

**PENSIONS: CONTRACTING OUT – SELF
INVESTED PERSONAL PENSIONS AND OTHER
CHANGES**

Consultation on Draft Regulations

**THE PERSONAL PENSION SCHEMES (APPROPRIATE
SCHEMES) (PROTECTED RIGHTS) (AMENDMENT)
REGULATIONS 2008**

December 2007

DWP Department for
Work and Pensions

CONTENTS

	Page No.
Consultation document	
Preface	1
Policy	4
The draft regulations	11

PREFACE

1. This consultation document seeks views on the enclosed draft regulations: The Personal Pension Schemes (Appropriate Schemes) (Protected Rights) (Amendment) Regulations 2008. It is on the Department's website at: <http://www.dwp.gov.uk/consultations/2007/>

Consultation Period

2. The Cabinet Office Code of Practice on Consultation advises that a minimum of 12 weeks is appropriate for public consultations, unless there are good reasons for a shorter period. In this case, the consultation period will be for 12 weeks, and will end on 29 February 2008.

How to respond to this consultation

3. Please send your response, **preferably by email**, to: contractingout@dwp.gsi.gov.uk or by post to:

Jane Bonner-Morgan
Department for Work and Pensions
3rd Floor
Adelphi
1-11 John Adam Street
LONDON WC2N 6HT

tel 020 7962 8411

4. When responding, please state whether you are doing so as an individual or representing the views of an organisation. If you are responding on behalf of a larger organisation, please make it clear who the organisation represents, and where applicable, how the views of members were assembled. We will acknowledge your response.

5. We have sent this consultation document to a large number of people and organisations who have already been involved in this work or who have expressed an interest. Please do share this document with, or tell us about, anyone you think will want to be involved in this consultation.

6. The information you send us may need to be passed to colleagues within the Department for Work & Pensions and published in a summary of responses received, and referred to in the published consultation report.

7. All information contained in your response, including personal information, may be subject to publication or disclosure if requested under the Freedom of Information Act 2000. By providing personal information for the purpose of the public

consultation exercise, it is understood that you consent to its disclosure and publication. If this is not the case, you should limit any personal information which is provided, or remove it completely. If you want the information in your response to the consultation to be kept confidential, you should explain why as part of your response, although we cannot guarantee to do this. We cannot guarantee confidentiality of electronic responses even if your IT system claims it automatically.

8. If you want to find out more about the general principles of Freedom of Information and how it is applied within DWP, please contact: Charles Cushing, Department for Work and Pensions, Adjudication and Constitutional Issues, Information Policy Division, Freedom of Information Unit, 1-11 John Adam Street, London WC2N 6HT (0207 962 8581, charles.cushing@dwpgsi.gov.uk or carol.smith14@dwpgsi.gov.uk)

9. More information about the Freedom of Information Act can be found on the website of the Department for Constitutional Affairs.

The consultation criteria

10. The consultation is being conducted in line with the Code of Practice on Consultation. The six consultation criteria are listed below, and the full version can be accessed at the Cabinet Office website.

- Consult widely throughout the process, allowing a minimum of 12 weeks for written consultation at least once during the development of the policy;
- Be clear about who may be affected, what questions are being asked, and the timescale for responses;
- Ensure that your consultation is clear, concise and widely accessible;
- Give feedback regarding the responses received and how the consultation process influenced the policy;
- Monitor your department's effectiveness at consultation, including through the use of a designated Consultation Co-ordinator; and
- Ensure your consultation follows better regulation best practice, including carrying out an Impact Assessment if appropriate.

11. We value your feedback on how well we consult. If you have any comments on the process of this consultation (as opposed to the issues raised) please contact our Consultation Coordinator: Roger Pugh, Department for Work and Pensions' Consultation Coordinator, Room 2A, Britannia House, 2 Ferensway, Hull HU2 8NF (01482 609571, roger.pugh@dwpgsi.gov.uk).

12. In particular, please tell us if you feel that the consultation does not satisfy these criteria. Please also make any suggestions as to how the process of consultation could be improved further.

13. If you have any requirements that we need to meet to enable you to comment, please let us know.

What will we do after the consultation?

14. A summary of responses will be published following the consultation. We will aim to publish this summary within three months of the consultation closing. The summary of responses will be available on the Department's website:
<http://www.dwp.gov.uk/consultations/2007/>

POLICY

Introduction

1. The Government is proposing to permit Self Invested Personal Pensions (SIPPs) to hold protected rights. This is something that is currently prohibited under DWP regulations. The change is planned for October 2008. In order to make the necessary changes, amendments are being made to *The Personal Pension Schemes (Appropriate Schemes) Regulations 1997 (SI 1997 No. 470)*. This change is in line with a more general shift towards lining up protected rights policy with tax law.
2. This consultation document also includes a proposal to make a minor amendment to contracting out legislation to remove the provision that permits a survivor's annuity to continue to be paid to any other person if the survivor dies during a five year guarantee period. This change will require an amendment to *The Personal and Occupational Pension Schemes (Protected Rights) Regulations 1996 (SI 1996 No. 1537)*.

Background

3. Contracted-out rights arise when an employee opts out of the State Second Pension. In return, that person receives a contracted-out rebate which is paid into a scheme approved to receive such rights. Where an individual is contracted-out through an Appropriate Personal Pension¹ (APP) these contracted-out rights are known as protected rights and are subject to certain rules.

SIPPs

4. Under current arrangements, SIPPs are prohibited from becoming an APP. This has been justified on the grounds that APPs include protected rights derived from the contracted-out rebate. The rebate calculation is based on the idea that it will generate a pension that is estimated to replace the State benefits foregone by contracting out. The view has been taken that protected rights should not be subject to the risk that can arise from self-investment especially as, until recently, the administration of SIPPs has been subject to low levels of regulation.
5. The legislation which currently prohibits SIPPs from holding protected rights is set out in regulations 2 and 3 of *The Personal Pension Schemes (Appropriate Schemes) Regulations 1997*. In particular regulation 2 sets out the forms of schemes which may be appropriate schemes and because of the investment requirements, the majority of SIPP schemes are excluded.

¹ The term used to describe a personal pension or stakeholder pension that can be used by its members to contract out of the State Second Pension.

6. The question of whether to permit SIPPs to hold protected rights is by no means a new one – it was considered as part of a consultation exercise on various contracting out changes made in 2005. At that time the Government considered the lack of a higher standard of prudential regulation as the major reason for not permitting SIPPs to hold protected rights. The Government response to the consultation stated that the position would be reviewed once the new Financial Services Authority (FSA) regulatory arrangements were agreed or in place.

7. In April 2007 the FSA implemented a new regulatory regime which introduced consistent regulatory treatment and protection for consumers across all types of personal pensions, including SIPPs. Particularly relevant is the fact that the FSA regulate the way that SIPPs are marketed and sold. The FSA have already emphasised that advisers must make sure that “advice given to transfer into a SIPP is suitable, reflects the customer’s needs, priorities and circumstances, and is not influenced by commission payments”. In the light of the new FSA regime the current rules on SIPPs are considered unduly restrictive.

8. We have also listened to the arguments from providers for a relaxation of rules on this issue and agree that SIPPs provide a useful option for some people. Our proposals would mean individuals would be able to hold all their rights in a SIPP if they wish (rather than having to find a separate plan for their protected rights). Our proposals would also put all SIPP providers on an equal commercial footing – currently the legislation permits a few insurance based SIPPs to hold protected rights whilst the majority cannot.

9. On a more general point, the Government has, in the Pensions Act 2007, legislated for the abolition of contracting out on a defined contribution basis. The implementation date is expected to be April 2012. The Pensions Act also removes many of the rules for past protected rights. However the Government is still considering whether the requirement for survivor’s benefits to be provided from protected rights should be retained. These wide ranging changes mean that the restrictions that prohibit protected rights from being held in a SIPP would, in any event, be removed when contracting out on a defined contribution basis is abolished.

10. The specific proposals in this consultation would, if taken forward, permit SIPPs to hold protected rights ahead of the more wide ranging changes to defined contribution contracting out. We propose the changes be introduced in October 2008, this will allow time for the FSA to consult on any rule changes they may need to make (see para 14).

Annuities

11. Where a member of a contracted-out defined contribution scheme dies before giving effect to his or her protected rights and is survived by a widow/widower/civil partner, the protected rights fund must be used by the survivor to either purchase an

annuity or, in the case of an appropriate personal pension, to provide payments under an interim arrangement.

12. Where protected rights are used to purchase an annuity and the survivor subsequently dies, *regulation 12(9) of The Personal and Occupational Pension Schemes (Protected Rights) Regulations 1996* makes provision for the annuity to continue to be paid to or for the benefit of a person or persons other than the survivor.

13. *Regulation 12(11)* sets out details of those to whom the annuity can be paid and allows the survivor to elect that where he or she dies, or remarries before pensionable age, the annuity can pass to his or her children and continue to be paid until the youngest reaches age 18. If, however, the children die or attain age 18 within 5 years of the date on which the annuity commenced, then it can continue to be paid to “*any one person*” for the remainder of the 5 years. From 6 April 2006 these provisions have been in conflict with the tax rules which prevent the annuity being guaranteed for a minimum number of years, or being to someone other than a dependant. The draft regulations therefore include a tidying up measure to align our legislation with HMRC tax law.

FSA regulation/consultation

14. The FSA currently require that, for personal pensions, a point of sale projection of future benefits is given. This includes a “contracting out comparison” which gives projections enabling the individual to compare the contracting out/ /contracting in position. When, following this consultation exercise, a final decision on SIPP and protected rights is taken, the FSA will consult on possible changes to their Conduct of Business rule book to take account of this.

Timing

15. We expect the changes to be introduced from October 2008.

Consultation questions

16. The approach we have taken in making the SIPP amendments is to remove regulations 2 and 3 of the Appropriate Scheme Regulations almost completely. Currently much that is in these regulations duplicates HMRC and FSA regulation on scheme registration and investment and we do not think this is necessary. We believe we can make these changes without impacting on other areas of policy but would be grateful if consultees could say if they think otherwise or can identify possible areas of conflict.

17. We consider that a full impact assessment of these changes is not necessary since permitting SIPP schemes to hold protected rights does not impose new

regulation, it simply gives those schemes the choice to apply for contracting out status if that is what they wish to do. Our view is that although there will be small administrative costs associated with applying for contracting out status and tracking protected rights this would be a commercial decision that SIPP schemes would take in the expectation of receiving new business and increasing profits as a result. We would be particularly interested in views on this, or on how the marketplace might be affected by the SIPP's change.

Commentary on the draft regulations

Regulation 1

18. A general provision, setting out in particular the date the regulations are to come into force.

Regulation 2

19. This regulation contains amendments to the Personal Pension Schemes (Appropriate Schemes) Regulations 1997 in respect of SIPPs.

20. Regulation 2(2) omits references in regulation 1 of the Appropriate Schemes regulations that are no longer necessary as a consequence of the main changes in this regulation (ie to regulations 2 and 3 of the AS regulations).

21. Regulation 2(3) amends regulations 2 of the Appropriate Schemes regulations to remove the provisions regarding the form of personal pension schemes which may be appropriate schemes. The condition that a scheme must be registered under s153 of the Finance Act 2004 will remain.

22. Regulation 2(4) amends regulation 3 of the Appropriate Schemes regulations to remove the provisions regarding who may establish an appropriate scheme.

23. Regulations 2(5)–(8) make further amendments that are consequential to the amendments of regulations 2 and 3 of the Appropriate Schemes regulations.

Regulation 3

24. This regulation repeals regulation 12(c) of the Personal and Occupational Pension Schemes (Protected Rights) Regulations 1996 so as to remove the provision allowing payment of the pension or annuity to continue in payment to any one person as specified.

Regulations 4 and 5

25. These regulations revoke amendments in the Personal Pension Schemes (Appropriate Schemes) (Amendments) Regulations 2006, which are superseded by the amendments now being made to regulations 1-3 of the Appropriate Schemes regulations.

List of those consulted:

Age Concern
Association of British Insurers
Association of Consulting Actuaries
Association of Independent Financial Advisers
Association of Member-Directed Pension Schemes
Association of Pension Lawyers
British Chambers of Commerce
Cabinet Office (Regulatory Impact Unit)
Confederation of British Industry
Consumers Association
DTI
EBS
Engineering Employers Federation
Equal Opportunities Commission
Fawcett Society
Federation of Small Businesses
Financial Services Authority
Government Actuaries Dept
Hewitt
HM Treasury
HMRC
HSBC
Institute and Faculty of Actuaries
Institute of Chartered Accountants
Institute of Chartered Accountants in Scotland
Institute of Directors
Law Society
Law Society of Scotland
Legal & General
Linklaters
Northern Ireland
Norwich Union
NAPF
National Consumers Council
Office of Fair Trading
TPAS
Pensions Management Institute
Pensions Ombudsman
Price Waterhouse Coopers
Prudential
Punter Southall
Scottish Equitable
Scottish Life
Scottish Executive
Scottish Widows

Society of Pension Consultants
Standard Life
The Pensions Regulator
Trades Union Congress
Watson Wyatt
Welsh Assembly

2008 No.

PENSIONS

The Personal and Occupational Pension Schemes (Appropriate Schemes) (Protected Rights) (Amendment) Regulations 2008

<i>Made</i> - - - -	***
<i>Laid before Parliament</i>	***
<i>Coming into force</i> - -	***

The Secretary of State for Work and Pensions makes the following Regulations in exercise of the powers conferred by sections 9(5)(a), 26, 28(5), 181(1) and 182(2) and (3) of the Pension Schemes Act 1993⁽²⁾.

In accordance with section 185(1) of that Act⁽³⁾ he has consulted such persons as he considers appropriate.

Citation and commencement

1. These Regulations may be cited as the Personal and Occupational Pension Schemes (Appropriate Schemes) (Protected Rights) (Amendment) Regulations 2008 and shall come into force on 1st October 2008.

Amendment of the Personal Pension Schemes (Appropriate Schemes) Regulations 1997

2.—(1) The Personal Pension Schemes (Appropriate Schemes) Regulations 1997⁽⁴⁾ shall be amended as follows.

(2) In regulation 1(2) (interpretation)⁽⁵⁾ omit the definitions of “deposit-taker”, “EEA state”, “Friendly Society”, “Home state regulator”, “open-ended investment company”, “recognised scheme”, “UCITS” and “unit trust scheme”.

(3) For regulation 2 (forms of schemes which may be appropriate schemes)⁽⁶⁾ substitute—

⁽²⁾ 1993 c. 48. Section 28(5) as amended by section 142(6) of the Pensions Act 1995 (c. 26) and section 284(5) of the Pensions Act 2004(c. 35). Section 181(1) is cited because of the meaning there given to “prescribed” and “regulations”.

⁽³⁾ Section 185(1) was amended by paragraph 46 of Schedule 3 and paragraph 80 of Schedule 5 to the Pensions Act 1995.

⁽⁴⁾ S.I. 1997/470; relevant amending instruments are S.I. 2001/943 and 3649 and 2006/147.

⁽⁵⁾ As amended by S.I. 2001/3649 and 2006/147.

⁽⁶⁾ As amended by S.I. 2001/943 and 3649 and 2006/147.

“2. A personal pension scheme can be an appropriate scheme only if it is a scheme which from 6th April 2006 is, or is treated as, registered under section 153 of the Finance Act 2004⁽⁷⁾ (registration of pension schemes).”.

(4) Omit regulation 3 (persons who and bodies which may establish schemes)⁽⁸⁾.

(5) Omit paragraph (1)(e) and (f) of regulation 4 (requirements in respect of an application for an appropriate scheme certificate).

(6) Omit paragraph (b)(iii) of regulation 6 (requirement to give the Commissioners for Her Majesty’s Revenue and Customs⁽⁹⁾ information)⁽¹⁰⁾.

(7) Omit regulation 18 (cancellation of membership of interest-bearing account-funded appropriate personal pension schemes).

(8) Omit Schedules 1 (kinds of unit trust scheme that may be an appropriate scheme)⁽¹¹⁾ and 2 (information to be included in notice).

Amendment of the Personal and Occupational Pension Schemes (Protected Rights) Regulations 1996

3. Omit paragraph (11)(c) of regulation 12 (death of member before effect given to his protected rights) of the Personal and Occupational Pension Schemes (Protected Rights) Regulations 1996⁽¹²⁾.

Revocations

4. The Personal Pension Schemes (Appropriate Schemes) (Amendment) Regulations 2006⁽¹³⁾ are revoked.

5. Regulation 4 (amendment of the Personal Pension Schemes (Appropriate Schemes) Regulations 1997) of the Occupational and Personal Pension Schemes (Perpetuities and Contracting-out) Amendment Regulations 2001⁽¹⁴⁾ is revoked.

Signed by authority of the Secretary of State for Work and Pensions.

Date

Name
Minister of State,
Department for Work and Pensions

⁽⁷⁾ 2004 c. 12.

⁽⁸⁾ As amended by S.I. 2001/3649 and 2006/147.

⁽⁹⁾ The functions of the Commissioners of Inland Revenue (“the former Commissioners”) were transferred to the Commissioners for Her Majesty’s Revenue and Customs by section 5 of the Commissioners for Revenue and Customs Act 2005 (c.11). See *also* section 50 of that Act in relation to the construction of references to the former Commissioners in other enactments.

⁽¹⁰⁾ See section 1(2) of, and Schedule 2 to, the Social Security Contributions (Transfer of Functions, etc.) Act 1999 (c. 2).

⁽¹¹⁾ As amended by S.I. 2001/3649.

⁽¹²⁾ S.I. 1996/1537, to which there are amendments not relevant to these Regulations.

⁽¹³⁾ S.I. 2006/147.

⁽¹⁴⁾ S.I. 2001/943.

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations amend the Personal Pension Schemes (Appropriate Schemes) Regulations 1997 (S.I. 1997/470) and the Personal and Occupational Pension Schemes (Protected Rights) Regulations 1996 (S.I. 1996/1537).

Regulation 2(3) and (4) amends regulations 2 and 3 of the Personal Pension Schemes (Appropriate Schemes) Regulations 1997 to remove provisions regarding the form and establishment of personal pension schemes which may be appropriate schemes.

Regulation 2(2) and (5) to (8) makes amendments consequential to the amendment of regulations 2 and 3 of the Personal Pension Schemes (Appropriate Schemes) Regulations 1997.

Regulation 3 amends regulation 12(11) of the Personal and Occupational Pension Schemes (Protected Rights) Regulations 1996 to remove the provision in paragraph (c) allowing payment of the pension or annuity to any one person as specified.

Regulations 4 and 5 make consequential revocations.

A full impact assessment has not been produced for this instrument as it has negligible impact on the costs of business, charities or the voluntary sector.