transfer payment) until:

- the member takes benefits from the receiving scheme
- the member transfers benefits to a subsequent scheme - details of the further revalued pension debit must accompany that transfer if the transfer is not made to simplified defined contribution scheme, or
- the death of the member before taking or transferring benefits from the receiving scheme.

A13.32 Where the receiving scheme is a scheme of the same or associated employer or when continuous service is granted in the receiving scheme, the pension debit is an aggregable benefit in relation to the maximum total benefits that can be paid to the member from the receiving scheme - the maximum total benefits that can be paid to the member had the pension sharing order not occurred is reduced by the amount of the (revalued) pension debit.

A13.33 If the receiving scheme is a scheme of a non-associated employer or is one where continuous service is not granted, the pension debit is treated as a retained benefit, together with the benefits payable from the actual transfer payment, for the purpose of the maximum total benefits payable to the member from the receiving scheme.

A13.34 In example 4, the active member left service at age 50 and immediately transferred benefits to another employer’s scheme. Benefits were taken at the receiving scheme’s normal retirement date, 60. The receiving scheme might have held the transfer on a money purchase basis (see paragraph 10.27) or the transfer might have been converted into added years (see paragraph 10.28).

A13.35 The pension debit figure accompanying the transfer is £9,333 a year (= £6,245 x 1.041\(^10\)). The notional deferred pension equivalent of the pension debit established at the date of divorce, £6,245, is revalued between the date of divorce and the transfer by the rate of statutory revaluation
that applies for a deferred, non-GMP, defined benefit - for the purpose of this example only, the rate is 4.1% a year compound.

A13.36 The revalued pension debit (£9,333) is an aggregable benefit for the purpose of the maximum total benefit calculation at the time of leaving the transferring scheme and the same figure is also used for the purpose of a lump sum certificate that might need to accompany the transfer.

The pension debit at the member’s normal retirement date in the receiving scheme is £13,949 a year (= £9,333 x 1.0410). The pension debit figure accompanying the transfer payment is revalued between the date of the transfer and the normal retirement date in the receiving scheme by the rate of statutory revaluation that applies for a deferred, non-GMP, defined benefit - for the purpose of this example only, the rate is 4.1% a year compound.

A13.37 The revalued pension debit (£13,949) must be taken into account, together with the benefits from the transfer payment, as a retained benefit for the purpose of calculating the maximum total benefits payable from the receiving scheme.

A13.38 A pension debit accompanying a transfer from a defined benefit scheme would follow the same principles set out above. The revaluation rate applied to the pension debit might need adjustment in relation to any GMP element reflected in the pension debit.
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