EXPLANATORY MEMORANDUM TO

THE REGISTERED PENSION SCHEMES AND OVERSEAS PENSION SCHEMES (MISCELLANEOUS AMENDMENTS) REGULATIONS 2012

2012 No. 884

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.

This memorandum contains information for the Select Committee on Statutory Instruments.

2. Purpose of the instrument

2.1 This instrument strengthens the tax provisions relating to the tax-free transfer of pension savings that have received UK tax relief to overseas pension schemes. This is so that the savings are used to provide an income in retirement as intended when the regime was introduced in 2006.

2.2 This instrument also makes consequential amendments to existing regulations as a result of changes in Finance Act 2011 reducing the annual allowance for tax relieved pension saving. This enables non-UK schemes to report to HMRC where they pay an annual allowance charge.

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

3.1 These regulations will be laid before the House of Commons less than 21 days before they enter into force. This is because they cover a complex area of international taxation which has generated significant avoidance activity. Responses to the consultation on the draft regulations continued to be received after the consultation period closed on 31 January 2012. Changes required further detailed consideration and Treasury ministers decided to make a Budget day statement linked to these Regulations to seek to prevent further avoidance activity in this area. It is necessary that the Regulations should still come into force on 6 April 2012 to tackle the avoidance relating to tax-free transfers of pension savings.

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), the Pension Schemes (Information Requirements – Qualifying Overseas Pension Schemes, Qualifying Recognised Overseas Pension Schemes and Corresponding Relief) Regulations 2006 (S.I. 2006/208), the Registered Pension Schemes (Provision of Information) Regulations 2006 (S.I. 2006/567) and the Registered Pension Schemes and Overseas Pensions Schemes (Electronic Communication of Returns and Information) Regulations 2006 (S.I. 2006/570).

4.2 Transfers of UK pension savings that have received tax relief can be transferred free of UK tax to pension schemes established outside the UK that meet the conditions to be a qualifying recognised overseas pension scheme (QROPS). Changes are being made to the legislation to ensure that the system is being used to support pension saving.

4.3 S.I. 2006/206 sets out the conditions that a pension scheme must meet to be an 'overseas pension scheme', which is the first step in a pension scheme meeting the conditions to be a QROPS. This instrument removes one of the two optional conditions relating to the recognition of a pension scheme for tax purposes and makes the other mandatory. This has the effect that a pension scheme must now comply with all of the first three tax recognition conditions. . The conditions a pension scheme must meet to be a recognised overseas pension scheme is the second step. This instrument amends those conditions so that pension schemes where non-residents have a relief that is not available to residents of the country in which the scheme is established will no longer meet the conditions. In addition a different condition will apply to certain pension schemes established in New Zealand. Following the changes some pension schemes that currently meet the conditions to be a QROPS will no longer do so.

4.4 S.I. 2006/208 sets out the information that a scheme manager of a QROPS is required to undertake to provide to meet the scheme's obligations as a QROPS. This instrument amends those requirements. It sets out categories of information that a scheme manager is required to provide and removes the need, in the majority of cases, for the scheme manager, when reporting information, to consider whether the individual is (or has been in the last five full tax years) UK resident. The scheme manager will also have to report all payments out of funds transferred from a UK scheme for a period of 10 years from the transfer of those funds to the QROPS. It also changes the timing of the reporting of information so that a scheme manager of a QROPS has to report a payment within 90 days of the payment being made.

4.5 S.I. 2006/567 sets out the information that must be provided by the registered pension scheme to Her Majesty's Revenue and Customs. This instrument introduces a requirement for an individual making a transfer of pension savings from a registered pension scheme to a QROPS to supply information to the registered pension scheme. There is a new requirement for registered pension schemes to send that information about the individual member, and some extra information, to HMRC. The timing of reporting of information has also changed for a UK scheme. It will have to report a transfer within 60 days of it being made.

4.6 S.I. 2006/570 sets out the information that a pension scheme should provide to HMRC electronically, including information under S.I. 2006/567. Following these changes the report by a registered pension scheme of transfers to QROPS will not have to be provided by electronic communication. Instead the transfer will be reported on a new form APSS262.

4.7 Also under paragraph 8 of Schedule 34 to Finance Act 2004 together with sections 237A to 237F of Finance Act 2004 (inserted by paragraph 15 of Schedule 17 of Finance Act 2011), a member who receives UK tax relief on contributions to a non-UK scheme (called a currently-relieved member of a currently-relieved non-UK scheme) in certain circumstances can require the scheme manager of that scheme to pay an annual allowance charge that arises. This instrument amends S.I. 2006/570 to change the requirement that the return the scheme manager must make of the annual allowance charge paid for the member must be submitted electronically, so that it does not apply to currently-relieved non-UK pension schemes. It means that scheme managers of non-UK schemes will not be required to make an electronic return of UK tax paid. Nor will UK registered pension schemes have to report transfers to QROPS electronically. S.I. 2006/570 is also amended so that scheme administrators can submit amendments to the registered pension scheme return under section 250 Finance Act 2004, to HMRC by paper.

5. Territorial Extent and Application

5.1 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 In April 2006 a new system of tax registration was introduced for UK pension schemes that receive tax relief. Pension tax reliefs are aimed at supporting saving to provide an income in retirement for the pension scheme member and/or their dependants. The pension tax rules set out what payments a registered pension scheme should make to or in respect of a member. These are known as authorised payments. Transfers of pension savings from one registered pension scheme to another are authorised payments and can be made free of UK tax.

7.2 Pensions savings under a registered pension scheme can also be transferred free of UK tax to a qualifying recognised overseas pension scheme (QROPS), subject to the lifetime allowance charge. QROPS is the name given to a pension scheme established overseas that satisfies certain conditions and is broadly similar to a UK registered pension scheme. The conditions that must be met for a scheme to be a QROPS are set out in SI 2006/206. The scheme manager of a QROPS also has to undertake to provide information to HMRC about the funds that have been transferred from a registered pension scheme (or another QROPS).

7.3 QROPS were designed to allow those who are leaving the UK to take their pension savings with them to their new country of residence and provide an income in retirement there. It was intended to be a way of continuing pension saving rather than a method of converting existing pension saving into a lump sum or of escaping taxation on pension savings.

7.4 HMRC has kept this system of overseas transfers of pension savings under review and it has found increasing evidence that the system is being undermined. QROPS are widely marketed as a means of turning pension savings into a tax-free lump sum which is contrary to the principles behind allowing the tax-free transfer of pension savings.

7.5 This instrument amends a number of regulations related to the operation of QROPS. It seeks to tackle attempts to manipulate the rules, while maintaining a workable system of transfers for those who are using the system as intended. The new provisions will apply from 6 April 2012.

7.6 Regulation 3 removes the condition that allows a pension scheme that is not recognised for tax purposes in its country of establishment to meet the conditions as the condition has not been used to satisfy the tax requirement since the regime was introduced in 2006.

7.7 Regulation 4 amends the tax conditions that a pension scheme must meet to be a recognised overseas pension scheme. It removes the distortion that makes a scheme more attractive for non-residents than residents from a tax perspective as it has been used to promote transfers primarily for tax rather than pension saving purposes. Also regulation 4 together with regulations 5 and 6 amend the conditions so that 70% of the funds transferred to certain pension schemes in New Zealand have to be used to provide an income in retirement as pension schemes established in New Zealand have been used to allow individuals to take their pension savings as a lump sum.

7.8 Regulations 8 to 10 amend the information that a QROPS is required to provide under S.I. 2006/208 and the timing of the provision of that information. The regulations make clear that any payment out of transferred funds made within 10 years of the transfer will have to be reported which will mean that in the vast majority of cases a QROPS will not have to decide whether a member is UK resident or has been UK resident at any time in the previous five full tax years. The regulations also set out the categories of information that HMRC may request from a QROPS. The information will have to be provided within 90 days of the payment, rather than after the end of the tax year which is intended to help the QROPS scheme manager who can deal with all related issues at the same time. However, information on when a scheme ceases to be a QROPS must be reported within a new time limit of 30 days. There is also a new requirement to report changes (other than minor changes) and errors as soon as possible.

7.9 Regulations 12 and 13 introduce a new requirement in S.I. 2006/567 for a member requesting a transfer to a QROPS to provide personal information to the registered pension scheme and for the scheme to check that information and send it to HMRC with the other information that is required within 60 days of the transfer taking place. This new requirement will ensure that individuals are aware of the potential tax consequences of the transfer they are requesting before the transfer is made.

7.10 Regulation 15 removes the requirement for a registered pension scheme to report a transfer to a QROPS by electronic communication as required by S.I. 2006/570. A new form APSS262 will be used for the reporting of these transfers which will make it easier to meet the requirement to report transfers within 60 days. It also removes the requirement for scheme managers of overseas schemes to report to HMRC by electronic communications where they pay an individual's annual allowance charge, but instead will report in writing and makes tidying up amendments to allow amendments to the pension scheme return to be sent in writing. Scheme administrators of UK registered pension schemes do not have to send the report on transfers to QROPS (or an amendment of that report) by electronic means.

- ***Consolidation***

7.11 Once finalised the Regulations will amend S.I. 2006/206, S.I. 2006/208, S.I. 2006/567 and S.I. 2006/570. None of the regulations will be consolidated.

8. Consultation outcome

8.1 The draft Regulations were published for comment on the HMRC website on 6 December 2011. Over 50 substantive responses were received, although many were questions on how the new system would work. Some changes have been made to the regulations: the condition that was 'condition 4' now applies to recognised overseas pension schemes rather than overseas pension schemes and the time limits for reporting have been extended from 30 to 60 days for registered pension schemes and from 60 to 90 days for QROPS. These changes to some extent relax the effect of the provisions that were consulted on.

8.2 Regulation 15 relating to the annual allowance was published in draft for comment on the HMRC website on 22 September 2011. No substantive responses were received on the proposed draft legislation and no changes were made as a result of the consultation.

9. Guidance

9.1 Guidance on the final version of this instrument as far as it relates to transfers to QROPS will be included in the next available update of the HMRC Registered Pension Schemes Manual after 6 April 2012.

9.2 Guidance on the effect of the annual allowance changes on scheme managers of non-UK pension schemes has been available on HMRC's website since 14 October 2010 at www.hmrc.gov.uk/pensionschemes/annual-allowance/index.htm.

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 The impact on the public sector is limited to the HMRC. An increased number of reports about overseas transfers will be received. They will contain more information than HMRC is entitled to receive at present. New processes and additional IT capability will be introduced to manage the extra information.

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 A Tax Information and Impact Note for the primary legislation and the element of this instrument relating to a pension scheme paying a member's annual allowance charge and reporting that payment to HMRC was published on 9 December 2010 alongside draft legislation for Finance Bill 2011 concerning the restriction of pensions tax relief. This was updated on 3 March 2011 to reflect further decisions relating to the restriction of pensions tax relief. It remains an accurate summary of the impacts that apply to the overall policy and this instrument.

10.5 The Tax Information and Impact Notes are available on the HMRC website at http://www.hmrc.gov.uk/tiin/tiin650.htm and http://www.hmrc.gov.uk/budget-updates/pensions-tax-relief.pdf.

11. Regulating small business

11.1 The legislation applies to small business.

11.2 To minimise the impact of the requirements on firms employing up to 20 people, the approach taken is to use the contacts and approaches that are already part of the transfer-making process for them.

11.3 The basis for the final decision on what action to take to assist small business is to restrict changes to information that will be provided to them and to use existing processes.

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.