SOVEREIGN PENSIONS UPDATE 09

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ARTWORK BY MAN FUNG YI

Flexible Pension Benefits and Temporary non-UK residents

The new flexible pensions regime, which will allow members of defined contribution pension schemes to draw benefits after the age of 55 without restriction, is to be introduced in the UK on 6 April 2015.

Where the pension scheme member lives outside of the UK there may also be the added advantage of drawing benefits without the imposition of UK income tax – either by claiming tax treaty relief where available, or by transferring the UK pension benefits overseas to a QROPS.

For the short-term non-UK resident, however, the decision to draw benefits using the new flexible rules could result in an unexpected UK income tax bill. Designed to prevent opportunistic tax arbitrage, the temporary non-residence rules allow flexible benefits to be taxed when a scheme member takes up UK residence again and where all of the following circumstances apply:

- The member was UK resident in at least four of the seven tax years before becoming non-UK resident;
- The period of time spent outside of the UK was not more than five years; and
- Flexible withdrawals during the period of non-UK residence were (cumulatively) £100,000 or more.

The tax falls due in the tax year of return and the rules apply equally to UK pensions and QROPS.

Lifetime Allowance – International Enhancement

The UK's lifetime allowance (LTA) cap of £1.25 million on tax relieved pension savings is an important consideration for many expatriates. Particularly as successive cuts in the LTA have succeeded in drawing more pension savers into the tax net.

Where an individual no longer resides in the UK but remains an active member of a UK pension scheme, it is possible to apply for an international enhancement to their LTA for periods of service after 6 April 2006. This enhancement is available provided the funding of the pension was not UK-tax relieved during the member's time overseas.
In order to claim an international enhancement the member must complete form APSS202, which is accessible here.

Transferring to a QROPS remains one of the most effective means of mitigating the LTA charge and a valuable planning tool for individuals with significant pension savings.

Defined Benefit Transfer Guidance

The Pensions Regulator (TPR) issued guidance, on 13 February, for UK defined benefit pension trustees when dealing with transfer requests to defined contribution schemes (including QROPS) after 6 April this year. The consultation document makes it clear that member advice must come from a firm holding the relevant UK Financial Conduct Authority (FCA) pension transfer permissions.

The guidance does not address the issue of advice for non-UK resident members where FCA-regulated advice will not be readily available. Sovereign will seek clarity on this issue as part of the consultation, which ends on 17 March. The paper may be viewed here.

It should be noted that defined benefit entitlements worth less than £30,000 fall outside the mandatory advice requirement.

PenTech - New Rules to Increase

Public Sector (PS) Defined Benefit Salary Related schemes are statutory and have been the centre of discussion with an indicated ban on transfers out of these unfunded – not to be confused with "underfunded" – arrangements to Defined Contribution (DC)/Money Purchase schemes, both UK and overseas.

The interesting point here is that the NHS, teachers, armed forces, civil service, police and firefighters are all unfunded PS schemes and fall within the prohibited transfer bracket.

An unfunded scheme is one where pension benefits are paid out of current income, as and when they become due. The interesting point here is that the NHS, teachers, armed forces, civil service, police and firefighters are all unfunded PS schemes and fall within the prohibited transfer bracket. However the Local Government Pension Scheme (LGPS) remains a funded PS scheme – one where the scheme member's pension rights are (should be) covered by assets held under trust – and therefore should fall outside this ban.

In reality, the last actuarial funding check completed on the LGPS recorded a deficit on an on-going/technical provisions basis (not "full solvency") of about £47 billion with a funding level of only about 79%. So, together with some 80% of private sector DB schemes that are in on-going deficit, the possible restriction of transfers will place increasing pressure on the UK government and employers alike to fund an arrangement that they are struggling to afford.

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Guernsey to Allow Flexible Benefits

Guernsey's Treasury Department "intends to bring proposals to allow flexibility of benefits to international pensions, such as Qualifying Recognised Overseas Pension Schemes (QROPS), held in Guernsey before the States of Deliberation (Guernsey's parliament) this summer," said Guernsey Finance in a statement on 13 February.

Guernsey's QROPS market has been restricted to Guernsey residents since 2012 as a result of UK legislative changes. However, there is still a significant book of business across the island from QROPS transfers that were made prior to 2012. It is anticipated that these schemes will benefit equally from the proposed flexible regime.

More information will follow once the proposals have been published and introduced into Guernsey's parliament for debate.

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