Stakeholder pension schemes: The current state of play

Received: (in revised form): 24th July, 2000

John Wilson

is a Research Consultant for HSBC Actuaries and Consultants Limited. He has 15 years' experience in the pensions industry, with consultancies and life offices, and has always worked in legal, documents and technical departments. He is an Associate of the Chartered Insurance Institute and an Associate of the Pensions Management Institute. He has written a number of articles for various publications and recently completed a series of stakeholder breakfast seminars, which were held all over the UK. In his 'spare time', he is studying for a law degree with the Open University and the College of Law.

Abstract This paper is a detailed report on stakeholder pension schemes, taking into account all authoritative material (ie, government material) which has been issued so far. In addition to setting out all the stakeholder requirements, including the new integrated tax regime, emphasis has been placed on the access obligations applying to employers. Essentially, this is a guide which should benefit both advisers and their corporate clients, by ensuring they understand fully what stakeholder is and what it may mean for them.

Keywords: *stakeholder pensions; minimum standards; employer access; advice; governance; tax*

Introduction

In December 1998, the Secretary of State for Social Security issued a Green Paper entitled 'A new contract for welfare: Partnership in Pensions'. Building on its welfare changes, this discussion document set out the Government's plans for radical reform of the whole pensions system. At the heart of these reforms are 'stakeholder pensions' — defined contribution schemes that are analogous to personal pensions, but which meet the specific conditions for stakeholder.

The principal target audience for stakeholder pensions is 'moderate earners' (those on about £10,000–£20,000 per annum), who cannot join occupational schemes and for whom personal pensions can be unsuitable. However, stakeholder pensions will also benefit those on higher earnings and certain members of

occupational schemes who wish to make additional provision for their retirement.

The proposals for stakeholder pension schemes have come a long way since the publication of the pensions Green Paper at the end of 1998. Defined in primary legislation as a pension scheme that meets certain conditions, the stakeholder 'bones' have recently been fleshed out by final regulations. These contain a number of changes from the draft regulations, which were issued earlier this year after six stakeholder consultation briefs, a DSS Press Release and draft Finance Bill clauses.

Consultation on stakeholder pension schemes began in earnest with the publication of Consultation Brief No.1 — 'Minimum Standards' — on 2nd June, 1999. This document put forward certain basic criteria for stakeholder pensions, covering charges, contributions,

John Wilson
(HSBC Actuaries &
Consultants Ltd, 15 Logie
Mill, Edinburgh EH7 4HG.

Tel: 0131 456 6850; Fax:
0131 456 6898)

investment and information. These minimum standards will be compulsory, unlike the CAT (cost, access and terms) standards under ISAs.

The inaugural Consultation Brief was followed, on 29th June, by Consultation Brief No.2 — 'Employer Access'. From October 2001, all employers not covered by one of the stakeholder exemptions will have to facilitate access to stakeholder pension schemes and offer a payroll deduction facility. There will be no requirement for employer contributions, but this does not mean that there will be no 'costs' for employers. Consultation Brief No.3 — 'Clearing Arrangements' — was, largely, complementary to the Employer Access document.

Consultation Brief No. 4, 'Regulation, Advice and Information', was published on 2nd August, and set out the proposed arrangements for regulating stakeholder pension schemes. Broadly, stakeholder pensions will be the subject of dual regulation by the Financial Services Authority (FSA) and the Occupational Pensions Regulatory Authority (Opra). The same document also considered arrangements for the provision of advice and information. The needs of most prospective stakeholder members are expected to be covered by the standard stakeholder charge, which must not exceed 1 per cent of any member's fund value each year.

The penultimate Consultation Brief (No.5), 'Governance', was also released on 2nd August and considered the governance requirements for stakeholder. Essentially, the Government would like to see most stakeholder pension schemes established under trust. Nevertheless, alternative governance structures will be possible and the Government, therefore, provided details of an outline model for 'secure stakeholder management'.

Consultation Brief No.6, 'The Tax

Regime', issued on 16th September, brought the Green Paper consultation process to a close. In addition to explaining the proposed tax system for stakeholder, which is not dissimilar to the present regime for personal pensions, this document contains a radical proposal for a new 'integrated tax regime', covering stakeholder, personal pensions and certain occupational money purchase schemes. Within this regime, an individual will be able to contribute to any number of defined contribution schemes, provided that the overall contribution limit is not exceeded.

The consultation process was followed up on 10th January by the first DSS press release of the new millennium. This announced the publication of key decisions on stakeholder pensions covering areas such as advice, exemptions from the stakeholder access requirements and governance. The press release also promised that further details of stakeholder pensions would be issued in early 2000.

Further details were duly issued on 22nd February, 2000, by the publication of details of the stakeholder tax regime and draft Finance Bill clauses. The accompanying Inland Revenue and DSS press releases confirmed that the tax arrangements for stakeholder will come into force on 6th April, 2001, by virtue of the Finance Bill 2000 and its attendant regulations.

Draft regulations, to clothe the dry bones of the Welfare Reform and Pensions Act 1999 (WRPA), were issued for consultation on 10th March, 2000. These regulations covered all the detailed aspects of stakeholder, apart from tax arrangements (see previous paragraph), and also made the necessary consequential amendments to the Pensions Schemes Act 1993 and the Pensions Act 1995.

The draft secondary legislation was, on

25th May, 2000, replaced by final stakeholder regulations, containing a number of important changes in the light of responses received to earlier proposals. These final regulations (the 'WRPA regulations') are reflected in this report.

Since the publication of the final regulations, there have been a number of important development:

- the Financial Services Authority has published a discussion paper on its approach to the regulation of the conduct of stakeholder pensions business (including 'Decision Trees' — see the 'Regulation, Advice and Information' section);
- the Inland Revenue has issued draft regulations, draft guidance and model documents for stakeholder pension schemes; and
- most importantly, the Government has announced that certain members of occupational schemes will be allowed concurrent membership of stakeholder pensions (see the 'Tax Regime' section).

This report is up-to-date as at July, 2000. At the time of writing, final tax regulations and full details of the requirements for 'non-trust' stakeholder pension schemes are still awaited.

Stakeholder — the framework

According to the WRPA, enacted on 11th November, 1999, a *stakeholder pension scheme* is a pension scheme which is registered with Opra as such and meets the conditions set out in the Act; viz:

- the scheme is established under trust or in such other way as regulations may provide (see Governance section);
- the provisions made by the

document(s) establishing the scheme comply with requirements to be set out in regulations (see Governance section);

- the scheme provides money purchase benefits (subject to prescribed exceptions) (see Minimum Standards section);
- the scheme complies with prescribed requirements regarding the use of contributions and assets to pay administrative expenses or commission (see Minimum Standards section);
- the scheme complies with statutory disclosure requirements (see Minimum Standards section);
- the scheme accepts any level of member contribution, subject to any prescribed minimum levels (see Minimum Standards section);
- the scheme accepts transfers; and
- the scheme is Revenue approved.

Opra will be responsible for keeping a register of stakeholder pension schemes (Opra is already the manager of the occupational and personal pension scheme registry, but stakeholder schemes will be separately identifiable from the main register). The WRPA contains some of the conditions for registration and provides for sanctions in the event of non-compliance. For trust-based stakeholder schemes, the trustees will be responsible for registration. For schemes not established under trust, registration is a matter for scheme managers.

The stakeholder pension scheme register will be available to anyone who wants to see it, although Opra may make a charge to cover their costs. Further, Opra may publish the register in any way they choose (eg, the intranet).

Employers must facilitate access to stakeholder pension schemes. Subject to any exemptions in regulations (see Employer Access section), an employer of *relevant employees* must:

- after consulting with his relevant employees (and their representatives), designate and provide details of a stakeholder scheme(s) that offers membership to all such employees. In addition, the stakeholder provider(s) should be allowed access to relevant employees to supply scheme information; and
- if asked, deduct and pass on to the designated scheme(s) any contributions from relevant employees.

Under the WRPA, *relevant employees* are all employees except those who are eligible for membership of the employer's occupational scheme(s) or those who earn less than the lower earnings limit. Further exemptions are set out in the WRPA regulations (see Employer Access section).

In designating a stakeholder scheme, an employer's responsibility extends only to the *duty of facilitation*. The WRPA provides that there is no need for employers to make any additional enquiries about the scheme or, in particular, investigate and monitor its performance. Nevertheless, the designated stakeholder scheme or schemes should always be chosen in good faith.

Opra is given statutory powers to ensure that employers are complying, or have complied with, their duty to facilitate access to stakeholder.

The WRPA extends certain sections of the Employment Rights Act 1996 to stakeholder schemes. This is intended to protect employee trustees from unfair dismissal and other detriment in the performance of their trustee duties. Such trustees are also entitled to reasonable paid time off for trustee training and performance of trustee duties.

Finally, the WRPA allows for the contracting-out rebates to stakeholder schemes to be set at different percentage levels to those applying to contracted-out

money purchase schemes and appropriate personal pension schemes. The DSS press release of 10th January, 2000 and the consultation paper accompanying the draft WRPA regulations state that, for 2001/2, the existing rebates for COMPS and APPS will apply to occupational stakeholder pension schemes and personal pension stakeholder pension schemes, respectively. A full review of rebates is to take place during summer 2000, before the introduction of the State Second Pension.

Stakeholder — minimum standards

Stakeholder pension schemes will be subject to compulsory minimum standards; this is different from ISAs, where the CAT (cost, access and terms) mark is optional for the provider. This is to ensure, *inter alia*, a level of standardisation across schemes, which will allow individuals to compare what is on offer more easily. Minimum standards will not, of course, offer a guarantee of performance or suitability.

One of the principal features that the Government believes stakeholder schemes should adopt is a simple and transparent charging structure. With this in mind, basic scheme charges should be levied only as an annual percentage of the value of the fund held by, or in respect of, each member. This percentage charge on fund value will mean some cross-subsidy from those with larger accounts to those with smaller funds.

In addition to the compulsory *basis* for charges, a *limit* on charges will also apply. The *maximum* charge, which has to cover all normal aspects of scheme membership and administration, is 1 per cent of fund per annum. Basic information and explanatory material will be included within this charge, but not individual financial advice.

Stakeholder schemes, like all other pension schemes, will be allowed to levy a separate charge to cover the expense of pensions earmarking orders and pension sharing costs. A separate charge will also be possible to cover, *inter alia*, the costs of providing an annuity or for operating income drawdown arrangements.

With regard to, for instance, individual financial advice, stakeholder schemes will not be allowed to provide any service other than the management of the scheme and its funds unless:

- such service is provided under a separate contract (or is provided free of charge, or within the deductions mentioned above); and
- the contract is in writing, setting out the amount of any charge and the terms on which it is to be paid.

It will not be possible for schemes, as a condition of membership, to require members to enter into separate contracts.

The basic principle in relation to charges is that, subject to foregoing exceptions and to court orders (eg, on divorce), a member's rights under a stakeholder scheme should only be used for the provision of benefits for and in respect of that member.

While charges are subject to a *maximum level*, contributions will be subject to a *minimum level*. No scheme will be able to require a minimum contribution of more than £20 (and contracting-out National Insurance Rebates must always be accepted). Schemes will also be prohibited from requiring any minimum frequency of payment.

Where a stakeholder pension scheme provides members with a choice of investments, there should also be a default investment option for members who do not want to make investment decisions.

The Individual Pensions Account (IPA),

a new tax 'wrapper' for pooled investments, could be used as the basis for investments in stakeholder schemes.

Whatever vehicle is chosen, a number of requirements relating to investments will have to be met.

Until very recently it was not clear whether stakeholder schemes would be able to offer with-profits arrangements. However, it is now known that with-profits investments will be permitted, provided such arrangements meet the conditions in the WIPA regulations.

The disclosure requirements for stakeholder will be analogous to those for other money purchase arrangements. Members must be provided with annual benefit statements and the WIPA regulations set out the required content of these statements in some detail. In addition, all stakeholder schemes will be subject to a requirement for an annual 'compliance' declaration, which will be available to scheme members on request.

In the event of a scheme losing its 'stakeholder status', it must be wound up, normally within 12 months, and benefits must be transferred to appropriate receiving arrangements.

Additional considerations for stakeholder schemes established under trust include the following:

- Schemes must not restrict membership by reference to a member's financial status, or the amount of contributions (above £20) to be made to the scheme, or the manner in which contributions are to be made (although contributions by means of cash or credit card can be declined)
- Schemes will, however, be able to restrict membership by reference to employment with a particular employer, employment in a particular trade or profession, or membership of a particular organisation

- At least one-third of the scheme trustees (or directors of a trustee company) must be independent from any person providing services to or managing the scheme
- A number of duties placed on trustees by the Pensions Act 1995 are extended to the trustees of stakeholder schemes — see Appendix I.

In relation to stakeholder schemes that are not established under trust, membership cannot be excluded by reference to any criterion (apart from the requirement for a minimum contribution of £20 and any prohibition on contributions by cash or credit card).

Other requirements for 'non-trust' stakeholder schemes include the following:

- A requirement for a written statement of investment principles.
- A requirement for managers to have regard to the need for diversification and suitability of investments, and to take proper advice (unless the managers are persons who may give such advice).
- A requirement to appoint a reporting accountant.

The above requirements largely mirror provisions which apply to trust-based stakeholder schemes.

Stakeholder — employer access

The WRPA provides, subject to certain exemptions, a duty on employers to facilitate access to stakeholder pension schemes. This duty will come into force on 8th October 2001, six months after the inception of stakeholder.

The 'duty of facilitation' (ie, access requirement) is comprised of three central components:

- selection/designation of a scheme (including consultation over the choice of scheme);
- provision of information; and
- a payroll deduction facility.

However, as indicated above, the access requirement applies only to *relevant employees*. These are employees with earnings at or above the lower earnings limit (LEL), who have at least three months' service and are not eligible for membership of the company scheme. An employee earns more than the LEL if their earnings have equalled or exceeded that amount in any week within the last three months.

The WRPA regulations provide additional exemptions from the access requirement:

- employers with fewer than five employees will be completely exempt. (If such an employer subsequently loses its exemption, it will have three months to comply with the access requirement); and
- employers who offer personal pensions will also be exempt provided that:
 - for every relevant employee aged 18 or over, the employer is contractually bound (or, for existing [pre-October 2001] arrangements, 'in effect' contractually bound) to contribute to a personal pension scheme and to provide a 'payroll deduction facility' for that scheme;
 - the personal pension does not impose 'exit charges or penalties' on employees who stop contributions or transfer out to another pension arrangement; and
 - employer contributions to the personal pension are made on each occasion on which the employee is paid basic pay (or at such longer interval as is agreed) and at a rate

of at least 3 per cent of the basic pay that is paid. Employer contributions may be subject to a 'matching' employee contribution of up to 3 per cent of basic pay (transitional provisions apply to arrangements set up before 8th October, 2001, — for these schemes, the employee contribution can be set at higher than 3 per cent provided that the employer at least matches it).

Even if all employees are eligible for the company scheme, a designated stakeholder scheme will still be needed (for employers with more than four employees) if the waiting period exceeds 12 months; the lower eligibility age exceeds 18 years; or the upper eligibility age is more than five years before normal retirement age. (The maximum waiting period for the personal pension exemption is three months, without any upper eligibility age.) Employees who are eligible for an occupational scheme, but who choose not to join or who join and then opt out of the scheme ('non-joiners' and 'opters-out') are not relevant employees and do not need to be provided with access to a stakeholder.

Employers that are not exempt from the access requirement will have to consult their workforce about the choice of stakeholder scheme. In this regard, employers are free to devise their own consultation process; eg, meetings or circulars. Ultimately, the final decision as to the particular stakeholder scheme that is selected rests with the employer.

It had been suggested that, by complying with its duty to facilitate, an employer might be seen to be endorsing the designated stakeholder scheme and accepting some responsibility for its performance. This concern was addressed by a late amendment to the WRPA. Designation is meant to be a neutral

process, but employers should still make it clear that they are not recommending the scheme.

Employers will have to provide sufficient details to enable employees to 'get in touch' with the designated scheme; ie, name and address of the scheme, and a contact number. In addition, stakeholder providers are to be allowed access to relevant employees in order to supply them with scheme information. Some providers may assist employers by providing information packs and even payroll software to comply with the requirement to deduct and pass on contributions.

Initially the stakeholder access requirement will apply only in respect of a single scheme. This does not mean that an employer cannot make arrangements with more than one scheme; eg, to accommodate different groups of staff.

Employers covered by the stakeholder access requirement must also offer a payroll deduction facility. This means that if an employee joins the designated scheme and asks to use the facility the employer must:

- deduct and record the amount requested from that employee's *post-tax* pay; and
- pass that contribution on to the designated scheme within a specified time.

The payroll deduction facility is *compulsory for employers*, but *voluntary for employees*. For instance, some employees may prefer to pay their contributions by direct debit or may find that the employer facility is not flexible enough for them. In any event, employers should ensure that they always have the individual employee's authority before making any deductions from earnings.

Employers will not have to *contribute* to the designated scheme, but may do so

if they wish. However, this does not mean that there will be no *costs* to employers; the requirements of *consultation, designation, information and payroll deduction* will all involve some expense.

It is presently the intention that employers will have to offer the payroll deduction facility for only the designated scheme (or, if the employer changes the designated scheme, for the current scheme and any previously designated scheme). If, at any time in the future, employers are compelled to make payroll deductions to all schemes, then it is likely that existing clearing arrangements will be utilised.

To limit the impact of the payroll deduction facility, the WRPA regulations restrict the frequency with which employees can amend their contribution rate to once every six months. However, whenever an employer does not comply with a request to vary contributions, the employee must be notified of this fact, be told the earliest date that the employer will comply, be advised that he/she can ask for deductions to cease at any time and be informed of the option to pay contributions direct to the stakeholder scheme. In the event that an employee requests payroll deductions to be cancelled, the employer will not have to offer them again for six months from the date of that request. However, the employer must notify the employee of this fact and of the option to pay contributions direct to the stakeholder scheme. Valid requests to vary contributions must be actioned no later than the pay period after that in which the request is made.

In line with current regulatory requirements, employers will be obliged to pay over employee contributions within 19 days of the end of the month of deduction. Trustees will report late payments to Opra. Notwithstanding the

regulatory requirements, employers may have to shorten this timescale if they are to avoid complaints of maladministration being made to the Pensions Ombudsman. For instance, an employer with one designated scheme should probably pay over contributions within five or six days of deduction.

Finally, employers must provide employees using payroll deduction facility for the first time (or varying contributions for the first time) with a notice as to how the facility operates. This notice must be provided within two weeks of the request to make or vary contributions.

Stakeholder — regulation, advice and information

There will be a number of bodies with a role in the *regulation* of stakeholder pension schemes: the Inland Revenue Pension Schemes Office; the Occupational Pensions Regulatory Authority (Opra); the Financial Services Authority (FSA); and, for trust-based schemes, the Pensions Ombudsman.

The two main regulators will be the FSA, which will be responsible for the marketing and selling of stakeholder pension schemes, and Opra, which will supervise their registration and operation. Regulatory arrangements will, to a degree, depend on whether a scheme is established under trust or any 'alternative governance structure'.

The *advice and information* proposals for stakeholder have been the subject of considerable debate. While the design of stakeholder pensions is intended to make advice simpler, its provision and the provision of information are somewhat constrained by the limit of 1 per cent on charges.

Correlatively, potential members of stakeholder pension schemes will, depending on their circumstances,

require different levels of service. Some will need only varying degrees of information; while others may seek much more individual, personal advice.

The Government's wish, expounded in following paragraphs, is to achieve a balance between costs and individual needs. Information and explanatory material will be available within the standard stakeholder charge, but individual financial advice may be subject to an additional cost.

As stakeholder pensions will, under financial services legislation, be 'investments', some information must be provided as of right: 'key features'; projections; and some generic advice. The Government envisages prospective members being supplied with an 'information pack', containing the mandatory information and details of other scheme benefits and conditions. The pack might also contain a *decision tree* — a tool designed to help guide people through the issues they should consider when they are deciding whether to join a particular stakeholder pension scheme.

In the event of prospective members needing further guidance or information, the Government expects stakeholder schemes to provide this (again, within the overall charge) in a number of ways:

- workplace meetings, organised under the terms of the employer access requirement;
- through telephone helplines; and/or
- interactive computer software.

For those that require individual financial advice, there will be no requirement to offer this within the 1 per cent charge (although some schemes may choose to do so). Schemes may, instead, levy an additional charge for such advice (subject to the requirements mentioned in the minimum standards section).

Trustees of stakeholder pension schemes are, in most cases, expected to appoint agents to promote and market their scheme. In consequence, there will be no need for them to be authorised to give investment advice.

As regards employers, provided that they do no more than discharge their duty of facilitation, there will be no infringement of financial services rules. There is also some scope for employers to provide extra information/general advice to employees. Guidance will be made available for employers wanting to offer this service.

As with personal pensions, there will be a 14-day 'cooling off' period for stakeholder pensions.

Stakeholder — governance

The Government wants stakeholder pension schemes to have a governance structure which ensures that schemes are run in the interests of members. With this in mind, they expect most schemes to be established under trust.

However, unlike most personal pensions, trust-based stakeholder schemes will not tie the trustees to a particular provider. Subject to any contracts they may enter into, trustees will be able to 'hire and fire' investment managers and providers of administration services whenever they decide it is in the interests of members to do so.

It has been suggested that it may prove difficult to find individuals willing to act as trustees for stakeholder schemes. The Government's view is that, at least initially, trustees will be provided by those involved in the development of schemes. While there will be no requirements for member-nominated or professional trustees, the Government does expect at least one-third of the trustee board to be independent.

Assuming trustees can be found, they

should be aware that, ultimately, they may be financially liable for the operation of the scheme. They will, however, be able to effect indemnity insurance and meet the premium from the standard stakeholder charge.

Other requirements for the governance of trust-based stakeholder pension schemes are set out in the Minimum Standards section. Many of these provisions will have to be incorporated into trust deeds and rules.

Notwithstanding the provisions for trust-based schemes, the Government recognises that the trust is not a panacea and the WRPAs therefore leaves the door open to the possibility of *alternative governance structures*.

Respondents to the stakeholder proposals identified a number of such alternatives and, building on these, the Government put forward, in Consultation Brief No.5, a blueprint for *secure stakeholder management*. A summary of this concept, which provides for stakeholder schemes to be established on a contractual basis, is provided at Appendix II.

The draft WRPAs regulations confirm that contract-based stakeholders will be permitted from April 2001, but details of the authorisation arrangements for these schemes are still awaited from the FSA.

Stakeholder — the tax regime

The tax regime for stakeholder pension schemes, while fundamentally analogous to the present system for personal pensions, is quite radical and could have important repercussions for all types of money purchase arrangement.

Departing from their original pensions Green Paper suggestion, which was to have a separate tax regime for stakeholder, the Government now intends that the arrangements for

stakeholder be extended (automatically) to personal pensions and (optionally) to money purchase occupational schemes.

In essence, the Government wants to create a new *simple integrated tax regime* for all defined contribution (DC) schemes. Within this regime, an individual will be able to contribute to any number of DC pensions provided that the overall contribution limit (see below) is not exceeded.

The Government's intentions, in more detail, are as follows:

- For contributions up to £3,600, there will be no link to earnings; nor will there be any lower eligibility age. Contributors will, however, have to pass a 'UK residency' test.
- Contributions above £3,600 will also be allowed, by reference to the existing age- and earnings-related personal pension limits. These can continue for up to five years after earnings have ceased, based on the highest level of earnings in the previous five years. After five years, contributions will be limited to £3,600 pa.
- All contributions from individuals (including the self-employed) are to be paid net of basic rate tax. The provider would then reclaim this tax from the Inland Revenue, with any higher rate relief being obtained through self-assessment.
- Contribution limits will apply to the total of all contributions from employers, individuals and the tax relief recovered on the individuals' contributions from the Inland Revenue. Contracted-out NIC rebates are, however, excluded.
- The above tax regime is to apply automatically to all personal pensions (but not retirement annuity contracts). Trustees of money purchase schemes may also 'opt in', but any election to

do so would be irrevocable. Before making such an election, trustees should consider the implications on contributions, benefits, life cover and overseas employees. Elections are subject to the approval of the Inland Revenue and can be made from 1st October, 2000, for an effective date from 6th April, 2001.

- As a corollary to this new flexibility, the existing carry forward provisions under personal pension schemes are to be abolished from April 2001. Carry back will be retained, but in amended form. From April 2001, a new arrangement will be introduced whereby a payment made before 31st January can, on election on or before it is paid, be treated as a payment for the previous tax year.
- Shares from an approved employee share scheme (ie, Save As You Earn Scheme or Approved Profit Sharing Scheme) can, with the contribution limits, be put into the pension 'pot' and attract tax relief.

The draft Finance Bill clauses provide that only 10 per cent of the pension contribution paid can be used for life assurance. This restriction will apply to all DC pensions where the contract for insurance is entered into after 5th April, 2001. Contracts made under existing rules before then will be subject to the present personal pension '5 per cent of earnings rule' (ie, up to 5 per cent of earnings can be used for life cover).

A related change is made to the rules for waiver of pension contributions insurance (ie, the insurance which pays pension premiums when the contributor is unable to due to ill-health). Where a policy is taken out after 5th April, 2001, waiver premium payments as part of the tax-exempt pension contribution will not be allowed. However, amounts paid out under any stand-alone waiver policy will

be treated like any other DC pension contribution. This change switches the 'timing' of tax relief — from the time of payment of the premium to the later time when the insurance payout is used to cover pension contributions. A waiver policy outside the scheme will be able to cover contingencies other than ill-health, such as unemployment.

The Government's original intention was that there would be no concurrent membership of occupational schemes and integrated DC schemes (including stakeholder), except where such membership was already permissible (eg, contracted-in company scheme with rebate-only personal pension). So, in respect of the same employment, it would not be possible to have a final salary scheme and a stakeholder. Nor would it be possible to have a money purchase scheme and a stakeholder, unless that scheme had opted into the integrated tax regime.

However, after extensive lobbying by the pensions industry, the Government finally backed down on the concurrency issue. From April 2001, concurrent membership of occupational schemes and stakeholder pensions will be allowed for non-controlling directors earning less than £30,000 per annum. Changes have been made to the Finance Bill to accommodate this relaxation and regulations will provide further detail (eg, how part year earnings are to be calculated).

According to the Government announcement, where concurrency applies, individuals will be able to pay maximum contributions to their company scheme and up to £3,600 to a stakeholder — on top. Earnings of less than £30,000 in a year will allow up to £3,600 to be paid into a stakeholder in any one of the next five years.

The concurrency relaxation also applies to personal pensions.

Other aspects of the proposed integrated regime are set out below:

- Members will not need to retire to draw their pensions; benefits can be taken at any time after age 50, or earlier in the event of incapacity.
- Phased vesting will be available but, unlike now, pension providers will be able to pay multiple annuities from a single arrangement. In other words, 'clustering' will not be necessary.
- Income drawdown will be available but, unless the rules for personal pensions are changed, an annuity will have to be purchased by age 75.
- The new regime will not apply to retirement annuity contracts (RACs). RACs will interact with integrated DC schemes in the same way as they currently interact with personal pensions — payments to a RAC will reduce the amounts payable to a DC pension scheme and payments to a DC pension scheme reduce the unused relief available under the RAC.

Conclusion

Stakeholder pensions are due to go 'live' in under a year's time. The pensions industry, employers and individuals all have a part to play in determining whether or not stakeholder will be a success. The Social Security Secretary, Alistair Darling, has already stated that the Government will if necessary, introduce compulsory contributions.

A number of providers in the industry have already started to develop their stakeholder contract and, in the meantime, numerous so-called 'stakeholder-friendly' personal pensions are available now. These arrangements comply with many of the minimum standards which will be compulsory for stakeholder pensions.

For employers, stakeholder is primarily a pension scheme access issue. However, it is only one of a number of pension scheme access issues (eg, the new part-time work regulations and the on going matter of whether excluding certain categories of employees from a pension arrangement could amount to indirect sex discrimination). Therefore, in the case of employers that do not already allow all employees into the company pension scheme, a relaxation of the scheme eligibility conditions may be the optimum solution. Where this is not viable, a stakeholder scheme may have to be nominated and employers should seek advice to ensure that they comply with their obligations and designate a scheme which fits with their needs.

Many individuals will still want advice before deciding whether to join a particular stakeholder pension scheme. In addition, information may be required in respect of transfers of previous pension rights and contracting-out of SERPS and the new State Second Pension. In relation to the Government's primary target group it is hard to envisage much of a take-up at the 'bottom end'. However, taking into account the advertising campaign which is planned for later this year, there may be a significant take-up by those on higher earnings.

As a result of the recent 'concurrency relaxation' (see the 'Tax Regime' section), individuals may also need advice when giving consideration to increasing their pension provision. For instance, should they pay additional voluntary contributions (AVCs) to their company scheme or make additional retirement provision via a stakeholder? One of the advantages of stakeholder pensions, compared to most AVC arrangements, is that tax-free cash can be taken from a stakeholder.

Will stakeholder pensions be a success?

The Government believes that those who can, should save for their retirement. They are committed to making stakeholder pension schemes work and, as stated above, have not yet ruled out compulsion.

Appendix I — Trust-based stakeholder pension schemes: Application of the Pensions Act 1995

(Extract from Consultation Brief No.5 — based on Schedule 1 of the Welfare Reform and Pensions Act 1999)

- Opra can remove or fine trustees in cases of breach of regulatory requirements, and can appoint trustees to the scheme in limited circumstances.
- Opra has the power to wind up schemes in certain circumstances.
- Opra can require trustees to publish statements by it about the scheme.
- Trustees cannot act as auditor of the scheme.
- Certain persons cannot be trustees.
- Trustees cannot be reimbursed out of scheme assets for fines for offences or Opra penalties.
- Trustees cannot exclude their liability for breach of their duties of care in performing investment functions.
- Trustees are responsible for selecting and monitoring an appropriate fund manager.
- Trustees must prepare a statement of investment principles. Trustees and their fund managers must consider the kind of investments to be held, the balance between them, the risk and the expected return.
- Trustees must appoint an auditor and (if they hold investments) a fund manager. They must not take professional advice except from an

adviser formally appointed by them. Resignations or removal of advisers must be accompanied by a statement of matters of significant interest to the members. (Stakeholder schemes do not require an actuary.)

- Trustees must make adequate information available to their professional advisers.
- Auditors are under ‘whistle-blowing’ obligations in relation to schemes for which they act.
- Trustees must keep monies received by them in a separate account or ensure they receive interest on monies held by someone else for them.
- Trustees must keep records of movement of monies and other things.
- Trustees must have an internal dispute-resolution procedure in place.
- Trustees may modify the scheme for certain purposes.
- Compensation may under certain circumstances be paid to the trustees by the Pensions Compensation Board in respect of scheme losses.
- Pension rights may not be assigned or forfeited except in limited circumstances.

Appendix II — Secure stakeholder management (or ‘contract schemes’): An outline model

(Extract from Consultation Brief No.5)

- The scheme is run by a stakeholder manager, which is a firm authorised by the Financial Services Authority (FSA). The role and functions of a stakeholder manager will be subject to specific FSA rules. A regulated activities order under s.20 of the Financial Services and Markets Bill will define the function of operating as a stakeholder manager as requiring authorisation.

- The activity of operating a stakeholder scheme will rank as investment business. The normal arrangements will apply for supervision, reporting, complaints, dispute resolution, discipline and enforcement.
 - The terms of business between the scheme and its members will be set out in a contract, which may be either standard or open to customisation for each member, or class of members.
 - The stakeholder scheme will be subject to similar minimum standards as trust-based stakeholder schemes. The manager will be responsible for registering the scheme with Opra and for ensuring compliance with the requirements for registration.
 - The stakeholder manager will be responsible for preparing a statement of investment principles, including the scheme's policy on socially responsible investment.
 - In addition to any investment options from which scheme members may choose, the stakeholder manager must set up default investment arrangements. In either case, FSA rules on suitability will apply.
 - The stakeholder manager is responsible for annual reports on the activities of the scheme as a whole, and for personal reports at least annually to each member on the value of their stakeholder savings, together with standard forecasts of future pension.
 - The manager must report payment delays to Opra (to the same standards as for trust-based stakeholder schemes).
 - Compensation under the financial services compensation scheme will be available on the standard terms in case of default of the stakeholder manager. In addition, the stakeholder manager must insure against the firm's default for risks above the compensation scheme limit and up to, say, £250,000 per scheme member.
 - There could be an optional advisory committee to represent the interests of scheme members.
- (See also Minimum Standards section).