

## Background

Stakeholder pensions were introduced by the Government with effect from 6 April 2001. However, stakeholder is a private pension scheme and not a State pension scheme.

For the first time, there is no requirement to have income from employment or self-employment to justify contributions to, what is effectively, a personal pension plan.

Stakeholder pensions were designed to offer good value private pension provision to those on low to average incomes. They were particularly designed for people without access to employer sponsored pension arrangements. However, their low cost and transparent design has gained a much wider appeal across all income ranges.

“Take up of the stakeholder pension has been well below expectations. It seems that it has mainly benefitted the rich by providing them with a vehicle for playing with their money, for example as a way of saving for their childrens' futures.”

[www.pensionsorter.co.uk](http://www.pensionsorter.co.uk)

To be classed as a stakeholder pension the arrangement must meet minimum standards and be registered with the Pensions Regulator. The Pensions Regulator was created under the Pensions Act 2004 and is the regulator of work-based pension schemes in the UK.

## Minimum Standards

The minimum standards are as follows:

- A simple transparent charging structure limited to 1.5 % pa of the fund value for the first 10 years and 1% pa thereafter.
- A minimum contribution of just £20.
- Members must be allowed to make contributions either on a regular basis, or as and when they wish.
- Transfers of pension rights from other schemes must be accepted.

# Stakeholder Pensions

by Arthur Childs Certified Financial Planner<sup>CM</sup>, Chartered Financial Planner

- There must be no additional charges for transfers in or out of stakeholder schemes.
- Each stakeholder scheme has to offer a clear default investment choice.

## Contribution Levels

The minimum contribution to a Stakeholder Pension is just £20 a month gross (£16 net).

This low entry level, however, does not mean that you can build up a useful pension by contributing at this level for very long. In this respect it is important to be aware of the system of ‘Pension Credit’ and you should refer to the separate heading below.

Essentially this could mean that if you were to build up a small pension fund you could find yourself not getting the full benefit of the money that you have set aside.

There is no limit to the amount that you can contribute to a stakeholder pension scheme. However, tax relief can only be obtained on contributions up to the level of your annual earned income (subject to an annual limit of £50,000 for the tax year 2011/12).

There is no requirement to show any earnings for contributions up to £3,600 gross (£2,880 net) in a tax year, or £300 gross (£240 net) a month by direct debit.

“Non-tax paying spouses should contribute to a stakeholder pension as a priority. They will get 20% tax relief at source (even though they are not paying any tax); 25% tax free cash from the fund at any time after age 55 and a taxable pension from the remainder (except that if they are still a non-tax payer they will be able to get the pension payments without deduction of tax).”

Arthur Childs  
Arch Financial Planning Limited

Contributions can be altered at any time down to the minimum of £20 a month or stopped altogether. In addition, one off contributions can be made at any time.

## Benefits

Unlike the State pension or an occupational pension scheme, the benefits under a stakeholder pension are not guaranteed. Instead, they depend on the amount you contribute, the charges made by the product provider (but these are low), the investment performance achieved on the underlying funds and the level of annuity rates available at the time you decide to take the benefits.

You can take benefits from a stakeholder pension at any time after age 55.

Under current legislation you can take 25% of the fund you have built up as pension commencement lump sum (currently paid tax free) and with the rest you can:

- purchase a 'secured pension', that is a conventional annuity (ie a known level of income for life). This could provide a level or increasing income.

You can either do this with your current pensions provider or transfer the fund first to another pensions provider (using the open market option) to obtain a more competitive annuity rate.

- purchase an 'unsecured pension', that is a pension drawdown product. This allows you to vary future income levels to fit in with your overall financial plan.

## Tax Relief

Contributions to stakeholder pensions generate direct tax savings. Basic rate tax relief (currently 20%) is given at source irrespective of whether you have earnings that are liable for tax or not. This means that you will only actually contribute £80 net for every £100 of contributions paid into your pension.

If you are a higher rate taxpayer (currently 40%) you will also make contributions net of basic rate tax and then claim additional relief by completing form PP120 and submitting it to your Tax Office or via your annual Self Assessment return. As a 40% taxpayer, therefore, you will only contribute £60 for every £100 of contributions falling within the higher rate band.

Your pension contributions once made will be based in funds where there is no liability to tax on capital gains and where all forms of investment income (except dividends) are also tax free.

Your money may therefore grow faster in a stakeholder pension than in most other forms of investment.

## Pensions Credit

On 6th October 2003 the Government introduced Pension Credit. This is in two parts:

- **the guarantee credit.** This is generally available for claimants aged 60 or over (in the case of a couple only the eldest person must be 60 or over) who are resident in Great Britain and are not subject to immigration control.

The Guarantee Credit will raise the claimant's income to the level of the appropriate minimum guarantee which for a single person is currently £137.35 a week and for a couple £209.70 a week (2011/2012).

- **the savings credit.** This is generally available for claimants aged 65 or over (in the case of a couple only the eldest person must be 65 or over). The amount of savings credit depends on how much a claimant's 'qualifying income' exceeds the savings credit threshold.

The maximum savings credit payable per week for a single person is currently £20.52 a week and for a couple is £27.09 a week (2011/2012). To obtain savings credit your qualifying income must be no more than £188 a week if you are single or £277 a week for a couple (2011/2012). In this context a 'couple' includes someone who has a husband, wife or civil partner, or they live with a person as if they were married to them or as if they were in a civil partnership with them.

The effect of Pension Credit is that, in some circumstances, individuals may only be slightly better off in retirement than if they had made no additional provision.

It is unlikely that you will know what your income/savings will be at the point of retirement. Furthermore, you cannot know what the qualifying criteria for Pension Credit will be at the time since governments over the years have, and will no doubt continue to, change benefit levels and structures.

This means that unless you will have a high level of income/savings in retirement you will not be able to be certain whether the Pension Credit will work for or against you.

## Members of Occupational Pension Schemes

A member of an occupational pension scheme may also contribute to a stakeholder pension scheme.

This presents an excellent opportunity to really build up your pension benefits, especially if you expect to retire early.

## If You Have Retired

Even if you have already retired you could still make use of a Stakeholder Pension to increase your pension income in later life.

You may have money on deposit which you are using to provide yourself with additional income. Such income may not be a great deal after tax. However, you could, for example, move a total of £14,400 over five years into a stakeholder pension. This would attract tax relief of a further £3,600 giving you a fund in five year's time of £18,000 plus investment growth.

You could take 25% of this as a pension commencement lump sum in five year's time and set up an additional pension from the balance. Although this additional pension is likely to be quite small it would generally be higher than the interest that you have forgone on the capital.

## Contributing on Behalf of a Child

You might like to put some money aside for one or more of your children or grandchildren. Whilst most people think of saving until a child is 18 or 21, there is something to be said for setting up a fund that cannot be used until the person concerned is age 55.

After all, to give too much money to a young person too early in life has been actually known to have a detrimental effect upon their prospects for achievement in life, rather than the reverse.

There is no minimum age limit for a Stakeholder pension but children younger than 16 need a parent's signature on the application form.

Basic rate tax relief is given at source even though in most cases the child will not have earnings that are liable for tax. Please note, however, that it is the child's tax rate that determines whether higher rate tax relief can be reclaimed.

The maximum contribution is again £2,880 net (ie £3,600 gross) in a tax year or £240 net (ie £300 gross) a month by direct debit.

## Existing Personal Pension Plans

In view of the 1.5% cap on charges under a Stakeholder pension, the question arises as to whether you should continue contributing to your existing personal pension plans or transfer them to a Stakeholder Pension.

Many large pension offices have solved this dilemma simply and easily by announcing that the maximum charge on their personal pension plans will in future also be capped at 1.5% a year.

This is not the case with all pensions product providers, however, and it could be in your interests to transfer an existing pension fund to a Stakeholder Pension in some cases.

We are happy to carry out a comparison of the future charges on your existing personal pension plan (or retirement annuity) with the charges that would apply if you were to transfer your fund to a Stakeholder Pension.

When considering such a transfer we will also take account of the strength of the product provider and the performance of their funds etc.

## Useful Links

**HM Government** stakeholder pension information [http://www.direct.gov.uk/en/Pensionsandretirementplanning/Companyandpersonalpensions/PersonalPensions/DG\\_4017567](http://www.direct.gov.uk/en/Pensionsandretirementplanning/Companyandpersonalpensions/PersonalPensions/DG_4017567)

The **Pensions Advisory Service** stakeholder pension helpline [www.stakeholderhelpline.org.uk/](http://www.stakeholderhelpline.org.uk/)

## Risk Factors

- The Key Features document which accompanies each stakeholder illustration, provides you with details of any risks and potential disadvantages associated with the contract recommended.
- An investment into a Stakeholder Pension or other Personal Pension Plan is intended as a long-term investment. Under the new pension rules it is not possible to access the funds prior to the age of 55.
- When you take the benefits you can only obtain a maximum of 25% of the pension fund as a cash sum. The balance of the fund has to be used to purchase a pension.
- Where past performance is mentioned please note that the past is not necessarily a guide to future performance. For example, the treatment of pension funds has changed with the removal of tax credit on UK equity investment.
- The value of units and the income from them may go down as well as up and your pension fund may be less than the amount you have invested.
- Tax relief depends on individual circumstances and tax rates and laws may change in the future.
- The illustrations use certain assumed rates of growth, as prescribed by the Financial Services Authority. These rates are not guaranteed and it would be prudent to review your contract on an ongoing basis.
- All statements concerning the tax treatment of products and their benefits are based on our understanding of current tax law and Inland Revenue practice. Levels and bases of tax relief are subject to change.

Please note that this information does not constitute personal advice and should not be treated as a substitute for specific advice based on your circumstances.

Any information given in this Guide relating to income tax legislation is based on our understanding of legislation and practice in force at the date of this Guide. Whilst we believe our interpretation of current law and practice to be correct in these areas, we cannot be responsible for the effects of any future legislation or any change in interpretation or treatment.

In particular you are warned that levels of tax and tax reliefs and also State Benefits that may have been referred to, are subject to alteration and, in any case, the value of such reliefs and benefits may depend on an individual's circumstances.

### For personal advice

If you would like to receive advice on your pension planning or discuss any issue that has been raised by these notes please ask your usual Arch adviser or contact us via one of the following:

Tel: **0845 3700 661**  
or **01483 204600** (if local)  
Email: **enquiries@arch-fp.co.uk**  
Online: **www.arch-fp.co.uk**



AUTHORISED AND REGULATED BY THE FINANCIAL SERVICES AUTHORITY