**EXPLANATORY MEMORANDUM TO**

**THE FINANCIAL ASSISTANCE SCHEME (TAX) REGULATIONS**

**2010 No. 1187**

**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.

**2. Purpose of the instrument**

2.1 The Financial Assistance Scheme (Tax) Regulations 2010 ("the Tax Regulations") prevents extra tax charges from arising when the property, rights and liabilities of a tax-registered occupational pension scheme that is winding up under-funded are transferred to the Secretary of State for Work and Pensions for the purposes of the Financial Assistance Scheme ("the FAS"). They also ensure that all the FAS payments receive broadly the same tax treatment as payments from a registered pension scheme in the hands of the recipient.

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

3.1 None.

**4. Legislative Context**

4.1 The Pensions Act 2004 and the Financial Assistance Scheme Regulations 2005 (S.I. 2005/1986) ("the 2005 Regulations") set out the legislative framework for the FAS. The FAS is currently not a pension scheme but a Government-funded arrangement to provide help for members of certain defined benefit occupational pension schemes (often known as final salary schemes) that wind up under-funded.

4.2 Part 4 of the Finance Act 2004 ("the 2004 Act"), which provides for the taxation of pension schemes, does not apply to the FAS. However, the FAS assistance payments are treated as the recipient's pension income for tax purposes. In this respect, the provisions in Part 9 of the Income Tax (Earnings and Pensions) Act 2003 ("ITEPA 2003") concerning pension income apply.

4.3 In December 2007, the Government announced a major extension of the FAS. One set of changes was that the Government would take in the remaining assets or sums of the relevant schemes and make the associated payments to their scheme members when due.

4.4 The Financial Assistance Scheme (Miscellaneous Amendments) Regulations 2010 (S.I. 2010/1149) ("the 2010 Regulations") amended the 2005 Regulations to allow such asset transfers and to extend the range of assistance payment available from the FAS, including the introduction of new lump sum types of payments.

4.5 Section 73 of the Finance Act 2009 enables HMRC to make regulations dealing with the tax treatment of the asset transfers and new lump sums. This is the first use of that power.

4.6 Section 164 of the 2004 Act authorises certain payments that may be made by registered pension schemes without attracting tax charges. Under the Tax Regulations, asset transfers to be made under the amended 2005 Regulations will be treated as if they were such authorised payments. This means the transfer of assets to the FAS will not generate a tax charge on the transferring scheme.

4.7 In addition, the Tax Regulations apply section 636A of ITEPA 2003 to the new lump sums the FAS will pay so that the tax exemption available in respect of certain lump sums made by registered pension schemes will apply to these payments from the FAS.

4.8 The Tax Regulations also apply to the FAS the provisions in the 2004 Act that give individuals a lifetime allowance in the amount of pension savings that can benefit from tax relief and apply a tax charge on savings beyond that allowance. These provisions will have broadly the same effects on all payments made by the FAS (lump sums and non-lump sums) made after the Tax Regulations come into force. This will ensure that the correct amount of tax relief is made available to any new recipient of assistance from the FAS.

4.9 Connected to the lifetime allowance provisions, the Tax Regulations impose in relation to payments made by the FAS certain information requirements and penalty provisions applicable to registered pension schemes under the 2004 Act.

## 5. Territorial Extent and Application

5.1 The instrument applies to all of the United Kingdom.

## 6. European Convention on Human Rights

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

## 7. Policy background

7.1 Pension tax relief is aimed at supporting saving to provide an income in retirement for the pension scheme member and/or their dependants. The pension tax rules set out what payments a registered pension scheme can make to or in respect of a member. These include payment of member benefits and death benefits and certain transfers to other schemes. These are known as authorised payments. Any other payment is known as an unauthorised payment which is subject to a tax charge of up to 70 per cent.

7.2 Since 2005, the FAS has been making assistance payments to members of certain final salary schemes that wind up under-funded. At present, these payments top up annuities arranged by the schemes to 90 per cent of the pension accrued at the point of the wind-up and they are subject to a statutory limit currently standing at £29,386. The FAS also pays assistance payments to surviving dependants. As the FAS is currently not a pension scheme, the pension tax rules do not apply. However, the payments made by the FAS are treated as the recipient's pension income for tax purposes.

7.3 The Government announced an expansion of the FAS in 2007 including the Government's taking in the remaining scheme assets and making associated payments when due. The 2010 Regulations will allow such asset transfers. There will also be changes to payments made by the FAS including the introduction of new lump sum types of payments.

7.4 The Tax Regulations will prevent extra tax charges from arising from these asset transfers and ensure that payments from the FAS receive broadly the same tax treatment as payments from a registered pension scheme in the hands of the recipient.

## 8. Consultation outcome

8.1 The Department for Work and Pensions ("DWP") has carried out an extensive consultation on the expansion of the FAS, most recently in relation to the 2010 Regulations between 12th August and 6th October 2009. The broad proposals for the tax treatment for asset transfers and new lump sums to be paid by the FAS were included in this latest DWP consultation document. Responses were broadly supportive: there was a general recognition that the Government was proposing a balanced approach to ensuring that members of the relevant final salary schemes would be treated fairly.

8.2 No separate consultation is required for the Tax Regulations.

## 9. Guidance

9.1 The Registered Pension Schemes Manual published on the HMRC website (http://home.inrev.gov.uk/rpsmmanual/rpsm01000010.htm) provides guidance on the pension tax rules. This will be updated at the next available opportunity to reflect the Tax Regulations. In the meantime, DWP (http://www.dwp.gov.uk/other-specialists/financial-assistance-scheme/) and the manager of the FAS (the Board of the Pension Protection Fund - http://www.pensionprotectionfund.org.uk/FAS/Pages/Fas.aspx) will publish guidance on their respective websites.

## 10. Impact

10.1 An Impact Assessment has not been produced for the Tax Regulations as they have no impact on business, charities or voluntary bodies.

10.2 As a result of the Tax Regulations, the manager of the FAS will be required to calculate the impact of payments it makes on the recipient's lifetime allowance and, if appropriate, calculate the resulting tax charge. It will also be subject to certain additional reporting requirements. These obligations are consistent with those of registered pension schemes.

## 11. Regulating small business

11.1 The legislation applies to small business but no additional burden has been identified.

## 12. Monitoring & review

12.1 HMRC will continue to monitor all aspects of the pensions tax legislation.

## 13. Contact

Windy Kwok at HMRC, telephone 020 7147 2835 or email: Windy.Kwok@hmrc.gsi.gov.uk, can answer any queries regarding the Tax Regulations.