**EXPLANATORY MEMORANDUM TO**

**THE PENSION SCHEMES (TRANSFERS, REORGANISATIONS AND WINDING UP) (TRANSITIONAL PROVISIONS) (AMENDMENT) ORDER 2010**

**2010 No. 529**

**1.** This explanatory memorandum has been prepared by Her Majesty's Revenue and Customs (HMRC) and is laid before the House of Commons by Command of Her Majesty.

This memorandum contains information for the Select Committee on Statutory Instruments.

## 2. Purpose of the instrument

2.1 This Order amends The Pension Schemes (Transfers, Reorganisations and Winding Up) (Transitional Provisions) Order 2006 (SI 2006 No 573) ("The Transfer and Winding Up Order"). The amendments allow some pension rights, built up under occupational pension schemes before 6 April 2006 and which are already protected by The Transfer and Winding Up Order, to be exempted from the tax charges that would normally apply if the rights were exercised after that date. The protection is maintained in certain circumstances when the pension rights are transferred from one pension scheme to another.

## 3. Matters of special interest to the Select Committee on Statutory Instruments

3.1 None.

## 4. Legislative Context

4.1 Part 4 of the Finance Act 2004 sets out the rules for the taxation of registered pension schemes that apply from 6 April 2006 ("A-Day"). In some cases, pension rights were acquired under the pre A-Day tax regimes which cannot ordinarily be exercised after A-Day without attracting tax charges. So Schedule 36 of the Finance Act 2004 contains transitional provisions (and section 283(2) allows the Treasury to make additional transitional provision through secondary legislation) exempting certain types of pre A-Day benefits from such charges.

4.2 The transitional provisions in and under Schedule 36 usually lapse where the protected retirement benefit rights are transferred on or after A-Day away from the pension scheme in which they originated. However The Transfer and Winding Up Order protects certain rights where the transfer results from a pension scheme being re-organised or wound up. The amendments to the Order extend this transitional protection to cover additional situations likely to occur when a pension scheme is re-organised or wound up.

4.3 This Order has retrospective effect back to A-Day. Section 282(A1) of the Finance Act 2004 contains the power to make secondary legislation with retrospective

effect if the provision does not increase any person's liability to tax. This Order does not increase any person's liability to tax as it extends transitional protection given by the Transfer and Winding Up Order.

## 5. Territorial Extent and Application

5.1 This instrument applies to all of the United Kingdom.

## 6. European Convention on Human Rights

6.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

## 7. Policy background

- ***What is being done and why***

7.1 Prior to A-Day, several different tax regimes existed, each applying to a different type of pension scheme. From A-Day, all pension schemes are now covered by a single tax regime with a common set of rules. Pension schemes approved under the pre A-Day pensions tax rules were automatically brought into the new tax regime as registered pension schemes and are subject to the new rules from A-Day – unless they specifically elected to opt out.

7.2 In most cases the post A-Day rules are more generous than what went before. But there are some circumstances where pension rights accumulated before A-Day are incompatible with the post A-Day tax rules and normally, where these come into payment after A-Day, they attract tax charges. Where this is seen to be unfair, transitional protection has been introduced through either primary or secondary legislation to provide exemption from these tax charges. Transitional protection recognises that it would be unfair to penalise or deny individuals' rights that had been legitimately acquired under an earlier tax regime.

7.3 In most cases, this transitional protection is lost when the protected pension rights are transferred away on or after A-Day from the pension scheme under which they originated. This is on the basis that the member normally has the choice of whether to keep the benefits within the protected scheme or transfer them elsewhere. But in some cases, primarily where an employer is restructuring its pension arrangements or a pension scheme is being wound up, the necessity to transfer benefits is imposed upon the member by the scheme.

7.4 The primary legislation covering transitional protection allows protection to continue for many such involuntary transfers. The Transfer and Winding Up Order provides that transitional protection is not lost where a member's pension rights are required to be transferred following a pension scheme re-organisation or wind up in certain circumstances that are not covered by the primary legislation. This protection covers the right to take benefits before the "normal minimum pension age" under the post A-Day regime of age 50 (age 55 from 6 April 2010) and/or the right to take a tax-

free retirement lump sum of more than the normal post A-Day limit of 25% of the total value of the retirement benefits coming into payment at that time.

7.5 Since this Order was laid in March 2006, further situations have emerged for which the Government considers the same transitional protection should also be available. These concern, in the main, situations where benefits are transferred from Scheme A to Scheme B with continuing protection and then as a result of the wind up of scheme B the member's retirement benefits are transferred into an annuity policy rather than a further pension scheme; or when the members' benefits are secured in the course of the scheme winding up by assigning an existing annuity policy to the member. This Order extends the original transitional protection to cover these additional circumstances.

7.6 HMRC have also taken the opportunity to address an additional matter concerning stand-alone lump sums (SALS) through this Order. Such lump sums are paid with no accompanying pension benefit and, whilst given transitional protection by 'The Taxation of Pension Schemes (Transitional Provisions) Order 2006' (SI 2006 No 572), this protection currently lapses when the pension scheme winds up and secures benefits by an annuity. So the opportunity has been taken to accommodate such SALS transfers within the transitional protection provided by this Order.

7.7 The amendments in this Order will take retrospective effect from 6 April 2006. They apply to lump sums paid and pensions that began to be paid on or after 6 April 2006, in respect of rights for which there was transitional protection at A-Day, but which were subject to further/onward transfers in cases of the reorganisation or winding up of a pension scheme.

- ***Consolidation***

7.8 There are no plans to consolidate the instrument that is being amended.

## 8. Consultation outcome

8.1 A draft of this Order was issued for public consultation on HMRC's website on 4 September 2007. Comments were requested by 5 October 2007 and 7 responses were received. Whilst welcoming the provisions in the draft Order a number of technical points were raised about the wording and how the Order was intended to operate. Many of these suggestions have been incorporated into the final version of the Order.

8.2 There were, in particular, detailed discussions with the Association of British Insurers (ABI) concerning how the Order could best cover all the types of annuity contract likely to receive transfers upon a reorganisation or winding up. This dialogue was necessary because it emerged from the consultation that there were significant differences in the nature of assigned annuity policies and purchased annuities and consequently how they were dealt with when a pension scheme was reorganised or wound up.

8.3 Because significant changes had been made to the draft Order since the original consultation, a further limited consultation exercise was carried out in

January 2010 to provide the previous respondents with the opportunity to comment on the revised draft. Four responses were received.

8.4 Respondents raised concerns that the Order does not extend transitional protection to transfers from one scheme into more than one annuity policy. This point was also raised and considered during the initial consultation exercise.

8.5 The policy intention in making this Order is to assist the vast majority of members of winding up schemes who will transfer into a single policy. The intention is to treat transfers into annuity policies in a similar way as transfers protected under the primary legislation, i.e. from one scheme to one other scheme.

8.6 Extending the scope of the Order to include transfers into more than one annuity policy would add significant complexity to this transitional provision, particularly surrounding the apportionment of protected lump sums. The Government does not think that the additional complexity this would impose justifies the benefits that a few individuals would receive.

## 9. Guidance

9.1 When the Order is made and laid, the final version and this Explanatory Memorandum will be published on HMRC's website. Details of the Order will also be set out in HMRC's on-line 'Registered Pension Schemes Manual'.

## 10. Impact

10.1 No impact on business, charities, voluntary bodies or public sector is foreseen.

10.2 An Impact Assessment has not been prepared for this instrument.

## 11. Regulating small business

11.1 The legislation applies to small businesses in the same way as it does to larger businesses. This Order extending protection from tax charges therefore benefits small business equally with larger businesses.

## 12. Monitoring & review

12.1 HMRC will continue to monitor the effectiveness of this Order as part of the normal course of Pension Schemes Services carrying out routine tax audits on individual schemes and will continue to be open, through our existing communications channels with the pensions industry, to discussion on difficulties with, or questions regarding, this Order.

## 13. Contact

Sarah Mee at HMRC (Tel: 0115 974 3013 or email: pensions.policy@hmrc.gsi.gov.uk) can answer any queries regarding the instrument.