OLD MUTUAL INTERNATIONAL

Pension transfers: 10 traps not to be forgotten

If you are a UK resident having moved abroad, it is likely you have built up a number of separate pensions. You have the option of keeping your existing UK pension plan(s) or transferring them into some other retirement pension scheme. Here are 10 of the most overlooked considerations which you may want to consider.

1. Flexi-access drawdown and the lifetime allowance (LTA)

A common reason to transfer benefits from a defined benefit (DB) scheme to a defined contribution (DC) scheme is to defer income, or to drawdown flexibly. However, a (DB) transfer can result in LTA considerations, given low gilt yields generating historically high transfer values. The assessment against the LTA is often more favorable for a DB scheme pension (20x pension plus any pension commencement lump sum) as opposed to the cash equivalent transfer value (CETV).

2. Passing on DC pension benefits free of inheritance tax (IHT)

Being able to pass on pension benefits upon death, free of IHT from DC plans, is often considered highly attractive. However, where an individual dies within two years of making a transfer, executors are required to report this to HM Revenue & Customs (HMRC). Where the person was in poor health when the transfer took place (for example, expecting to live for less than two years) then an IHT charge can arise. So if death benefits are a key driver due to the ill health of a member, being aware of the IHT position is critical.

3. Preserving the pre April 2016 LTA

Fixed Protection 2016 (FP2016) and Individual Protection 2016 (IP2016) enable members to protect themselves from the fall in the value of the lifetime allowance from £1.25m to £1m. FP2016 will preserve the pre April 2016 lifetime allowance of £1.25m, but a number of conditions apply, including a restriction on contributions to a DC plan and a restriction on accruals to a DB scheme. You may want to seek professional advice on this before making any decision.

4. Enhanced CETVs and protected lifetime allowances

As employers increasingly look to close schemes or sell liabilities to insurers in order to remove an open-ended and unquantifiable liability, enhanced CETVs are sometimes offered. It should be remembered that fixed protection (and also enhanced protection) may be lost if the value of a transfer payment is not equal to the value of the pension rights being transferred.

5. Transfer considerations for existing DB pensioners

Approximately 40% of DB scheme members are drawing benefits. DB scheme trustees often do not allow pensioner members to transfer out, but if they do, the new trustees must continue to provide a scheme pension or otherwise the transfer would be considered an unauthorised payment, and the member would incur a tax charge of 55% of the value transferred.

6. The 'non-residence factor'

Where an individual is working abroad but is a member of a UK scheme, they may not receive UK tax relief on contributions to, or the accrual of benefits under, a registered pension scheme. Yet the resulting benefits may count towards benefit crystallisation events. For this reason, the individual's lifetime allowance may be enhanced by a factor which is called a 'non-residence factor' which takes into account the value of the contributions/accrual that did not receive UK tax relief.

7. The 'recognised overseas scheme transfer factor'

Where an individual transfers from a recognised overseas pension scheme (ROPS) or a qualifying recognised overseas pension scheme (QROPS) back to a UK relevant scheme such as a SIPP, the individual's lifetime allowance may be enhanced by a factor which is called a 'recognised overseas scheme transfer factor'. This takes into account the value transferred back to the UK (not including any contributions to the ROPS or QROPS which had UK tax relief).

8. Temporary non-residence

Individuals overseas who take benefits, may retrospectively have to pay UK tax on certain payments from their pension (normally only in excess of their pension commencement lump sum and £100k of pension income) made while they were non-resident, if the UK's 'temporary non-residence' rules apply. These rules will apply if both:

- the individual returns to the UK within five years of moving abroad (or five full tax years if they left the UK before 6 April 2013), and
- the individual was a UK resident in at least four of the seven tax years before they moved abroad.

9. The overseas transfer charge

Transfers to a QROPS after 8 March 2017 can be subject to the overseas transfer charge even if not initially caught. If the client's situation changes during the 'relevant period', so that the charge would have applied at outset, the charge of 25% applies retrospectively. The relevant period covers the rest of the tax year in which the initial transfer was made and the next five full tax years– which could be closer to six calendar years, if the initial transfer is shortly after the start of a tax year.

10. Double tax treaties

On occasions double tax agreements can throw up some compelling opportunities, particularly if tax is not chargeable where the pension is located and where the member resides, when the benefit is enjoyed. Care needs to be taken to understand the qualifying residency conditions overseas, and the completion of the 'DT-Individual' form, should the pension in question come from the UK. HMRC's newly updated 'Digest of double tax treaties' is a good place to start.

What does this tell us?

Advice on pension transfers should be undertaken in the context of a highly personal, full financial planning service, subject to ongoing review including possible changes to your residency both in the short and medium term. Always remember to speak to your financial adviser before you make any pension transfer decisions.

By Jason Pearce, Head of Technical Sales, Hong Kong & NE Asia, Old Mutual International.

About Old Mutual International

Old Mutual International, part of Old Mutual Wealth, provides offshore and cross-border wealth management solutions for affluent and high net worth local, internationally mobile and expatriate investors. The Hong Kong branch was established in 1991, and the Singapore branch in 2008, to provide innovative, flexible, wealth management solutions and local support to its customers.