Guernsey
The symbol of international finance

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Why Guernsey is a popular jurisdiction for pension schemes for the mobile client

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The Finance Act 2004 radically changed UK pensions. It heralded a raft of new measures aimed at simplification and came at a time when, across Europe, other jurisdictions were also realising that change was necessary to meet the rising costs of pension provision.

In the UK there had been mis-selling of pension products and several high profile cases of thefts from pensions funds. This coupled with a desire to improve transparency, flexibility and mobility meant that there was generally a welcoming of the provisions which came into force on A Day (6 April 2006).

For those with connections offshore significant improvements were introduced post A Day affecting the mobility of pensions and extending UK tax relief on contributions made to schemes with an overseas connection.

For UK residents retiring overseas, or for non-UK individuals who have worked temporarily in the UK and have accumulated pension contributions in that time, the current pension legislation can be very beneficial.

Prior to 6 April 2006 Guernsey had a reciprocal arrangement with the UK relating to the transfer of pensions rights. HM Revenue and Customs (HMRC) terminated its agreements with the Republic of Ireland, Jersey, Guernsey and the Isle of Man for the transfer of pension rights with effect from that date.

From 6 April 2006 transfers of pensions and payments to the four countries ceased to be subject to HMRC discretion, and individuals no longer had to meet the conditions which had previously applied under the reciprocal agreements. The new rules made it easier to make transfers. In particular it facilitated transfers into Qualifying Recognised Overseas Pension Schemes (QROPS).

In the years since a significant number of pensions have been transferred to these jurisdictions. According to HMRC's list of QROPS, of those which have consented to be listed, Guernsey is the third most popular jurisdiction.

At the top of the list is Australia, followed by Ireland. Australia adopted its own QROPS legislation and subsequently saw the greatest number of transfers. It is possible that this is due to the significant number of UK emigrants, as this has been a popular destination for retiring expats.
Ireland has also been popular but there are specific restrictions on the schemes which can be transferred such that there has to be a genuine Irish connection before the QROPS is 'wholly acceptable' in Ireland.

In Guernsey, however, there are no such restrictions. Furthermore Guernsey offers a well established and highly regulated finance industry and a robust legislative framework to support the pensions industry in the island.

Guernsey has been a premier finance centre for some decades, and its cooperation with various international bodies has been rewarded by its inclusion on the OECD's "white list", issued in April 2009. Guernsey's openness, transparency, and willingness to work with other jurisdictions have enhanced its status in the financial environment.

What type of overseas pension qualifies for special HMRC treatment?

There are different definitions for international pension schemes post A day, as classified by HMRC. An "Overseas Pension Scheme", which is the basis for all qualifying overseas pensions, must satisfy certain criteria. It must provide for benefits to be paid to a member such that it qualifies as a pension scheme and it must be established outside the UK. It has also to be regulated as a pension scheme in the jurisdiction in which it is established and be recognised for tax purposes as such in that territory. It cannot be a registered pension scheme (broadly a UK scheme).

To be a qualifying scheme the scheme must be established in an EU jurisdiction, Norway, Liechtenstein or Iceland. Failing one of these it must be in a country with which the UK has a Double Taxation Agreement that contains exchange of information and non-discrimination provisions.
The type of scheme must be open to residents of the jurisdiction (i.e. not exclusively for non-residents). At least 70% of the fund must be designated to provide an income for life and any benefit (including any lump sum) must be payable no earlier than "normal minimum pension age", currently 50, but increasing to age 55 on and after 6 April 2010.

In addition to a Double Tax Agreement, Guernsey has a Tax Information Exchange Agreement with the UK which satisfies part of the information exchange requirement. Guernsey's pension legislation encapsulates these criteria in the 's157A scheme'. A pension regulated under section 157A of the Guernsey Income Tax Law 1975 provides that:

- The scheme must be approved by the Director of Income Tax in Guernsey, as being a retirement trust;
- It must provide for the payment of an annuity to the individual;
- It must commence the payment of this annuity between age 50 and 75 (unless the Director of Income Tax agrees that the individual is in an occupation where, typically, a person would retire at an age below 50); or
  - (i) In the event of the death of the individual the trust must pay an annuity to the surviving spouse; or
  - (ii) In the event that there is no surviving spouse the trust is payable to some other person, and
- That a maximum tax-free lump sum of no more than 25% of the trust fund can be taken on retirement; and
- Any annuity received from the scheme will be regarded as taxable income in Guernsey and will be taxed as such (at a rate of 20%).

One of the major benefits of a s157A scheme is that an annuity does not need to be purchased at retirement. Instead an amount equivalent to an annuity (based on actuarial values) can be paid from the scheme. As such, therefore the risk of losing the pension pot to a life company on premature death is avoided leaving funds available to support surviving spouses and others.

During the life of the pension scheme any income earned by it is tax free. Capital gains tax does not exist in Guernsey. Pension withdrawals are subject to Guernsey tax at a rate of 20% and the tax is deducted at source and paid away to the Administrator of Income Tax by the scheme administrator. The s157A scheme has all the necessary attributes to qualify as a QROPS. It is therefore eligible to receive transfers of pensions from the UK. As stated above the number of QROPS listed as being administered in Guernsey, on the HMRC website, attests to the suitability of Guernsey in this respect.

Transfers of UK pensions

Individuals who have been resident in the UK for any period of time and who have been contributing to a UK pension, who then move abroad, may be able to commute their UK pension into an overseas scheme without losing any of the tax relief previously granted.

To ensure the payments retain their eligibility for relief at the time the transfer to the overseas scheme is made (and for a period after this – see below) the receiving scheme must be a Qualifying Recognised Overseas Pension Scheme (QROPS) such as a Guernsey s157A scheme.
To satisfy this status the scheme must evidence the same criteria as for a Qualifying Overseas Pension Scheme. That is that it must prove that at least 70% of the UK tax-relieved transferred amounts would be designated to provide an income for life, and that benefits (including any lump sum payment) are payable no earlier than the "normal minimum pension age".

Furthermore the scheme manager must have notified HMRC that the scheme is a recognised overseas pension scheme, and have provided evidence of that if required. He must have undertaken to notify HMRC if the scheme ceases to be a recognised overseas pension scheme, and also to provide HMRC with specific information if and when payments are made in respect of certain scheme members. Provided scheme managers report any event or payment which crystallises a charge during the period of 5 years after the scheme is transferred overseas, and meet HMRC criteria for the provision of information, the scheme should avoid a claw-back of previously granted UK tax relief.

Counteracting abuse

In the period immediately after A day there were reports of abuse occurring. In some territories the transferred pension stayed for only a brief period in the receiving scheme, before that scheme was wound up and the assets distributed. Clearly this went against UK legislation but HMRC was unable to claw back the tax relief previously granted, due to the jurisdictional separation. Moreover this went against the spirit of pension provision, at a time when many jurisdictions were working hard to encourage and foster the habit of pension saving.

The consequence of persistent abuse would have been for HMRC to rescind the ability to transfer pensions overseas, and it was recognised that this was a step backwards.

To demonstrate its commitment to the UK legislation and its support of the regime Guernsey introduced a number of ancillary measures and protections. Some of these were done in association with HMRC. One of these changes was that additional conditions are now imposed on the approval of any s157A scheme which can admit non-Guernsey residents as scheme members. The measure was specifically designed to prevent Guernsey schemes being collapsed after the inward transfer of funds from the UK. In addition transfers of Guernsey QROPS funds, which had received inward transfers from the UK , to some other jurisdiction which might then allow the scheme to be terminated, was prevented. Guernsey cannot be used as a conduit.

In addition any difference in treatment between schemes established for Guernsey residents and those established to receive inward transfers were removed. Previously there might have been some flexibility regarding the retirement age applied to the scheme for the non-resident, or a lump sum of greater than 25% (perhaps based on calculations which might have been applicable in the UK), but this is no longer the case.

Contributions in respect of UK earnings made to foreign schemes

For pensions with an overseas connection there is more relief offered than simply for those leaving the UK. Where individuals have lived and set up pensions overseas but then spend some time working in the UK, UK tax relief may be granted on the contribution from UK earnings to the scheme (subject to limits).

This will apply provided the scheme member is a Relevant Migrant Member, and the pension scheme is a Qualifying Overseas Pension Scheme (not necessarily a Qualifying Recognised Overseas Pension). These pensions are often known as International Pension Plans (IPP). The member must be in receipt of relevant UK earnings. Moreover relief may also be granted on contributions made by an employer to that scheme.

A Relevant Migrant Member is an employee who was not resident in the UK when he became a member of the scheme. The relevant contributions are those made to the scheme in respect of periods when he was resident in the UK. Tax relief is only granted on contributions to the scheme which would have been subject to relief, in the jurisdiction in which the member was resident, before he came to the UK. Relief will also only be granted if the scheme manager agrees to notify HMRC if there is any payment or circumstance which crystallises an event which needs to be reported to HMRC. Guernsey has a scheme with all the necessary attributes to qualify as an IPP, and it is specifically exempted from Guernsey tax. This is defined under s40(ee) of the Guernsey Income Tax Law 1975.

The income derived from investments and deposits of the scheme are exempted provided the scheme was established in Guernsey in connection with the carrying on of a business or the exercise of functions wholly outside of Guernsey. Payments made by the scheme need not have Guernsey tax deducted at source from them, nor are the payments taxable in Guernsey.

Finally in the armoury of pensions available in Guernsey for non-residents there is the s40(o) scheme for corporate international pension schemes. These are schemes that are based in Guernsey to benefit non-resident members who are usually employed by an international company, and operate in many different jurisdictions. These are well-known in the pension industry and have been in existence for some time.

In summary

If you are a mobile executive, a person moving temporarily to the UK to work or someone leaving the UK for retirement, creating a pension in Guernsey may be a way to maximise retirement planning opportunities while in the UK without being left with a pension subject to UK tax on retirement. Such a scheme allows for a consistent and unbroken investment policy and avoids fractured, small pension pots, scattered in different jurisdictions.

Not only does Guernsey have a wealth of legislation to support the establishment, transfer into and maintenance of a pension in Guernsey, but it has the strong finance industry support to help good financial performance and investment management. Moreover the States of Guernsey is committed to ensure there is no abuse of the arrangements with the UK and those in the industry support this. Guernsey has created a strong foundation in this field.