

Sneaky pension planning

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You may well be aware of the government's full frontal assault on legitimate pension planning as a result of restricting higher rate tax relief for those with earnings in excess of £150,000. You may not, however, be aware of a totally legitimate way of completely side stepping these draconian restrictions, and securing some very significant tax relief on your hard earned cash, as long as you carry out your working duties outside of the United Kingdom (UK) and qualify as UK non-resident.

The benefits

Assuming that you qualify for this planning here's what you can look forward to:


- Substantial employer contributions are permitted and are fully allowable against Corporation Tax in the UK;
- Usually no tax liability or social security costs on the employee on the contributions made;
- Benefits may be taken **entirely as a tax free lump sum** by UK residents;
- Benefits available from age 55, although they may be taken **earlier than 55** if the member is leaving service or a material change is made to employment terms;
- Funds grow in a **tax free** environment;
- The plan assets do not form part of the member's estate for UK inheritance tax;
- There is no need to take an annuity or benefits at age 75;
- The plan assets can be invested in a very wide choice of assets, including residential or commercial property, equity holdings, investment funds and cash deposits.

Overseas activities

Any type of worker can take advantage of this planning if they carry out some or all of their work duties outside of the UK, whether that is on a short or long term basis. The four broad categories of people who can benefit are:

- Any employee of a UK Limited Company whose duties are conducted wholly outside the UK.
- Executives of multi-national employers of overseas parentage with a UK presence.
- Self employed or contracting expatriates, of any nationality, who are working in any country other than the UK.
- UK resident Executives of a UK Limited Company who conduct specific duties outside the UK amongst their other UK duties.

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If you are a self-employed individual who would otherwise qualify for this planning then you can take advantage by either forming a UK employment structure or joining an umbrella employment structure from one of the specialist providers in this market.

A special type of pension Trust

In order to secure these tax benefits, an employer (which can be a special purpose vehicle established for this purpose) establishes a special type of irrevocable trust. The sole purpose of this trust is to provide superannuation benefits for non-resident employees whose business is undertaken wholly or in part outside of the UK. The trust is constituted under s615(6) of the Income and Corporation Taxes Act 1988.

Each trust must have either the employer or a UK trust corporation as the trustee and satisfy the criteria established by the Pension Scheme Office Overseas Schemes Section. As such each scheme is submitted to, and accepted by, the Overseas Pension Section, ensuring that the benefits will not subsequently be subject to challenge. This grants full pension scheme status to the trust, which is recognised internationally as a genuine **pension arrangement**.

Although Her Majesty's Revenue and Customs (HMRC) grants acceptance status to the Pension Trust, it is **not a UK approved pension scheme** and thus is not subject to all the rules of registered pension schemes, such as lifetime allowance, special annual allowances etc.. However, once HMRC has granted acceptance of the trust, all employer contributions are fully deductible against UK corporation tax subject to in the UK in the same way that contributions to a UK occupational pension scheme would be. Unlike with registered pension schemes there is no spreading of tax relief for large single contributions. However, the wholly and exclusively test will apply for corporation tax returns.

For example, if someone worked for a company they controlled and had accumulated £3,000,000 in the company whilst paying themselves a salary of £100,000 to date, then continued with the salary but made a one off pension contribution of £3,000,000, it is likely that the company's tax inspector would be tempted to disallow some of the contribution. There is no specific funding restriction on contributions - 10 times salary would not give rise to any difficulties - which makes salary sacrifice a powerful tool.


Whether the worker will be subject to UK taxation or not on their overseas earnings or any employer contribution to the pension trust will depend on their residency status, which will be determined by a number of factors including time spent out of the UK. To avoid UK income tax and National Insurance on the pension trust contribution, the member needs to be non UK resident, otherwise it will be taxed as would any other emolument.

If the individual is not subject to UK tax on overseas earnings, he or she faces the possibility of being taxed in the country in which they are working. Not everyone can work in low taxed jurisdictions and countries based in the European Union can have tax rates comparable with or even higher than the UK's. For non UK resident individuals the Special Pension Trust maximises the tax savings by avoiding UK tax and, in most jurisdictions, avoiding local taxes on the pension contribution, in the country where the member is working.

A French Affair

The following example is based on an individual seconded to work in France, and the significant tax savings afforded by the pension trust.

Employer	Do nothing €	s615(6) €	Saving €
Gross Salary	500,000	100,000	
s615(6) Contribution	-	400,000	
Social Contributions	103,295	22,895	<u>80,400</u>
Total Cost	<u>603,295</u>	<u>522,895</u>	
Employee			
Social Costs	45,263	18,146	
Income Tax	166,020	11,930	
Net Income	288,717	69,924	
Section 615(6) Contribution	-	400,000	
Salary + Pension Value	<u>288,717</u>	<u>469,924</u>	<u>181,287</u>
			<u>261,607</u>
Percentage of Gross salary Received	57.7%	94%	
Percentage of Ers Outlay Received	47.9%	89.9%	



Even if one has managed to avoid UK tax on earnings arising from overseas work, and paid little or no tax in the country of residence, there is still the problem of UK income and capital gains tax arising on those funds which have been saved, when one eventually returns to live in the UK. Even those who anticipate retiring abroad might find they need to return to live in the UK if medical needs are such that staying abroad is not viable. The tax 'drag' on long-term investment returns can be significant, particularly at the UK's top income tax rate of 50%. The Special Pension Trust allows one to avoid such taxes completely.

That age 75 thing

Because there is no provision for changes to taxation treatment at age 75 under the Special Pension Trust, HMRC are powerless to change the income tax treatment on irregular distributions of capital nor levy inheritance tax on any benefits payable upon death to beneficiaries. However, getting written confirmation on this point from HMRC is like getting blood out of a stone. Certainly no annuity needs to be purchased and there is no restriction to the cash sum available.

The member could also establish a separate UK lifetime trust specifically for the purpose of receiving any death benefits that would arise before taking benefits under the Special Pension Trust, in this case the member would need to complete a nomination of beneficiary declaration for the trustees of his Special Pension Trust in favour of that lifetime trust. Because the death benefits would be free of IHT they could pass into the lifetime trust tax free and thus shield the capital from 'hostile' creditors including IHT on the estates of the beneficiaries, while allowing them to benefit by way of loans from the trust.

To make this type of planning viable the employer needs to be making contributions of at least £50,000 per annum per scheme. If the employer isn't keen to act as the trustee then they can outsource this to a UK trust company for a modest fee. Active membership of an employer's UK registered pension scheme may continue for an individual who is working overseas for up to 10 years and has no impact on eligibility to join the Pension Trust.

If the forthcoming increases in taxation are tempting you to leave the UK to work abroad then now you know how to preserve as much of those earnings as possible, such that they remain completely free of income, capital gains and IHT when you return to the UK.

For further information please get in touch with your usual Bloomsbury contact, telephone 0207 194 7830 and ask for a member of the wealth team or alternatively e-mail info@bloomsburyfp.co.uk.

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