EXPLANATORY MEMORANDUM TO

THE PENSION SCHEMES (CATEGORIES OF COUNTRY AND REQUIREMENTS FOR OVERSEAS PENSION SCHEMES AND RECOGNISED OVERSEAS PENSION SCHEMES) (AMENDMENT) REGULATIONS 2012

2012 No. 1221

1. This explanatory memorandum has been prepared by Her Majesty's Revenue and Customs and is laid before the House of Commons by Command of Her Majesty.

2. Purpose of the instrument

This instrument stops certain types of pension schemes established in Guernsey from being eligible to receive tax-free transfers of pension savings from UK registered pension schemes. This strengthens the rules on tax-free transfer of tax-relieved pension savings from the UK to overseas pension schemes. These rules are set out in the Registered Pension Schemes and Overseas Pension Schemes (Miscellaneous Amendments) Regulations 2012 ("S.I. 2012/884").

3. Matters of special interest to the Select Committee on Statutory Instruments

None.

4. Legislative Context

4.1 These Regulations amend the Pension Schemes (Categories of Country and Requirements for Overseas Pension Schemes and Recognised Overseas Pension Schemes) Regulations 2006 (S.I. 2006/206).

4.2 Transfers of UK pension savings that have received tax relief can be transferred free of UK tax to overseas pension schemes which meet the conditions to be a qualifying recognised overseas pension scheme (QROPS).

4.3 S.I. 2006/206 sets out the conditions to be a QROPS. This instrument amends those conditions so that one type of pension scheme established under Guernsey's legislation (section 157E of the Income Tax (Guernsey) Law 1975 - a "157E scheme") will no longer meet the conditions to be a QROPS if it is open to non-residents of Guernsey.

5. Territorial Extent and Application

This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. Policy background

- ***What is being done and why***

7.1 The tax regime for pension savings provides that individuals leaving the UK can transfer their tax-relieved pension savings to another country. The intention is to allow portability of pension savings for migrant workers. Provided the overseas pension scheme receiving the transfer meets certain conditions, the transfer can be made free of UK tax. (This is subject only to a charge on any funds above the lifetime allowance, currently £1.5 million.)

7.2 In order to guard against such transfers being made for tax-motivated reasons, the conditions the recipient overseas scheme must meet are intended broadly to ensure that tax advantages are not available which would not be present if the funds remained in the UK.

7.3 S.I. 2006/206 sets out these conditions, one of which aims to ensure that, as in the UK, benefits payable from the scheme are subject to tax. This reflects the general UK taxation of pension savings, where contributions to and investment growth within the pension scheme are exempt from tax but benefits payable are taxable.

7.4 Some countries had introduced tax regimes designed to attract transfers of non-residents' tax-relieved savings by offering different treatment to residents and non-residents. Under these regimes, residents continued to be taxed on benefits paid out of pension schemes, but non-residents were not subject to tax. This meant that individuals, who had built up their pension savings tax-free in the UK, could transfer their funds to an overseas scheme operating within such a regime and enjoy tax-free benefits paid from the scheme.

7.5 To address this, S.I. 2012/884 introduced a new condition that a pension scheme has to meet to be a QROPS. The condition prevents a scheme from being a QROPS if there is tax relief on a pension paid to a non-resident that is not available to a resident.

7.6 Following the introduction of S.I. 2012/884, the Guernsey Parliament introduced the "157E scheme". The 157E scheme provides for pensions to be paid free of Guernsey tax to residents and non-residents.

7.7 In a paper published on 27 January 2012 and discussed in the Guernsey Parliament on 7 March 2012, it was stated that "these schemes [157E schemes] are unlikely to be attractive to a large proportion of Guernsey resident taxpayers". This is because normal Guernsey residents would not receive tax relief on their contributions to the scheme (nor would a

contributing employer). Also if they wanted to transfer pension savings from an existing Guernsey pension scheme there is a 20% tax charge. This means that, in practice, 157E schemes are a vehicle for non-residents, and would encourage transfers being made from UK schemes primarily for tax reasons.

7.8 On 21 March 2012, the Government announced in the Budget Report that "where the country or territory in which a QROPS is established makes legislation or otherwise creates or uses a pension scheme to provide tax advantages that are not intended to be available under the QROPS rules, the Government will act so that the relevant types of pension scheme in those countries or territories will be excluded from being QROPS."

7.9 This instrument acts to exclude 157E schemes from being QROPS in order to prevent them from being used for tax-motivated transfers from UK tax-relieved pension schemes.

7.10 Regulation 2 amends the conditions that a pension scheme has to meet to be a QROPS so that a 157E scheme that is open to non-residents of Guernsey does not meet the conditions to be a recognised overseas pension scheme. The new provisions will apply from 24 May 2012.

- ***Consolidation***

7.11 The Regulations will amend S.I. 2006/206. They will not be consolidated.

8. Consultation outcome

There was no consultation on these Regulations as they will ensure that existing regulations operate as intended.

9. Guidance

Guidance on the final version of this instrument will be included in the next available update of the HMRC Registered Pension Schemes Manual.

10. Impact

10.1 The legislation will have a negligible impact on business and no impact on charities or voluntary bodies is foreseen.

10.2 There is no impact on the public sector as these Regulations are intended to ensure that the existing regulations operate as intended.

10.3 A Tax Information and Impact Note on transfers of UK pension savings to QROPS was published on 6 December 2011. It remains an accurate summary of the impacts that apply to transfers to QROPS.

10.4 The Tax Information and Impact Note is available on the HMRC website at http://www.hmrc.gov.uk/thelibrary/tiins.htm

11. Regulating small business

The legislation does not apply to UK small business. However, it is intended to prevent those who establish pension schemes in Guernsey under section 157E of the Income Tax (Guernsey) Law 1975 from operating those pension schemes as QROPS if they are open to non-residents of Guernsey.

12. Monitoring & review

The impact of the changes will be monitored through information collected from notifications, information reported, receipts and other statistics.

13. Contact

Beverley Davies at HM Revenue & Customs Tel: 020 7147 2869 or email: pensions.policy@hmrc.gsi.gov.uk can answer any queries regarding the instrument.