Isle of Man
Government
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A Proposal Document

Proposed New Pension Scheme to Provide Greater Pension Freedoms

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Proposed New Pension Scheme to Provide Greater Pension Freedoms

1. Introduction

In July 2015, Tynwald approved a motion in relation to Isle of Man pension schemes. The motion read as follows:

"That Tynwald supports the concept of pension freedom; and is of the opinion that Treasury should bring forward by October 2015 proposals to allow Manx residents pension freedoms equal to or better than those currently available in the UK".

In October 2015, the then Treasury Minister announced to Tynwald that it had not been possible to prepare a report to review options and proposals in the timescale. He did, however, advise that he had asked the Department of Economic Development to lead on the matter and that a working group, attended by a range of private sector and Government participants had met and was considering the relevant issues. Subsequently, in January 2016 he advised Tynwald that an additional technical group had recently been formed to consider the options available.

In the 2016 Budget, some measures of pension freedom were introduced:

- the trivial commutation limit was increased to £50,000 (this is the level up to which members of approved pension schemes can opt to convert one or more small, untouched pension funds into lump sum payments);
- the age at which a trivial commutation lump sum may be paid was reduced to 55; and
- the age at which a fund remnant may be paid was reduced to 55 (the fund remnant is the amount remaining following the withdrawal of funds from an approved pension scheme and it cannot exceed the value of the commutation limit).

Since that time Treasury and the Department of Economic Development have continued to work with the pensions industry and other interested parties to find the best way to introduce further pension freedoms in the Island whilst at the same time protecting the pensions industry as well as the general revenue.

2. Purpose of this document

The purpose of this document is to set out the basic details of a new pension product that would deliver pension freedoms in the Island and to seek responses to questions raised as well as general feedback and suggestions regarding what is being proposed.

3. Proposed new pension scheme

Following much consideration about how best to introduce pension freedoms in the Isle of Man, a new pension product is being proposed. This new product will essentially provide certain pension scheme members, who have pension pots which exceed the current trivial commutation and fund remnant thresholds, greater flexibility to access their pension pots, subject to the applicable rules and requirements, as well as providing a new retirement savings vehicle for individuals.

This will take the form of a new pension scheme that will be provided for in the Income Tax Act 1970. It will be available to both residents and non-residents and it will be possible to transfer funds from an existing approved scheme into the new product ("approved scheme" refers to a pension scheme approved by the Assessor of Income Tax under the Income Tax (Retirement Benefit Schemes) Act 1978, the Income Tax 1989 or the Income Tax Act 1970). The new scheme will, however, be limited to no more than one per person. The main features of the scheme are set out below.

3.1 Main features of the proposed pension scheme

The basic structure of the scheme being proposed is as follows:

- a minimum retirement age of 55;
- no maximum retirement age;
- tax relief on contributions:
    - up to an annual contribution limit of £5,000; and
    - allowed at the rate of 10%;
- pension growth builds up tax-free;
- full access on reaching the scheme retirement age, including the ability to take the whole of the pension pot in one withdrawal or to make smaller withdrawals as and when required by the member;
- 40% tax-free lump sum;
- remainder of funds are subject to income tax at a rate of only 10%;
- no tax on death.

The proposals do not constitute views or recommendations about the suitability of the proposed new scheme for individuals, and the proposed new scheme may not be appropriate for every individual. If the proposals are enacted, prospective members should carefully consider all of the costs and benefits associated with the new scheme before making a decision about their pension savings and, if necessary, seek appropriate financial advice.

Question 1

Do you agree that individuals should be able to access their entire pension pot instead of the pension providing an income in their retirement?

Question 2

Do you agree with the proposed basic structure of the new scheme? If not, what would you change and why?

3.2 Approval by the Assessor

The proposed new pension scheme will need to be approved by the Assessor of Income Tax in order for contributions paid into the scheme to qualify for tax relief. Approval will require the scheme to satisfy certain conditions which are anticipated to be similar to some of those that need to be satisfied by current pension schemes when gaining approval. There are currently several different types of scheme that require approval and each has its own set conditions. In order to illustrate possible conditions, the following are examples taken from a selection of existing schemes and, as such, this is not a list of conditions that need to be satisfied by any one particular scheme.

The conditions for approval will include some of the following:

- that the scheme is properly established under irrevocable trusts governed by the laws of the Island (for a personal pension scheme) or under irrevocable trusts in relation to a trade or undertaking (for an occupational pension scheme);
- that the administrator (or the administrator and at least one trustee) of the scheme are resident in the Island;
- that the administrator has a fixed place of business in the Island from which the administrator's business is conducted;
- if an amendment is made to an approved scheme without being approved by the Assessor, her approval of the scheme shall cease to have effect;
- for an occupational pension scheme:
    - that the employer is a contributor to the scheme;
    - that the scheme is recognised by the employer and the employees to whom it relates, and that every employee who is, or has a right to be, a member of the scheme has been given written particulars of all essential features of the scheme which concern him.

Question 3

Are there any particular conditions that you think the new scheme should, or should not, be required to satisfy?

3.3 Nature of pension scheme

The proposed scheme can be either a personal pension scheme or an occupational pension scheme. It cannot, however, be a defined benefits pension scheme and the new scheme will not be permitted to accept transfers in from a defined benefits scheme.

Question 4

Do you agree that the proposed scheme could include an occupational pension scheme?

3.4 Transfer fee to protect revenue

Given the proposed reduction in the rate of income tax that the pension will be charged and the higher tax-free lump sum proposed, an appropriate fee will be charged for the transfer of a pension from an existing scheme in order to protect revenue, particularly as contributions to the scheme being transferred may have already received tax relief at up to 20%. The level of fee proposed is 15% of the sum to be transferred and the amount of fee charged will not be taken into account for the purposes of the income tax cap. The fee will be deducted before the transfer, by the administrator of the existing pension scheme, and paid to the Assessor.

Question 5

Do you agree with the level of the proposed transfer fee? If not, what would you suggest?

4. Comparison of existing schemes with the proposed new scheme

4.1 Example 1

a) In this example, the total value of the pension scheme at the time of retirement is £100,000, there is no transfer fee and the member takes their whole pension pot in one withdrawal.

Tax treatment of existing scheme under existing rules:

Pension scheme value			£100,000
Tax-free pension commencement lump sum @ 30%			(£30,000)
Chargeable balance			£70,000
Less personal allowance			(£12,500)
Taxable balance			£57,500
Lower rate band	£6,500 @ 10% =	£650	
Higher rate band	£51,000 @ 20% =	£10,200	
Total tax payable			**£10,850**

Tax treatment of new scheme under proposed rules:

Pension scheme value (& value transferred)	£100,000
Tax-free pension commencement lump sum @ 40%	(£40,000)
Chargeable balance	£60,000
Less (balance of) personal allowance	(£12,500)
Taxable balance	£47,500
Total tax payable – 10% of remaining balance	**£4,750**

Difference between the existing scheme and the new scheme:

Existing scheme	£10,850
New scheme	£4,750
Difference	**- £6,100**

b) Effect of introducing a pension transfer fee of 10%:

Pension scheme value to be transferred	£100,000
Transfer fee @ 10%	(£10,000)
Balance transferred to new scheme	£90,000
Tax-free pension commencement lump sum @ 40%	(£36,000)
Chargeable balance	£54,000
Less (balance of) personal allowance	(£12,500)
Taxable balance	£41,500
Total tax payable – 10% of remaining balance	£4,150
Total fee & tax payable	**£14,150**

Difference if there is a 10% transfer fee payable:

New scheme	£14,150
Existing scheme	£10,850
Difference	**£3,300**

c) Effect of introducing a pension transfer fee of 15%:

Pension scheme value to be transferred	£100,000
Transfer fee @ 15%	(£15,000)
Balance transferred to new scheme	£85,000
Tax-free pension commencement lump sum @ 40%	(£34,000)
Chargeable balance	£51,000
Less (balance of) personal allowance	(£12,500)
Taxable balance	£38,500
Total tax payable – 10% of remaining balance	£3,850
Total fee & tax payable	**£18,850**

Difference if there is a 15% transfer fee payable:

New scheme	£18,850
Existing scheme	£10,850
Difference	**£8,000**

4.2 Example 2

a) In this example, the total value of the pension scheme at the time of retirement is £500,000, there is no transfer fee and the member takes their whole pension pot in one withdrawal.

Tax treatment of existing scheme under existing rules:

Pension scheme value			£500,000
Tax-free pension commencement lump sum @ 30%			(£150,000)
Chargeable balance			£350,000
Less personal allowance			(£12,500)
Taxable balance			£337,500
Lower rate band	£6,500 @ 10% =	£650	
Higher rate band	£331,000 @ 20% =	£66,200	
Total tax payable			**£66,850**

Tax treatment of new scheme under proposed rules:

Pension scheme value (& value transferred)	£500,000
Tax-free pension commencement lump sum @ 40%	(£200,000)
Chargeable balance	£300,000
Less (balance of) personal allowance	(£12,500)
Taxable balance	£287,500
Total tax payable – 10% of remaining balance	**£28,750**

Difference between the existing scheme and the new scheme:

Existing scheme	£66,850
New scheme	£28,750
Difference	**- £38,100**

b) Effect of introducing a pension transfer fee of 10%:

Pension scheme value to be transferred	£500,000
Transfer fee @ 10%	(£50,000)
Balance transferred to new scheme	£450,000
Tax-free pension commencement lump sum @ 40%	(£180,000)
Chargeable balance	£270,000
Less (balance of) personal allowance	(£12,500)
Taxable balance	£257,500
Total tax payable – 10% of remaining balance	£25,750
Total fee & tax payable	**£75,750**

Difference if there is a 10% transfer fee payable:

New scheme	£75,750
Existing scheme	£66,850
Difference	**£8,900**

c) Effect of introducing a pension transfer fee of 15%:

Pension scheme value to be transferred	£500,000
Transfer fee @ 15%	(£75,000)
Balance transferred to new scheme	£425,000
Tax-free pension commencement lump sum @ 40%	(£170,000)
Chargeable balance	£255,000
Less (balance of) personal allowance	(£12,500)
Taxable balance	£242,500
Total tax payable – 10% of remaining balance	£24,250
Total fee & tax payable	**£99,250**

Difference if there is a 15% transfer fee payable:

New scheme	£99,250
Existing scheme	£66,850
Difference	**£32,400**

5. Submissions

Responses to the questions raised in this document, together with any comments or suggestions concerning the proposals, would be welcomed. Anyone wishing to submit a response to this proposal is invited to do so by Friday 15 September 2017. Responses should be sent to:

Paul Martin, Deputy Assessor
Income Tax Division
2nd Floor Government Offices
Bucks Road
Douglas IM1 3TX Email: consultation@itd.treasury.gov.im

In any consultation exercise the responses received do not guarantee that changes will be made to what has been proposed.

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All information in responses, including personal information, may be subject to publication or disclosure in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2015 and the Data Protection Act 2002). If you want your response to remain confidential, you should explain why confidentiality is necessary and your request will be agreed to only if it is appropriate in the circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding.

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