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A guide to QNUPS: Qualifying Non-UK Pension Schemes

Introduction

Qualifying non-UK Pension Schemes (QNUPS) were finally confirmed on 15th February 2010 via an HMRC issued 'Statutory Instrument SI 2010/51', following the insertion of a new clause from the Finance Act 2008, ("qualifying non-UK pension scheme" inserted into IHTA 84 by FA2008-S92-Sch29-para 18[8]).

With effect from this date, not only was the tax treatment of certain overseas pension schemes clarified, but it became possible for individuals to make post tax contributions to a QNUPS, whereby providing themselves with a fund which will grow free of Income & Capital Gains tax, and provide valuable additional pension benefits, as well as protection from Inheritance Tax.

As non-UK approved schemes, QNUPS do not automatically confer these benefits, but if properly structured in the right jurisdiction, attractive advantages may be made.

What is a QNUPS?

A QNUPS is an offshore unapproved pension. To qualify, a pension should;

- Be established in a country or territory which regulates pension schemes
- Not provide benefits to the member before the normal retirement age (circa 50)
- Be 'recognised for tax purposes' in the country or territory that it is established
- Be open to residents and non-residents in the country or territory in which it is established

A QNUPS must also satisfy the definition of a pension scheme set out in Section 150 of Finance Act 2004 (FA2004). A QNUPS should also fall within the requirements set out in section 271A Inheritance Tax Act 1984 (IHTA) and Inheritance Tax (Qualifying non-UK Pension Schemes) Regulations 2010 (SI2010/51).

What are the reporting requirements?

A QNUPS, unlike a (Q)ROPS, has no reporting requirements to HMRC. Having not sought approval from HMRC and not being in a position to accept UK pension funds, the only reporting issues to be considered would be the domestic ones in the territory in which it is established.

What is the tax position on contributions?

From a purely UK perspective, contributions to QNUPS generally will be made with post-tax assets, either income or capital. A QNUPS does not qualify for relief under Section 188 Finance Act 2004 (FA2004). If a member is resident in the country in which the QNUPS is established, there may be domestic tax relief available. Please consult your Advisor on this for more information.

There should be no CGT issues where contributions are made from cash. Transfer of actual assets, however, could trigger a taxable gain.

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Generally, no IHT charges arise on transfer of assets by a member to the extent that there is any reduction in the value of 'the estate'. Section 10 IHTA operates to prevent a transfer being a transfer of value where it is "not made ….to confer any gratuitous benefit".

What level of contribution is acceptable?

There are no specific guidelines as to what is deemed reasonable, but when looking at a level of contribution, HMRC will look at what would, in the normal cause of events, be 'usual'.

If funding is disproportionately large, then it would suggest to HMRC that avoidance of taxation was the purpose. Income and gains may then be subject to anti-avoidance measures under Section 261 Income Tax (Trading & Other Income) Act 2005 ("ITTOIA"), section 720 Income Taxes Act 2007 ("ITA") and Sections 86 &b 87 Taxes of Chargeable Gains Act 1992 ("TCGA").

It is therefore very important that either an actuarial report or advice from a suitably qualified independent financial advisor or accountant is obtained before a QNUPS is created and funded. Evidence based contributions are recommended.

What is the Income/Capital Gains tax position within the fund?

In most jurisdictions where QNUPS will be set up, there are no income or capital gains taxes on accrual within the fund, however, this is jurisdictionally dependent.

There are two sets of taxes that could be attributed to a UK settlor. Section 621 ITTOIA requires there to be an element of 'bounty'. HMRC have indicated that where the QNUPS is reasonably funded with beneficiaries who are relatives of the contributor, they would not argue the issue of 'bounty'. Section 720 ITA is subject to a motive defense.

Transfers by a member to a QNUPS should not be caught by the Income Tax anti-avoidance provisions provided that the scheme operates as a true pension fund and is not over-funded.

What is the position in relation to Retirement Benefits?

The retirement options in respect of a QNUPS are as per Section B.4.6 of the Rules for Personal Retirement Schemes issued in terms of the Retirement Act 2011 and as follows.

Initial Cash Lump Sum

Members can commence benefits, irrespective of whether they continue to work, at any time from age 50 and no later than age 75. Members can take up to 30% of their Fund as an Initial Cash Lump Sum.

The remaining benefits after the initial cash lump sum can be used to provide a pension income in one or a combination of the following ways:

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(i) Programmed withdrawals (''PWD'')

The remaining funds after the initial cash lump sum must be used to provide members with a regular pension income payable at least annually, with the maximum annual payment based on the 10 Year Malta Government Bond Yields, the fund size and age at point of initially taking the income. This limit will be reviewed every 3 years until age 75, and annually thereafter.

The maximum annual payment will be available within a twelve-month period of the first calculation and can be taken in a one off payment or by setting up a regular payment at the frequency of the members' choosing.

(ii) Purchase an Annuity

Alternatively, members can elect to purchase a lifetime annuity at any time, by transferring all or part of their remaining Pension Fund to an appropriately licensed Annuity Provider

(iii) Additional Cash Lump Sum (ALS)

After three years from the date of commencement of retirement benefits, members may request an Additional Cash Lump Sum income payment. Thereafter they can make a request annually to take further ALS, subject to the conditions below.

Additional Cash Lump Sum Income can only be paid where at the point of request and based on the members' age, value of the fund and 10 Year Malta Government Bond Yields, we establish that the fund is adequate to generate sufficient retirement income throughout the members' lifetime. If this applies, then 50% of the excess value of the pension fund may be withdrawn as an ALS Income. Sufficient retirement income is defined as the current annual national minimum wage in the country where the member is residing.

A QNUPS is a pension fund and as such is designed to provide you with an income in retirement. Failure to do so, or to take only a nominal income, may involve tax implications as described above.

Note: Advice should be sought from your adviser as to the tax implications on payment of benefits in your country of residence.

What is the Income Tax position on withdrawals?

When making an income payment out to a member of a QNUPS, we will need to ascertain what the members' country of tax residency is. If Malta has a working Double Taxation Agreement with the country in which the member is tax resident at the time of the payment, the payment will be made Gross.

Where there is no working Double Taxation Agreement between Malta and the country in which the member is tax resident, we will have to withhold tax on payments made of up to 35%.

Once the payment is made to the member, it is imperative that the member seeks tax advice on that payment to ensure that the tax situation in their country of residency is assessed and, where necessary, tax is settled directly by the member.

Please consult your advisor for more details on your personal circumstances.

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What is the position on death of the member?

Benefits on death should be treated as 'excluded benefits' for Income tax purposes, and there should be no IHT to pay on funds which, following the death of the member, have not been spent on benefit to the member, provided that there is no choice for the member to receive a pension or instead pass on the value as a death benefit. Careful planning of how assets are transferred on death to beneficiaries needs to be made.

Investment Flexibility

Many QNUPS providers impose investment restrictions, however schemes offered by TMF offer genuine 'open architecture' (investment freedom) within the range of permissible investments:

The Trustees' preference is for a client/advisor to appoint a fund/investment manager to take safe custody of the assets and to act on the investment mandate laid down by the client. This will allow investments to be managed within the following categories:

- Stocks
- Bonds
- Alternative investments
- Hedge funds
- Structured products
- Deposits

In addition, the following asset classes are permitted:

- Private Equity – held indirectly through a separate wholly owned offshore company
- Commercial Real Estate – held indirectly through a separate wholly owned offshore company

Assets can be held in any denomination.

Please be aware that assets that cannot be liquidated to provide you with an income or physical assets that do not provide a regular income stream, will almost certainly invalidate your scheme for IHT purposes.

Other points to consider

Double Tax Treaties: Depending upon the member's country of residence, it may be beneficial to have your QNUPS in a jurisdiction which is protected by tax treaty. Not all countries recognize pension fund structures in non-tax treaty jurisdictions.

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