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2 February 2017

Her Majesty's Revenue & Customs

Pension Scheme Administration

Overseas Pension Schemes

e-mail: pensions.policy@hmrc.gsi.gov.uk

Dear Sir \ Madam,

Re: Consultation on changes to conditions to be an 'overseas pension scheme'

The Association of Superannuation Funds of Australia (ASFA) would like to lodge this submission in response to the United Kingdom (UK) Government's consultation on the changes to the conditions to be an 'overseas pension scheme' and a 'recognised overseas pension scheme'. Draft guidance with respect to this was published on 5 December 2016 and updated on 3 January 2017.

ASFA is a non-profit, non-political national organisation whose mission is to continuously improve the superannuation system so people can live in retirement with increasing prosperity. We focus on the issues that affect the entire Australian superannuation system. Our membership, which includes corporate, public sector, industry and retail superannuation funds, plus self-managed superannuation funds and small APRA funds through our service provider membership, represents over 90 per cent of the 14.8 million Australians with superannuation.

Comments

Thank you for the opportunity to provide comments on the changes to the conditions to be an 'overseas pension scheme' and a 'recognised overseas pension scheme'.

ASFA represents a number of superannuation funds that were QROPS prior to the 6 April 2015 changes (former QROPS)) We broadly welcome the changes to the conditions which a scheme must meet, with effect from 6 April 2017, to be considered to be a QROPS. The changes generally strike an appropriate balance between endeavoring to ensure that UK tax relieved money is preserved for the member's retirement, while generally accommodating the diverse range of overseas regulatory regimes and scheme benefit designs.

Having said that, some former QROPS have identified and raised with us the following issues with respect to the revised UK overseas pensions regime.

1. Consideration of amendment to permit ‘quarantining’ of UK tax relieved monies

One change which would significantly enhance outcomes would be permitting QROPS to ‘quarantine’ UK tax relieved pension monies from those monies which have been contributed to the scheme from within that jurisdiction or from other sources. This would more readily facilitate the overseas scheme restricting access to the UK tax relieved monies in accordance with the UK ROPS legislation.

Currently any withdrawal from a scheme which contains any money transferred from the UK is deemed to have been derived first from the UK transfer amount, irrespective of whether the UK transfer monies are in a separate account. We understand that the underlying policy rationale for this is that this ensures that any liability to UK tax is extinguished at the earliest opportunity.

The majority of overseas schemes will also hold amounts accumulated from contributions or other sources which have no connection to the UK. The overseas regulatory regime may permit the payment of a part benefit, prior to retirement age, in circumstances which would not be considered to meet the UK pension age test.

Provided the overseas regulatory regime only permitted the payment of these benefits, and did not mandate them, it would be open to the trustees/operators of the overseas scheme to amend their governing rules to the effect that any member with any UK tax relieved monies would be unable to access such payments. By virtue of the operation of the deeming rule, this would need to apply irrespective of the amount of non UK tax relieved monies in the scheme.

Trustee/operators, however, may be reluctant, or even unable, to amend their governing rules on such a basis, especially if it were to have retrospective effect. In particular, trustees/operators may not consider it appropriate that members who have transferred UK tax relieved monies, who find themselves in adverse circumstance, are denied access to payments which are available to all other members of the scheme and which could be funded from the member’s non UK sourced money, leaving the UK tax relieved amount unaffected.

It is worth noting that, had a member transferred the UK tax relieved monies into one overseas scheme and contributed to a second, separate, scheme, the making of a payment which did not meet the pension age test from the second scheme would not contravene the UK ROPS legislation. It could be argued that this outcome, as a result of the UK tax relieved monies being in a separate scheme, is a matter of ‘form over substance’ and, as such, unfair as between two members where the only difference between them is whether the UK and locally sourced amount are in the same or different schemes.

Accordingly, in ASFA’s view, if the deeming rule were to be amended to permit the ‘quarantining’ of UK tax relieved pension monies from those monies contributed to the scheme from within the overseas jurisdiction or other sources, this would facilitate the overseas scheme being able to more readily restrict member access to UK tax relieved monies.

2. New regulatory requirements test

From 6 April 2017, how a scheme satisfies the regulatory requirements test will depend on whether it is an occupational pension scheme. Under both circumstances the test will be met if a scheme is regulated by the regulatory authority of such schemes.

In Australia the main regulatory authorities are

- for 'registrable superannuation entities' (RSEs) - the Australian Prudential Regulation Authority (APRA)
- for self-managed superannuation funds (SMSFs) - the Australian Taxation Office (ATO).

Former QROPS have sought confirmation from HMRC of their interpretation that all RSEs and SMSFs, as they are regulated, will satisfy the regulatory requirements test.

3. Pension age test - serious ill-health

In Australia the payment types set out in the table below are permitted to be made to a member aged under 55.

	Type of release	Background	Comment
1	Terminal illness <i>Superannuation Industry (Supervision) Regulations 1994 (SIS regs)</i> Schedule 1 – Conditions of release – item 102A	Funds are permitted to release a member's benefit if the member is able to obtain certificates from two medical practitioners (including one specialist) stating they have <ul style="list-style-type: none"> • a terminal illness; and • a life expectancy of less than 24 months 	We believe that release before 55 on these grounds is consistent with the principles which underpin the UK pension age test
2	Total and permanent incapacity SIS regs Schedule 1 – Conditions of release – item 103	Funds are permitted to release a member's benefit if the fund is reasonably satisfied the member is unlikely, because of ill health, to engage in gainful employment for which the member is reasonably qualified by education, training or experience.	
3	Temporary incapacity SIS regs Schedule 1 – Conditions of release – item 109	Funds are permitted to release a member's benefits where the member has ceased to be gainfully employed due to ill-health, even though the member may not be permanently incapacitated. It must be in the form of a non-commutable income stream for: <ul style="list-style-type: none"> • the purpose of continuing (in whole or part) the gain or reward which the member was receiving; and • a period not exceeding the period of incapacity from employment of the kind engaged in immediately before the temporary incapacity Virtually all funds insure this benefit through a group insurance policy, and the benefit payments are made directly from the insurance company to the member, such that the member's benefit in the fund is unaffected.	

We respectfully request that HMRC confirm whether the payments in the above table will be considered to satisfy the pension age test.

In particular we note that: -

1. Terminal illness benefit
 - is not conditional upon the member ceasing employment
 - can be made where the member has a life expectancy of less than 24 months (as opposed to the UK where life expectancy must be less than 12 months).
2. Total and permanent incapacity would appear to be equivalent to retiring due to ill-health
3. Temporary incapacity
 - is not conditional upon the member ceasing employment
 - must be in the form of a non-commutable income stream.

If the terminal illness benefit and/or the temporary incapacity benefit are not considered to meet the pension age test we respectfully ask HMRC to consider granting some form of relief or exemption to Australian schemes to the extent that

- a terminal illness benefit can be paid with respect to a 24 month period of life expectancy; and/or
- a temporary incapacity benefit is funded from the proceeds of an insurance policy and not from the member's benefit in the scheme.

4. Pension age test - refund of excess contribution lump sum

In Australia there are restrictions on the amount members can contribute to superannuation within a given financial year.

If a person exceeds their

- 'concessional contributions cap' (before tax contributions) – the excess amount will be included in their personal taxable income and taxed at their marginal rate, and they can choose to release up to 85% of the excess contributions from their superannuation fund
- 'non-concessional contribution cap' (i.e. contributions generally funded from after tax monies, including the transfer of UK tax relieved monies) - they can choose to release their excess contributions, as well as 85 per cent of relevant earnings (the remaining 15 per cent is paid as tax). A person who does not withdraw the excess contributions is subject to excess contributions tax at the top marginal tax rate and the amount of this tax must be withdrawn from the individual's superannuation account. From 1 July 2018 such withdrawals will only be permitted to be made to the ATO, rather than to the member, and will be used to offset the individual's tax liabilities.

This mechanism appears to be comparable to a 'refund of excess contribution lump sum' from a UK registered scheme.

Accordingly, we respectfully request that HMRC confirm that the release of excess contributions (and earnings) is considered to be a 'refund of excess contribution lump sum'.

5. Pension age test - other mandatory payments under Australian law

For Australian superannuation funds there are additional, mandatory, payments. We consider these either are consistent with the requirements of the new pension age test or at least are not inconsistent with the policy rationale underlying the test. These types of payments are listed below.

	Type of release	Background	Comments
1	Transfer of small, lost & insoluble accounts to ATO SIS regs Schedule 1 - Conditions of release - item 103B	Legislation requires trustees to transfer accounts which are <ul style="list-style-type: none"> • small and lost (up to \$6,000); or • insoluble (unidentifiable) to the ATO. These amounts are held by the ATO until such time as they are claimed by the member. Unless the member has reached age 65 years and retired the ATO is required to pay the money back into the member's superannuation fund.	We do not believe this provision is inconsistent with the UK pension age test as: <ul style="list-style-type: none"> • accounts are paid to the ATO, not to the member • the funds are held by the ATO on behalf of the member until such time as the member claims the amount • the amount must be paid into the member's super fund, unless the member is aged 65.
2	Payment of super tax liabilities to the ATO SIS regs Schedule 1 – Conditions of release - items 111B, 111C, 112 & 112A	In some circumstances members are able to\must pay super tax liabilities using funds held in their super accounts. The most common example is payment of 'Division 293 tax', an additional 15 per cent tax on pre-tax contributions imposed on members with an annual taxable income in excess of \$300,000. This is implemented pursuant to a 'release authority' issued to the member\fund by the ATO. It is mandatory for a super fund to comply with a 'release authority'.	We do not believe that the release of funds on receipt of a mandatory release authority from the ATO is inconsistent with the policy rationale underpinning the UK pension age test.
3	Court orders\family law agreements (family law settlements, proceeds of crime orders & orders in favour of a trustee in bankruptcy) SIS regs Part 7A (family Law) <i>Superannuation Industry (Supervision) Act 1993</i> (SIS Act), sub-section 6.17(2C) (proceeds of crime) SIS Act, section 349A (bankruptcy)	Super funds must in limited circumstances release funds from a person's super account pursuant to a court order or family law settlement. This includes <ol style="list-style-type: none"> 1. family law – court order or settlement 2. proceeds of crime - court order 3. bankruptcy - court order. The later two are extremely rare and only are available where contributions were made <ul style="list-style-type: none"> • from the proceeds of crime; or • to prevent assets being available to creditors and\or to defeat the trustee in bankruptcy respectively.	We do not believe that the release of super in response to a court order or family law settlement (which must be complied with by the trustee) is inconsistent with the policy principles underpinning the UK pension age test.

Accordingly, we respectfully request that HMRC confirm whether it is able to treat the above payments as authorised payments for the purposes of the new pension age test. If not then, if this is possible, we respectfully request that HMRC consider granting limited relief or an exemption to Australian schemes to allow the above payments to be made in respect to members before they turn age 55.

6. The ability for Australian superannuation funds to be ROPS

A number of Australian superannuation funds, including some large funds that were ROPS\QROPS prior to 6 April 2015, are keen to work with HMRC to better understand whether, given the Australian regulatory regime, amendment to their scheme rules can be sufficient to satisfy the new pension age test. This would facilitate transfers to Australian superannuation funds for individuals below age 55, as well as the current position with respect to members who are aged 55 or over.

The mass loss of ROPS status for Australian superannuation funds (other than public sector schemes and those confining membership to those aged 55 and over) has placed a restriction on the ability of member to be able to transfer their superannuation between schemes – an inherent feature of the Australian superannuation system. Accordingly, we respectfully request that HMRC give consideration to introducing some flexibility in respect of potentially permitting members to transfer benefits between former ROPS\QROPS as these would continue to be subject to the reporting obligations.

7. Conclusion

We would like to thank you for the opportunity to provide comments on the changes to the conditions to be an 'overseas pension scheme' and would welcome the opportunity to discuss with HMRC the matters raised in this submission.

Ultimately we would like to be able to reach an understanding as to whether

- given the Australian regulatory regime; and
- subject to necessary amendments to scheme rules being effected

Australian superannuation funds could be considered to be capable of meeting the new pension age test and, accordingly, able to be granted ROPS status.

Should you have any questions on any of the matters raised in this submission please do not hesitate to contact me on +61(0)3 9225 4021 or +61(0)431 490 240 or via fgalbraith@superannuation.asn.au.

Yours faithfully

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