

# Tax clampdown on flexible pensions

Britons retiring abroad and using flexible offshore pension schemes to exploit tax loopholes face the risk of a hefty tax bill.

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The Government is targeting overseas pension schemes that can be used as a tax loophole Photo: Getty Images

Thousands of Britons retiring abroad and using flexible offshore pension schemes to exploit tax loopholes face the risk of a hefty tax bill.

Offshore pensions, known as Qualifying Recognised Overseas Pension Schemes (QROPS), have generated a lot of interest among Britons leaving for foreign shores since they were first introduced in April 2006.

In some cases, these schemes have been promoted as a way to avoid buying an annuity by the age of 75 while still retaining tax relief granted on pension contributions made in Britain.

However, HM Revenue & Customs (HMRC) is expected to crack down on these schemes as increasing numbers of retirees with large pension pots escape paying British tax on their pension income.

Mike Morrison, the head of pensions development at Winterthur Life, said: "HMRC will look carefully at whether the jurisdictions for QROPS have a legitimate pensions framework.

The point of these plans is to allow people to move abroad and take their pension scheme with them – they're not meant to be a way to get additional benefits."

Under QROPS rules, those leaving the UK on a permanent basis can transfer their pensions to an overseas scheme and retain their UK tax benefits after a holding period of just five years, provided the new scheme can demonstrate that at least 70 per cent of the fund will be used to provide a pension in retirement.

However, Lee Smythe, the managing director of Killik Chartered Financial Planners, said: "Quite a few providers were marketing the schemes as a way of taking as much money out after five years as you like – rather than a lump sum and then having to buy an annuity.

"Yet to qualify in the first place the QROP is meant to mirror the amount that can be taken as tax-free cash in the UK and be bound by that.

"The issue is that after five years in a QROP the requirement to report to HMRC any transfers or lump sums taken from the scheme drops away.

"As a result, some people have been taking all the money out in one go, rather than using it to provide pension benefits."

Yet any scheme promoting this avenue risks being wiped off the authorised scheme list.

HMRC states that individuals can face tax charges of up to 55 per cent of the sum transferred if QROPS do not comply with UK tax rules to claw back tax relief granted in the UK.

A government spokesman said: "The rules for transferring UK pension funds overseas are intended to make life in retirement simpler for those who choose to take their pension funds with them to a new home abroad; and to use those funds for the purpose for which the Government has provided generous tax relief – namely to provide an income for life.

"HMRC is looking carefully at the operation of transfers to QROPS to ensure that the system works for those who genuinely need it."

Some jurisdictions have already been taking steps to ensure they fall under the HMRC rules.

For example, Guernsey announced tighter restrictions last year on QROPS based on the island. These are understood to include a restriction limiting any lump sum payments to 25 per cent of the fund applicable to both residents and non-residents.

Mr Morrison said: "Guernsey has taken the lead to show it's a responsible QROPS jurisdiction. Yet while HMRC may be tightening up on these schemes, it needs to be careful as there does need to be a way of moving between different countries and taking your pension with you."

Matt Brunwin, a pensions specialist at independent financial adviser Bestinvest, added:

"The Revenue will be keeping a closer eye on whether QROP providers are remaining in the spirit of what they're meant to be doing – moving your pension abroad to create an international pension fund.

"Yet as this avenue has arrived, it's potentially open to abuse, and as we've seen in the past the Government likes to close those doors pretty quickly."

There are around 1,700 of these schemes in existence at present, but many could delist from the authorised overseas pension register if they are found to fall short of legislation.

Speculation over QROPS has grown steadily since overseas pensions schemes based in Singapore were delisted from the authorised register following allegations of abuse last summer. The pension fund industry believes other countries could follow.

The number of pension transfers to popular destinations has grown steadily in recent years.

Jurisdictions such as Hong Kong, the Irish Republic and the Channel Islands all offer more lenient tax treatment on retirement income options, inheritance and lump sum payments from pension funds.

As Singapore does not levy inheritance tax on remaining pension pots upon death and some pensioners may avoid local income tax altogether, it was heavily marketed by offshore advisers.

However, investors being targeted with "pension-busting" promises, allowing them to take their funds partly or wholly in cash ahead of retirement should tread carefully.

HMRC said it will monitor foreign jurisdictions to make sure they comply with basic UK rules and were no more attractive, from a tax position, than remaining in Britain.

Mr Smythe said: "The Government is quite precious over pension benefits because it sees the tax relief offered in this country as very generous and believes people should be told what to do with their retirement fund.

"Yet for people who are leaving the UK QROPS can offer better value than leaving money in a UK pension scheme.

"If there isn't a structured scheme in the country they are moving to, then using a QROPS provides a method of managing their money."

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