Implications for overseas arrangements

Our earlier newsletter, “UK Pensions - Tax Simplification” summarises the Revenue’s simplification proposals and so provides the background to this note. A copy of that newsletter is available from julie.west@linklaters.com

The Revenue’s simplification proposals primarily affect UK pension arrangements. However, the proposals also have implications for some non-UK arrangements, as explained in this newsletter.

Changes to eligibility requirements

Proposed change

Currently, non-UK resident employees of a non-UK employer cannot accrue benefits under a UK exempt approved scheme. The Revenue proposes that, from the date when its simplification proposals take effect (“A-Day”), such employees should be able to join registered schemes.

This means that employers will, in principle, be able to include non-UK employees in their main UK-registered schemes, rather than operating separate offshore or “S615” arrangements. However, this does raise issues:

– the UK scheme is likely to need tax approval in the jurisdictions where the employer is resident, to ensure tax relief is obtained on employer contributions. This will require compliance with local tax approval requirements, including local limits on benefits – as well as the simplified UK regime

– the lifetime allowance will impose a “cap” on benefits for employees whose benefits will normally be “uncapped”.

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Secondments
Currently, the Revenue only allows a person seconded to a non-UK employer to remain in a UK approved scheme for 10 years (subject to the fulfilment of certain other conditions). The change in eligibility requirements ought to mean that such employees can remain in UK-registered schemes on an unlimited basis.

Changes affecting non UK schemes

Offshore schemes for UK employees
Some employers operate offshore arrangements for UK employees. Such arrangements are treated for tax purposes in a way that is similar to a UK FURBS. Although the proposals are silent, it would appear that the changes in tax treatment for FURBS will apply to such schemes.

Section 615 Schemes
Some employers operate schemes approved under S615 of ICTA. These schemes have a UK Trustee but are established for the benefit of non-resident employees of employers whose business is wholly or partly outside the UK. Benefits paid under these schemes are not liable to UK tax when paid to non-residents, and lump sums paid to UK residents are also not taxable.

The Revenue proposes to abolish the S615 regime from A Day on the basis that these schemes will no longer be required because such employees can be included in a UK-registered scheme. This does raise some issues:

- some S615 schemes offer 100% cash which would not be permissible under a UK-registered scheme
- S615 schemes are exempt from many of the Pensions Act requirements which helps to avoid conflict with regulatory requirements in any jurisdiction where members are employed
- registered schemes will be subject to UK funding and statutory debt requirements. S615 schemes are not currently subject to those requirements. Including former S615 members in a registered scheme will therefore mean that employers are subject to more onerous funding obligations under UK law than presently.
- benefits under these schemes may need to comply with local tax requirements in jurisdictions where employees are based, including local limits on benefits. Applying these limits, as well as the new simplified regime for registered schemes, may be administratively complex.
Correspondingly approved schemes
Currently, an employee may obtain relief from tax on employer contributions to a non-UK scheme if:

– the employee is not UK domiciled for tax purposes
– the employee is in receipt of “foreign emoluments” (paid by a non-UK employer)
– the UK Revenue accepts the overseas scheme as “corresponding” to a UK approved scheme. Broadly, this means that certain requirements as to the residence and approval of the scheme must be met, and certain limits on benefits and contributions apply.

The Revenue proposes to replace “corresponding relief” with a system of “migrant relief” from A Day. If “migrant relief” is granted, employees will obtain tax relief on employer contributions in the same way as under the present system.

There are some key differences however:

– relief will be available only where the scheme provides benefits in a form which would be acceptable under a registered scheme. Many correspondingly approved schemes provide 100% cash. It appears this will no longer be permitted
– where migrant relief is given, benefits will be subject to the lifetime allowance and the annual allowance. Currently, the only limit applying to benefits is a maximum pension of 70% of final remuneration after 20 years service. For highly paid employees, this may be worse than their current position. Accrued benefits will, however, be ringfenced from this treatment
– it is not clear whether the requirements for corresponding relief will be applied in their entirety
– the proposals require that the employer is a member of the relevant overseas scheme immediately before coming to the UK. Often this will not be the case (e.g. where an employer sets up a new scheme for a new employee). It is not clear whether the Revenue intends to exclude these arrangements from relief.
– the individual concerned will be responsible for payment of any recovery charge. The charge can be paid when benefits vest (in which case the Revenue must be notified on vesting) or when UK relief ends
– it is not clear whether “migrant relief” will only be available to non-UK domiciled employees as under the present system. The Revenue’s proposals suggest it may be available to any employee coming to the UK.

If schemes do not meet these conditions, they will not be capable of migrant relief.
Overseas transfers

The Revenue proposes to simplify the regime governing overseas transfers:

– transfers can be made from a registered scheme to a pension scheme which is recognised or regulated in its country of establishment

– transfers to other overseas schemes will be treated as unauthorised payments and taxed

– a registered scheme can accept a transfer from an overseas scheme registered or regulated in its country of establishment. So long as the transfer does not include funds which have benefited from UK tax relief, the transfer will not count towards the annual allowance and the benefits provided will not count towards the lifetime allowance

– in all other circumstances, transfers in will count towards the annual allowance and benefits provided will count towards the lifetime allowance.

Together with the changes on eligibility, this may allow some employers to simplify pension arrangements by consolidating UK and overseas arrangements. However, there remains some lack of clarity:

– what is the position where the country of establishment has no regulatory regime?

– what is the position where funds have been transferred from a UK scheme to an overseas scheme and are transferred back? This could arise where the overseas scheme was created by way of transfers from a UK arrangement.

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