



Trusts and Fiduciary

QROP Schemes - The Pertinent Issues

QROP schemes a few years on – some pertinent issues

Whilst many trustees and providers are now familiar with the QROPS regime, as schemes mature and members seek to avail themselves of the funds in their schemes in various ways, important questions are arising in relation to matters as diverse as the level and age on which benefits can be taken, how to align Guernsey and English taxation requirements and what restrictions apply in respect of investments and the granting of loans.

It is by now widely known that the consequences of not complying with the laws and regulations applicable to QROPS can be very damaging, as unauthorised payment charges and surcharges, as well as scheme sanction payments, can amount to a 70% tax charge. It is therefore immensely important for trustees and providers to ensure they understand the rules relating to how the funds in QROPS can be properly applied.

In this note we have sought to identify some of the most pertinent and frequently raised issues arising in relation to the QROPS regime. We would encourage all providers and trustees to consider the issues raised in order to ensure they do not fall foul of the rules and regulations and discharge their fiduciary obligations.

1. Does registration of a scheme as a QROPS by HMRC mean that HMRC has approved the scheme?

The simple answer to this question is that HMRC does not approve QROP schemes. The form that providers need to send to HMRC to achieve QROPS registration functions merely to notify HMRC that the scheme is a QROPS in accordance with sections 150(8) and 169 of the Finance Act 2004. The form does not provide for the submission of scheme documentation, so HMRC does not verify whether the requirements for QROPS status are in fact met. Providers are required to ensure that the scheme is compliant and qualifies as a

QROPS – it is a form of self-certification. Providers are also required to administer the scheme in compliance with the said sections of the Finance Act. Scheme marketing materials should not state that the scheme is HMRC approved, but rather that it is registered with HMRC as a QROPS.

2. Loans from QROPS

The documentation of many QROPS permits the trustees to make loans to members. However when members ask for loans from schemes, many trustees question whether they can grant such loans and whether a member's length of non-UK residency affects this.

The RATS Code of Practice permits the making of loans subject to certain conditions (the loan must be secured, constitute no more than 30% of the member's fund, be repaid before benefits under the scheme may be taken, and a commercial rate of interest must be charged). The position is therefore clear with respect to Guernsey members with no UK-transferred funds.

However loans made from QROPS in respect of members with UK-transfer funds constitute unauthorised member payments under the Finance Act 2004 and associated regulations and, as such, are reportable to HMRC. Unauthorised payments are likely to give rise to adverse tax charges in the form of unauthorised payment charges.

However the UK QROPS notification requirements are disapplied in respect of members to whom the member payment provisions do not apply. The member payment provisions do not apply to members unless they are resident in the UK when the payment is made or, although not resident in the UK at that time, have been resident in the UK earlier in the tax year in which the payment is made (or treated as made) or in any of the five tax years immediately preceding that tax year.

This would suggest that after a five year period of non UK residence,

the making of loans will not trigger an unauthorised payment charge, and the loan would not be a reportable event (but note that it would still need to meet the loan conditions contained in the RATS Rules). However it is advisable for trustees to require members to obtain independent tax advice before agreeing to make a loan.

3. Minimum retirement age

Questions frequently arise about the minimum retirement age from which a member can take his pension, particularly in respect of Guernsey members of a QROPS with no UK-transferred funds. The minimum retirement age in respect of Guernsey RATs schemes is age 50, however the UK minimum retirement age is age 55. The UK Overseas Pension Schemes and Regulated Overseas Pension Schemes) Regulations 2006 (SI 2006/206) (the “QROPS Regulations”) provide specifically that payments to members under the scheme (rather than UK-transferred funds only) must be payable to the member no earlier than if so-called “pension rule 1” in section 165(1) of the Finance Act were to apply. Pension rule 1 specifies that the minimum retirement age is age 55. Therefore, the minimum retirement age must be age 55 for all members, both because of the requirements of the QROPS Regulations and because the equal treatment of members is a condition of section 157A Approval.

4. Commutation limits

As schemes mature and members seek to commute their pensions, queries frequently arise in relation to the level of commutation permitted under QROPS and the age from which commutation is permissible.

Whilst the commutation limit in the UK is 25%, QROPS Regulations permit commutation of up to 30% of the UK transfer fund but only after age 55. No commutation is permitted prior to age 55 nor may any part of the balance of 70% of the UK transfer fund be commuted. However we would strongly recommend that English tax advice is

obtained before making a lump sum payment.

5. What makes a scheme investment regulated?

Where members can ‘direct, influence or advise’ on the manner in which their fund is invested, a scheme is considered to be an investment regulated pension scheme. Specifying a preference for certain types of investments either to an investment adviser or to the trustee, or selecting the funds in which they can invest, would in our view constitute ‘directing, influencing or advising’ for the purposes of the legislation.

It is important to understand that whether a member has directed, influenced or advised is a question of fact. The scheme may not explicitly state that a member may make an investment selection (indeed, unless a member is aware of and consents to being subject to the consequences of his scheme being investment regulated, we would advise schemes not to give members such powers), but the absence of such language does not preclude the scheme from being investment regulated.

The legislation does not specify who the member needs to be able to influence, advise or direct for the scheme to be considered investment regulated. The test is whether the manner of investment can be directed, influenced or advised upon directly or indirectly by the member. Some providers erroneously believe that if the trustee delegates investment powers to an investment adviser whom the member is capable of influencing, advising or directing, the scheme would not be investment regulated. However a scheme may be considered to be investment regulated where a trustee appoints a member’s financial adviser as a financial adviser to the scheme unless the financial adviser is engaged upon terms where he cannot be (and in fact is not) influenced, advised or directed as to investment selections by the member. Where members can make investment selections (whether to an adviser or to the trustee) in respect of their fund, the scheme will be investment regulated.

6. What is the consequence of a scheme being investment regulated?

An investment regulated pension scheme is to be treated as making an unauthorised payment (resulting in adverse tax charges) to a member if the scheme acquires an interest in or improves taxable property, which comprises residential property and tangible moveable property. The term 'tangible moveable property' is not defined in the legislation but is understood to include objects such as boats, art, fine wine etc. There are some very limited exceptions to the tangible moveable property restrictions, and these must be carefully analysed to see if they apply to a particular situation.

Furthermore, the QROPS reporting obligations subsist beyond the five year non-residency period in respect of investment regulated pension schemes – there is no cut-off reporting period for investment regulated schemes.

7. For how long are QROPS members bound by HMRC's notification requirements?

The QROPS notification requirements are disapplied in respect of members to whom the member payment provisions do not apply. The member payment provisions do not apply to members unless they are resident in the UK when the payment is made or, although not resident in the UK at that time, have been resident in the UK earlier in the tax year in which the payment is made (or treated as made) or in any of the five tax years immediately preceding that tax year.

However the notification requirements subsist beyond the five year period in respect of investment regulated pension schemes.

8. Which triviality levels should I be applying in my scheme?

Many trustees have identified the fact that triviality limits in the UK are lower than those in Guernsey, and that triviality payments can be made without incurring unauthorised payment charges only once a member has reached age 60.

This has given rise to questions as to the triviality limits that should be applied in QROPS. We have been unable to identify any provisions which apply the UK triviality provisions to QROPS, however it is without a doubt the safest route to apply the UK triviality rules at least with respect to the UK Transfer Fund.

9. Is it possible to administer QROP Schemes as single rather than multi-member schemes?

Trustees often seek to understand whether it is possible to establish QROP Schemes for single clients, or for joint members (a married couple, for example) and restrict entry to any other members.

One of the main criteria for obtaining QROPS status is that schemes need to be "open to persons resident in the country or territory where they are established" (Condition 1). The QROPS Regulations do not explain what is meant by the words "open to". Does it mean "available to" or should it be demonstrably open in the sense that the scheme either has locally resident members or is actively marketed as being open to locally resident members? The regulations are unfortunately not clear.

However if the single member or joint members are Guernsey resident, then it seems the scheme can be shown to be open to local residents (Condition 1 does not require schemes to be permanently open to local residents, as the legislation cannot have been intended to prevent trustees from being able to close schemes). Therefore it appears to be possible to administer QROP Schemes as single (or joint) member schemes rather than multi-member schemes, but only if the member(s) are Guernsey resident.

It is however doubtful whether single member schemes where that single member is not Guernsey resident would meet the criteria. Even if the scheme rules would permit admission of local members but the scheme is administered (or promoted) in a way such that it is clear that there is no intention to admit local members, its QROPS status would be open to challenge.

Please note that this briefing is only intended to provide a very general overview of the matters to which it relates. It is not intended as legal advice and should not be relied on as such. Legal and tax advice should be sought by trustees and pension providers to deal with specific queries.

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