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Core Unit 1A – Understanding Retirement Provision

Assignment 4 Notes

(Part 4 – Workplace Pensions)

Recommended Time: 1 Hour

1. **Write short notes on Self-Invested Personal Pensions (SIPPs). Your answer must refer to the term Income Drawdown.**

**10 Marks**

Answer should cover the following:

* Introduced following a government initiative announced in the 1989 Budget
* Making it easier for members to control their own pension fund investment
* Finance Act 1995 introduced income drawdown which increased its popularity
* Income drawdown allowed members to take an income which can vary year to year.
* Pre 6 April 2015, two types of drawdown – capped / flexible
* Capped – maximum amount of income that could be taken but no minimum
* Flexible – satisfy the minimum income requirement, lifted the maximum that could be taken
* Works the same way as a normal personal pension plan, contributions paid, and benefits are relied upon amount of contributions and investment return.
* Downfall – been susceptible to pension scams.

(Relevant section of the manual is Part 4 Chapter 1.2.3)

1. **Outline what a final salary pension is and state how it differs to a Career Average Revalued Earnings scheme.**

**10 Marks**

Answer should cover the following:

Final Salary pension scheme:

* Historically the more common type of design
* Amount of pension on retirement is provided by a set formula:
* Pension = N x Accrual Rate x Final Pensionable Salary

N =the length of service, Accrual Rate is a fraction commonly 60ths or 80ths

* Final Pensionable Salary is based on the member’s salary at the time of leaving the scheme over a specified length of time, i.e., 12 or 36 months. In some cases, an amount may be disregarded for LEL. Also, may specified that certain elements of pay are to be disregarded.

CARE scheme:

* Are increasing their popularity to final salary schemes
* The principal difference is the benefits reflect earnings throughout the period of membership rather than just in the period preceding date of leaving
* Benefits are accrued on a yearly basis and revalued each year
* Offer a DB scheme whilst maintaining a measure of predictability and so more control over costs
* Also, maybe more suitable to members with variable earnings as it effectively averages the remuneration out over the members working lifetime.

(Relevant sections of the manual is Part 4 Chapter 2.1.2 & 2.1.3)

1. **What is a Cash Balance scheme?**

**10 Marks**

Answer should include the following:

* DB schemes
* Share some characteristics of money-purchase schemes
* Contributions are paid each year by the employee and employer
* Contributions are invested and at retirement the member is provided a lump sum which can be used to provide a pension
* The cash sum is defined at the outset and does not depend on investment return
* The employer will make up any shortfall
* Lump sum can be defined and known in advance, but the amount of pension payable will depend on market conditions at retirement.
* For example, a company might set up a cash balance scheme and members are required to pay 5% of salary each year in return for a lump sum of 20% of final salary for each year of membership. Or alternatively, the rules might stipulate the contribution rate and the rate of investment return to be allocated.

(Relevant section of the manual is Part 4 Chapter 2.1.5)

1. **Outline what a collective defined contribution scheme is.**

**5 Marks**

Answer should include the following:

* The Pension Schemes Act 2021 sets out the framework – CDC schemes
* Pool risks and costs between members
* Offer a targeted but not guaranteed level of income at retirement
* Employer will benefit from fixed cost defined contributions
* The Pensions Regulator laid down a code of practice in June 2022 which detailed the necessary criteria for authorisation and the ongoing supervision.

(Relevant section of the manual is Part 4 Chapter 2.2.2)

1. **Write short notes on small self-administered schemes and other executive arrangements.**

**10 Marks**

Answer should cover the following:

* SSAS – a trust based occupational scheme
* For a small number of employees – directors / key staff
* Members are able to direct / control investments
* Classed as investment regulated pension schemes and subject to special tax rules
* Prior to 6 April 2006 – required to have an experienced professional trustee from an approved list of pensioneer trustees. No longer required
* Executive schemes (historically known as top hat schemes) – offer a higher level of benefits than that provided by the standard company pension scheme offered to majority of employees
* Top up / supplementary scheme sits alongside the main scheme
* Executive entitled to benefits from main scheme and topped up by the executive scheme
* Executive retires, the benefits are aggregated
* Section 226 policies – legacy arrangements
* Exceed annual allowance / lifetime allowance thresholds, company may provide additional benefits from an employer-financed retirement benefits scheme.

(Relevant section of the manual is Part 4 Chapter 2.3.5)

1. **Explain the term ‘short service refunds’?**

**5 Marks**

Answer should cover the following:

* Trust based schemes were able to offer short service refunds to members who leave with less than 2 years’ service
* Not include employer contributions
* Contract based schemes not permitted to offer short service refunds except for cooling off period of 30 days service
* However, short service refunds now been abolished for new entrants from 1 October 2015.

(Relevant section of the manual is Part 4 Chapter 3.1.2)