LONDON & COLONIAL
INNOVATION IN PENSIONS

Press Release

‘Retirement Planner’ Feature - Adam Wrench, Head of Business and Product Development, looks at how QROPS and QNUPS can be used to mitigate any potential tax charges for those in danger of breaching the UK Lifetime Allowance.

Chancellor George Osborne’s decision last December to slash still further the Lifetime Allowance, and with it the limits applicable to the levels of pension savings which qualify for tax relief, came as little surprise to many.

As from April 2014, the maximum amount investors will be allowed to accumulate in their pension fund, without incurring a tax charge on the fund, will drop from the current level of £1.5 million to a new ceiling of £1.25 million – a far cry from the heady days of the £1.8 million limit that applied only a few short years ago (assuming that no protection applies).

This second reduction in as many years now means that those investors fortunate enough to be able build up a pension fund of over £1.25 million face the prospect of an additional tax charge. With this latest reduction, not only will those already in possession of a healthy pension ‘pot’ find themselves in the firing line, but the same will of course apply to those individuals who, as a result of their high earning potential, are now more likely to reach and exceed the new limit over the coming years.

With the original allowance having already been drastically reduced over the last few years there is speculation that further reductions in the Lifetime Allowance may well take place – perhaps even down to the symbolic £1 million “millionaire” level.

So for those who have already worked hard and saved into their pension fund throughout their working life, so as to be able to accumulate a healthy enough pension pot with which to fund a comfortable retirement (as well as for those currently in the process of doing so), the future now looks somewhat less ‘rosy’ than perhaps it once did. What exactly are the options available to those who already find themselves exceeding, or in danger of exceeding, the newly announced limit?

One option would be to stick with a UK pension fund whilst crystallising only the amount equivalent to the lifetime allowance. However, doing so would mean that any remaining funds over the lifetime allowance would eventually trigger a Lifetime allowance tax charge when they reach age 75 and this would be either 25% if taken as pension income or 55% penalty charge if taken as a lump sum.

Under the circumstances described above there is even more reason to consider moving pension funds into a QROPS rather than leaving them behind in the UK. Apart from QROPS being specifically designed for those currently living, or eventually seeking to live, abroad a QROPS can also help to mitigate any further tests against the Lifetime allowance. By transferring an existing UK pension pot into a QROPS, while it is tested against the lifetime allowance on transfer there are no further tests against the lifetime allowance.

Furthermore, by ensuring that any transferred amount is equal to, or less than, the lifetime allowance, no charges would be incurred and the fund would be effectively ring-fenced from any future lifetime allowance taxation charges - regardless of the amount by which the fund may increase in value over the years following the transfer. (However other charges may apply, for example unauthorised payment charges).

In order to illustrate this, consider a client whose current pension is worth £1.2 million and as a result of ongoing contributions the fund is expected soon to be at risk of exceeding the new limit. Now by transferring the full amount of his pension fund into a QROPS, firstly no Lifetime allowance tax charge will be incurred on transfer. Secondly, if the client's fund grows to say £3 million after the transfer then no further BCE takes place and no lifetime allowance charges will be incurred.

The additional benefit also applies on the death of the client. Going back to the previous example whereby the fund has, since the transfer, increased to £3 million, assuming the client dies while within the QROPS then the initial transfer amount will still be subject to the 55% death tax charge however the growth over and above the initial transfer i.e. £1.8 million would not suffer the 55% death tax charge. Whereas had these funds remained in a UK scheme then this would trigger a 55% death tax charge on the whole crystallised fund of £3 million. The simple reason why HMRC has no entitlement to tax the "growth" element on any transferred UK tax relieved funds is that the tax relief on the "gross roll up" has not been provided by HMRC but by the jurisdiction where the QROPS is based.

As the government continues to clamp down on retirement savings, it is becoming increasingly important for both investors and their advisers alike to explore fully all of the options currently available. Not only is this the best way to ensure that any levels of potential taxation are reduced to a minimum, but doing so will ensure that there is more money available in the long term with which to enjoy that well deserved retirement.

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Notes to Editors

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