

UK PENSION SCHEMES – THE IMPACT OF BREXIT



Chase Buchanan

PRIVATE WEALTH MANAGEMENT

UK Pension Schemes – The Impact of Brexit

What does the future hold for British nationals retiring in Europe?

Introduction

With around half a million UK nationals living out their retirement in the sunnier climes of Europe, Chase Buchanan explores how the landscape will change once the Transition Period ends on 31st December 2020.

Europe has long been a popular retirement destination, with countries such as France, Spain and Portugal offering a calm pace of life, comfortable weather and peaceful retirement.

However, for many British citizens approaching retirement the advent of Brexit seems to be putting a dent in those aspirations.

A key concern is in regard to pensions – how easily they can be accessed, what taxes are payable and whether it remains financially viable to retire in the EU.

Previously, retirees were required to extract a 25% lump sum from their retirement funds and to transfer the balance to purchase an annuity fund, to secure a reliable income for their retirement.

While Brexit is causing much concern, interest rates also remain at record lows. This means that investing in an annuity now offers far less value than in the past.

UK retirees have the comfort of the pension freedoms announced in April 2015, which state that "pensioners will have complete freedom to draw down as much or as little of their pension pot as they want, any time they want."

The big question remains around taxation, and what HMRC liabilities may arise.

Here we look at the optimal strategies for retirees resident or considering retiring to countries including Cyprus, France, Malta, Portugal and Spain.

Chase Buchanan has put together this guide to assist with understanding pension options as well as the pros and cons of each potential course of action.

UK Pension Schemes

Explained

The first stage in planning for retirement is understanding the type of pension schemes you hold and their value.

Pension income includes the UK State Pension, as well as private schemes, employer-sponsored schemes, and personal plans you may own.

UK State Pensions

The State Pension is available to all UK nationals who have paid the required National Insurance contributions or were exempt from making those contributions.

You can verify whether your contributions are sufficient to be eligible to draw the State Pension. The minimum is 35 years worth of payments or applicable credits, and there is the option of making a voluntary contribution to make up any shortfall.

Check your State Pension entitlement online, or contact the Future Pension Centre for a projected income statement.

Private UK Pension Schemes

Private schemes are separate from the State Pension and can be funded through an employer scheme, or privately.

This category includes stakeholder pensions, personal pension plans (PPP) and self-invested schemes (SIPP).

Employment schemes are typically based on two scenarios:

- Defined benefit schemes – usually based on your final salary.
- Defined contribution schemes – also known as money purchase schemes.

Let's break down the differences between those two classifications.

Defined Benefit Schemes

Also referred to as final salary pension schemes, this type of pension calculates your benefits depending on your number of years of employment, and the salary you were earning.

Defined benefit schemes are paid for life and usually increase in line with inflation. This type of plan is highly valuable and should be carefully managed.

Defined Contribution Schemes

Unlike a defined benefit scheme, this type of plan determines your pension income against how much money is invested in the pension fund.

Once the fund has paid out all of its reserves, there are no further payments, so it is essential to review your drawings to ensure the scheme lasts the requisite number of years.

An investment strategy is critical and needs to take into consideration your acceptable risk levels.

Defined contribution schemes should be carefully monitored and managed, and the investment plans adjusted as required.

Pension Management *Options*

Consolidating Pension Schemes

Many retirees find themselves with multiple pension schemes. Often this is because they have held their own fund, receive an employer fund, and have worked for numerous businesses during their career, each of which has a related pension benefit.

The difficulty in this scenario is being able to manage and track multiple pension schemes, and the costs associated with making investment decisions about your pension funds.

It is also very challenging to effect a consistent risk strategy across multiple pension schemes.

For people holding multiple pension schemes, the new advantages of digital transfers make it possible to transfer various smaller schemes into one fund – which makes managing your money more efficient.

Time Delays in Pension Transfers

Pension scheme members are often keen to transfer their pensions and take advantage of the pension freedoms available.

With increases in the volume of pension transfer requests the process often takes a significant amount of time.

Currently, the process is taking anywhere from three to five months, and transfers from defined benefit to defined contribution schemes from six to seven months.

Transferring Pension Funds from Defined Benefit Schemes

While pension freedoms exist, these are not always applicable to defined benefit schemes.

This is a complex scenario, as while scheme owners can exercise their right to transfer the calculated value of their anticipated pension income into a defined contribution scheme, in doing so they forfeit the security available from a defined benefit pension.

Remember that defined benefit pensions guarantee a stable income for life that increases with the cost of living.

Choosing to sacrifice that stability for a fluctuating investment must be carefully considered.

There are safeguards in place, whereby if you transfer any more than £30,000, you are required to seek professional advice from an independent expert who is not involved with the pension fund provider.

Making the Right Decisions

If you are already a member of a defined contribution scheme or have transferred defined benefit pension funds into a defined contribution scheme, there are multiple options to choose from.

1. Keeping the Funds in Your Pension

Your first option is to retain your pension funds in the scheme and take advantage of the tax efficiencies available.

Usually, this is the simplest option for retirees who have other sources of income and are not reliant on their defined contribution pension scheme.

However, in some EU countries, pension funds are taxable on the same terms as succession taxes. This means that alternative investment options that incorporate allowances against succession tax can be a more lucrative option.

2. Withdrawing the Funds from Your Scheme

The second option is to withdraw all of your pension funds from your defined contribution scheme – however, the tax implications should be very carefully considered.

You will become liable for tax on withdrawing the funds, and the sum will be included within your estate and subject to inheritance tax in the future.

For most EU residents, this type of withdrawal – called a Pension Commencement Lump Sum (PCLS) – is taxable. It depends on your country of residence, but this can vary from zero to 5% right up to 40% and above.

It is therefore critical to know the tax payable on a lump sum withdrawal and deciding the optimal strategy to minimise this cost.

3. Partial Fund Withdrawal and Annuity Purchase

Another option is to withdraw some, or all of your pension scheme, and purchase an annuity.

An annuity provides the stability of guaranteed income for life. However, it is also essential to consider the value for money.

Interest rates are currently extremely low, and so this may not be the most appropriate decision.

However, if you anticipate needing to draw on your annuity payments for only a shorter period, you might decide that it is worthwhile taking advantage of higher annuity rates in the short-term.

4. Partial Withdrawal & Partial Pension Scheme

Finally, you may decide to withdraw some of your pension scheme funds, and leave the balance in your pension scheme until you choose to draw upon it.

The same considerations apply as above, and it is essential to understand the tax implications and the security of your ongoing income streams.

Pension Considerations for UK Expats

There is an added layer of complexity for expats living outside of the UK and drawing on a British pension scheme.

Along with the enjoyment of your retirement lifestyle comes the challenge of managing pension income in a different currency, and understanding the tax rules in your host country.

Here, we will explore the key considerations to bear in mind when planning your pensions for retirement outside of the UK.

Currency Fluctuations

Most UK pension schemes will make payments in Sterling (GBP).

However, this means receiving your pension in a different currency than you will be using for your day-to-day living expenses, which throughout the EU will be Euros.

One strategy to avoid any loss of income when the currencies fluctuate in value is by matching your pension income with your expenditure, both in Euros.

Overseas Transfer Charges for Moving Your Pension Scheme

There is a tax called an Overseas Transfer Charge, introduced by the UK government in March 2017. This imposes a 25% fee against pension funds transferred overseas, which is a massive chunk of your pension savings.

However, until December 2020, when the Transition Period ends, you can transfer pension funds to an EU/EEA country without paying the Overseas Transfer Charge.

This option is eligible for residents of an EU country who will remain resident for a minimum of five years following the date of the transfer.

Brexit will no doubt have an impact on pension transfers from the UK to the EU. It is not yet clear whether the Overseas Transfer Charge will apply to EU transfers. However, it is possible.

That means that if you live in Europe and hold a UK pension scheme, or plan to retire soon, it is very wise to transfer your fund now to avoid paying a potential 25% tax from 2021 onwards.

Expats Returning to the UK

If you decide to return to the UK within five years of your pension transfer, you may become liable to pay UK income tax on the benefits received from your overseas pension scheme.

This is based on rules designed to avoid giving an unfair tax advantage to expats who were not resident in the UK, but only for a short period.

Expats are considered temporarily non-resident if they are living away from the UK for five years or less.

In this scenario, your income is assessed for UK income tax.

Should that income be higher than £100,000, the full amount of income will be taxable. If the income is lower than £100,000, then any payment of a Pension Commencement Lump Sum (PCLS) will not be considered part of the assessment process.

Taxes Payable on Retirement Income

Your pension taxes depend on:

- Where you are resident.
- Where your pension fund is located.

UK pension funds usually issue payments net of UK income tax as a default.

However, double tax treaties exist, which means you won't need to pay taxes both in your country of residence and in the country where your pension fund is based if these are not the same state.

That means needing to apply for UK tax exemption on a British pension scheme to receive the gross value of your payment, and then paying local tax.

However, you might decide to invest your pension fund in Euros. In that case, you can avoid the inconvenience of needing to claim UK tax exemption under the double tax treaty by transferring your fund to a Recognised Overseas Pension Scheme (ROPS).

This type of pension was formally known as a QROPS, and is similar to a UK PPP or SIPP, but is more flexible in allowing holders to manage investments and make withdrawals in multiple currencies, such as Euros.

Pension Tax *Planning*

It is always advisable to seek expert advice when planning your pension income to be as tax-efficient as possible.

UK residents have a stable taxation rate, and aside from the pension freedom allowing retirees to draw 25% of their pension fund tax-free, pensions are taxed as earned income as standard.

However, in EU countries, pension taxes can work very differently. For example, some EU countries tax pensions at a reduced rate of 5% or 7.5%.

Other states allow you to withdraw the entirety of your pension fund, without any tax liability arising. Other states will tax such a withdrawal at a steep 40%.

The optimal solution for your pension depends on your requirements, your country of residence, and the type(s) of pension scheme you hold.

It can be advantageous to invest funds outside of pension schemes, and accepting a tax liability on withdrawal should there be a more tax-efficient investment option available in your host country.

EU Pensions *Overview*

Here is a summary of the current pension regulations in the most popular EU states for UK national expats.

Please note that after December 2020, laws and taxation for British nationals may change, so it is essential to plan now for your future pension income.

France

French pension funds are taxable along with your estate for succession taxes. However, you can withdraw a proportion of your pension fund, or indeed all of your fund, and pay a reduced tax rate of 7.5%.

This cash can be reinvested into tax-efficient structures and those where higher tax allowances are available for succession planning.

Spain

Spanish pension schemes offer a tax-efficient investment option. However, it can be expensive to withdraw lump sums from a pension scheme without expert advice.

Portugal

Portuguese residents who become tax residents before April 2020 may be able to access pension income free of tax.

For those who became tax residents after this date, the tax rate on pension payments is at a reduced rate of 10%.

Cyprus

Overseas pension scheme benefits are taxed at a low rate at a maximum of 5%.

Malta

Non-Maltese residents only pay tax on pension payments paid into Malta. Diligence is required to ensure that planning takes into account double tax treaty requirements.

Moving Forward with *European Pension Planning*

This guide has summarised the most important points to consider when planning for your pension income on retirement in Europe.

For more detailed advice, personalised support, and bespoke strategies, it is always advisable to consult a pension planning expert who understands the taxation regulations in each European country and can recommend the most beneficial plan for your retirement.

Chase Buchanan can assist you with:

- Analysing and understanding your pension options.
- Breaking down those options, types of pension scheme, and values involved to make sound decisions.

- Understanding the tax implications, and most advantageous structures to avoid paying unnecessary taxes on your pension fund or withdrawals.

Whether you are a UK national resident in Europe or planning for retirement in the EU, the team at Chase Buchanan are on hand to help.

With our international network of offices in Belgium, Cyprus, Portugal, Spain, Canada, Isle of Man, the USA and the UK, we work with a global network of clients, providing qualified advice and recommendations about the best way to plan a financially secure retirement.

MISSION STATEMENT

Chase Buchanan
differentiates itself from our
local and global competitors
by establishing a truly
professional organisation
that continues to push the
boundaries in forward
thinking international
tax and wealth
management
solutions.

Chase Buchanan consistently provides world class, international financial solutions and standards of advice and service to our clients. In respect of our approach to client relationships we seek to advise and not simply sell a product. Our aim is to take on each client for the long term and manage their wealth effectively. It is our hope that by doing so we will continue to operate in niche markets and to compete on an equal basis with the larger private banking groups for the attention of wealthier clients.

THE SERVICES WE OFFER

The primary services we offer are:

Investments and
portfolio management

Retirement and
pension analysis

UK pension advice
including SiPPs/QROPS/ QNUPS

Stocks and
shares analysis

Savings

Bespoke specialist tax planning
and repatriation planning

Life, medical and
critical illness insurance

Wills and
estate planning

Property and
mortgages

Trusted advice made simple

TALK WITH AN ADVISER

+44 (0) 1252 852 045

info@chasebuchanan.com

Chase Buchanan Ltd
Head Office
Office 2
6th Floor
Panagides Court
Chrysanthou Milona 1
Limassol 3030
Cyprus

T: +357 2521 2858 / 2521 2859
E: info@chasebuchanan.com
W: chasebuchanan.com

Chase Buchanan Ltd is authorised and regulated by the Cyprus Securities and Exchange Commission with Licence No: 287/15.

Chase Buchanan Insurance Services, Agents & Advisors Ltd is authorised and regulated by the Cyprus Insurance Companies Control Service with Licence No's: 492, 3906 and 507.

Chase Buchanan Ltd and Chase Buchanan Insurance Services, Agents & Advisors Ltd offer services in the EU on a cross border basis as per the provisions of MiFID and IDD.