Stakeholder pensions

Stakeholder schemes were introduced by the Government to encourage people with moderate earnings to save for their retirement. They are intended to be cost-effective, flexible and accessible to all.

Unless you already have a pension scheme which all your employees are entitled to join, you will almost certainly have to arrange for them to have access to a stakeholder scheme.

This briefing explains what stakeholder schemes are and how they will affect you as an employer. It covers:

- Whether you are obliged to offer access to a stakeholder scheme.
- Which employees you must offer access to a scheme.
- What is involved.
- Where to get help.

1 The stakeholder picture

Stakeholder pensions are designed to provide a simple, low-cost pension arrangement.

1.1 Stakeholder schemes may be more **basic** than personal pensions.

- The choice of fund may be more restricted than with personal pensions.
- Advice without charge will be limited but you can choose to pay a separate fee for further advice.

1.2 They are normally **established by** investment and savings institutions (such as life assurance companies).

- Employers can offer their own schemes, managed by trustees, but only very large companies are likely to do this.

1.3 They can be offered directly to **individuals** or through employers.

- Most businesses with five or more employees have to designate at least one stakeholder pension scheme.
- If employees wish to contribute, the employer must offer to deduct their contributions from pay and pass them on to the provider.
- The employer does not have to make contributions to the employee's stakeholder pension, but can do so.
- Employees do not have to take out a stakeholder pension with the provider designated by the employer.

They can invest their contributions with another provider, in which case the employer need not become involved, or they can decline to take out a stakeholder pension scheme at all.

A business is not liable for the investment performance of the stakeholder pension scheme it designates.

1.4 Stakeholder pensions are designed to be **easy to understand**.

- They are money purchase arrangements, which means that the size of the eventual pension is not guaranteed.
  It will depend on the amount of money paid in, the investment performance of the fund, the level of charges deducted from the fund, how long you have to retirement and the level of annuity rates when the pension is paid.
- Pension providers offer various investment alternatives. For example, stakeholder pension members may be able to choose to invest in funds associated with specific geographic areas, or companies.
  But there must always be a 'default' option, for those who feel they do not have the time or expertise to make a choice about how their contributions are invested.

1.5 Stakeholder pensions are **flexible**.

- Individuals do not have to make regular contributions.
- Employers must allow members to stop, start or change the size of their contributions but some timing restrictions apply (see **2.3**).
- They can move their pensions from one provider to another without any penalty.
- They can contribute as little as £20.

If employees ask you to collect contributions in the form of deductions from salary (see **2.3**), it will usually be done monthly.

1.6 Stakeholder pension **costs** remain low.

- Annual management charges must not exceed 1.5 per cent (previously 1 per cent) of the value of the fund. Charges on stakeholder pensions set up before April 2005 are still capped at 1 per cent a year, and charges on newer arrangements must revert to 1 per cent (or less) after ten years.
- If individuals decide to move to another provider (for example, when they change jobs), the existing provider cannot impose any transfer charges or penalties.
- However, there may be extra charges for additional services eg where an employee needs advice on his or her pension position. If fees are charged, they must be provided for under separate contracts.

Employers need incur no direct costs in providing stakeholder pensions. But there will be hidden costs in the shape of extra paperwork, book-keeping and setting up systems to pass on employees' contributions. It may be possible to keep costs down (see **5**).

2 The employer's role

All employers (with certain exceptions, see **3**) are required by law to make stakeholder pensions available to their employees.

2.1 You should have a **designated** stakeholder pension scheme for relevant employees.

- Consult your staff about which scheme to choose. While you should consider their views, you are not obliged to act on them.

The limits on contributions

Though most people are entitled to pay into stakeholder pensions, contributions are limited by law because of the tax benefits available for pension schemes.

A **Tax favoured** contributions from earnings can be made by those who contribute to other pension schemes, providing they observe the new annual allowance (£235,000 in 2008/09) limiting all increases in the size of their funds.

- Contributions in excess of the annual allowance will be taxed at 40 per cent.

B Contributions can be made by people **earning little or nothing**. For example, employees on sabbatical or on additional maternity leave could keep making contributions, even if they were not being paid

- Contributions of up to £3,600 can be paid each year without evidence of earnings.

The rules on tax relief have recently been greatly simplified, with the introduction of the lifetime limit (initially set at £1.65 million) on the size of funds when benefits are taken and the annual limit (initially set at £235,000 in 2008/2009) on tax-favoured contributions.

➨Since 5th December 2005 civil partner employees must be treated in the same way as married employees. If a benefits package (such as pension survivor benefits) is available to an employee's spouse, it must also be available to an employee's civil partner.

A civil partner who is treated less favourably than a married person in similar circumstances will be able to bring a claim for discrimination on grounds of sexual

- Ensure that the designated scheme is registered with the Pensions Regulator (formerly Opra).

2.2 You must make your employees **aware** of the scheme you have designated, but you do not need to promote it actively.

- You must be prepared to pass information about the scheme to your employees, or to allow the provider to do so.
- Your provider should produce most of the marketing materials.
- You need some system for answering employees' questions but do not give employees individual advice.
- You can encourage staff to invest in a pension, but do not recommend one particular scheme.

2.3 You must **deduct the employee's contributions** from pay, if asked to do so, and forward them to the provider of the designated stakeholder scheme.

- The employee decides on the size of his or her contributions. He or she can now choose to put up to 100 per cent of their earnings into pension funds, and provided they are registered with HM Revenue & Customs, the whole amount will qualify for tax relief.
- Employees must be allowed to change the level of their contributions, but the employer need not accept more than one change every six months. They can ask you to stop deductions at any time. If this is the case, you do not have to restart them until six months is up.
- Deductions are made from earnings after tax. HM Revenue & Customs will credit basic rate tax relief for all members to the stakeholder pension provider later. Higher rate tax payers can claim additional relief through self-assessment tax returns.
- Contributions deducted from pay must be paid to the provider by the 19th of the following month.

Penalties for failure to meet stakeholder pension obligations (unless you are exempt, see **3**) can be up to £5,000 (for each offence) for an individual and £50,000 for an organisation. The Pensions Regulator may investigate and penalise employers who fail to offer access to a designated scheme to all relevant employees.

3 Who is exempt?

Some classes of employer are exempt from the requirement to offer stakeholder schemes.

3.1 Employers with **fewer than five** employees.

- However, companies which offer pension schemes — particularly schemes to which the employer contributes — will find it easier to recruit and retain employees.

3.2 Employers that already offer an **occupational pension scheme**.

But access to a stakeholder pension scheme must be provided if you have some employees who cannot join the occupational scheme because of eligibility requirements.

For example:

- If the qualifying service requirement for membership of your occupational scheme exceeds one year; or if the lowest age at which employees can join the main scheme is more than 18; or if the highest age at which they can join is more than five years before normal pension age, you may have to provide the over-50s with access to a stakeholder scheme.

3.3 Employers that offer a **group personal pension** to all relevant employees (see **5**), as long as they offer to make contributions and, if required, deduct any employee contributions from payroll.

- This exemption also applies to employers who contribute to employees' personal pensions.
- The employer must offer to contribute at least 3 per cent of employees' basic pay to the scheme.
The employer contribution offer can be made conditional on the employee contributing a specified rate, which normally cannot exceed 3 per cent of basic pay.
- The waiting period for joining the scheme must be no more than three months.
- There must be no exit charges for those who stop contributing or transfer from the scheme.

3.4 Employers whose employees all earn less than the **NI lower earnings limit** — £90 a week in 2008/09 (before tax).

4 Which employees?

4.1 Some individuals **cannot be enrolled** in your designated scheme.

- Anyone who is resident outside the UK, and does not have UK net relevant earnings, cannot join a stakeholder pension scheme (unless they are Crown Servants or their spouses or civil partners).

- People who are resident outside the UK but do have UK net relevant earnings can join, but only for the year or years in which they have those earnings.
- Anyone aged 75 or over cannot join.

4.2 With some employees you **need not make deductions**.

- You do not have to provide employees with access to your designated scheme within their first three months.
  This means that you do not have to pass on information to, or make deductions for, temporary or very short-term employees.
- You do not need to provide access for employees whose earnings have fallen below £90 a week for one or more weeks in the last three months.

4.3 There are **limits** on the amount that individuals can contribute to stakeholder pension schemes (see box, page 2).

Within these restrictions employees can join a stakeholder scheme, even if they already pay into an occupational pension scheme.

5 Keeping the costs down

Setting up a stakeholder pension will inevitably involve you in time and effort. However, there may be scope for limiting the overall costs.

5.1 Review your existing pension arrangements.

- It may make sense to extend the eligibility criteria that apply to your existing arrangements, in order to gain exemption.
- It may make sense to offer stakeholder pensions prior to membership of your existing scheme, especially to employees who are unlikely to stay for long.

5.2 Find out whether a stakeholder pension scheme is being offered by any of the **affinity groups** to which your company or its employees belong.

- For example, your trade association or the trade union to which your staff belong may have set up an arrangement for members. Such arrangements are likely to involve lower costs and easier administration.

5.3 Compare providers' terms and arrangements.

- Some may save you time and trouble by offering more help with administration or better marketing materials.
- Check investment performance too. Professional financial advisers can guide you on relative investment performance.

6 Finding help

Since you are legally obliged to offer a stakeholder pension scheme (unless you fall into one of the exempt categories), it will pay to get things right first time.

6.1 Consult your **professional advisers** (eg your HR adviser, accountant or financial adviser) especially if you intend to rely on one of the exemptions (see **3**).

- You cannot afford to make mistakes and the detailed legislation on stakeholder pensions is very complex.

6.2 Consult a **financial adviser** to help you set up a scheme.

- To find companies which are approved to sell stakeholder pensions, contact the Financial Services Authority (0845 606 1234 or www.fsa.gov.uk).

6.3 Information is available on most aspects of stakeholder pensions. Visit www.stakeholderpensions.gov.uk for links to relevant websites.

- For information on stakeholder pensions and registration requirements, contact the Pensions Regulator on 0870 606 3636. Consult the website to find out if you are exempt from offering a stakeholder pension (www.thepensionsregulator.gov.uk).

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