Amendments 13 to 29 to Schedule 3: Overseas Pensions

Summary

1. These amendments make technical changes to ensure that Clause 17 and Schedule 3 work as intended, in particular ensuring that the current tax treatment continues to apply in respect of lump sums paid out of funds built up as a result of foreign service before 6 April 2017, and in respect of pension saving under specialist foreign pension schemes (known as "section 615 schemes") before this date.

Details of the amendments

2. Amendment 13 amends subparagraph 3(3) of the Schedule so that new section 615(6A) of the Income and Corporation Taxes Act (ICTA) 1988 is extended to apply to cash balance and other types of arrangement under superannuation funds ("section 615 schemes"). The effect of this is that these funds may continue to receive the benefit of exemptions from UK tax in respect of the additional types of arrangement where certain conditions are met (the benefit accrual condition).

3. Amendment 14 amends subparagraph 3(3) of the Schedule to insert new subsection 6AA into section 615 of ICTA 1988 to determine whether there is an increase in an individual's rights under a cash balance arrangement and so whether the benefit accrual condition is met.

4. Amendment 15 amends subparagraph 3(3) of the Schedule with the effect that new subsection 615(6B) of ICTA 1988 ensures that certain increases in the value of rights that accrued before 6 April 2017 are ignored for the purpose of establishing whether the benefit accrual condition is met.

5. Amendment 16 amends subparagraph 3(3) of the Schedule by inserting new subsection 6BA into section 615 of ICTA 1988. This subsection provides a power for Her Majesty's Revenue & Customs (HMRC) to make regulations to determine the increase in the value of an individual's rights, the amount of any increase and whether that increase can be ignored under an arrangement that is neither a money purchase nor a defined benefits arrangement.

6. Amendment 17 amends subparagraph 3(3) of the Schedule with the effect that new subsection 615(6C) of ICTA 1988 now applies the definition of the relevant percentage for all parts of section 615 of ICTA 1988 that refer to it.

7. Amendments 18 and 19 amend subparagraph 3(3) of the Schedule to remove what is now an unnecessary power under new section 615(6D) and to allow provisions under all new powers in the Schedule to be made by amending section 615.

8. Amendment 20 amends subparagraph 4 of the Schedule to insert new definitions in respect of the various types of arrangements into subsection 615(7) of ICTA 1988.

9. Amendment 21 amends subparagraph 4 of the Schedule to insert new subsections 11 to 14 into section 615 of ICTA 1988.

10. New subsection 11 provides that any disqualifying contributions or increases in rights made to a scheme that meets the conditions to be a section 615 scheme will be treated as not arising under the section 615 scheme - the actual fund. Instead they are treated as arising under a separate superannuation fund, the shadow fund, to which section 615 does not apply.

11. New subsection 12 provides that a contribution or an increase is disqualifying if it would cause the benefit accrual condition not to be met, so that the excess of an increase over the relevant percentage would be a disqualifying excess.

12. New subsection 13 ensures that certain sums, assets or increases would not be disqualifying contributions or increases where there is a recognised transfer, as defined in new subsection 14.

13. Amendment 22 removes subparagraphs 6 to 8 of Schedule 3. These subparagraphs provided that section 615 of ICTA 1988 would continue to apply in respect of contributions made and benefit accrual arising before 6 April 2017, but this effect is now provided through new subsections 11 and 12 of section 615 of ICTA 1988 as inserted by amendment 21 to the Schedule.

14. Amendments 23 and 24 amend paragraph 7 of the Schedule so that the inserted new subsection 554Z4(7) of the Income Tax (Earnings and Pensions) Act (ITEPA) 2003 refers to new subsections 554Z4(7A) and (7B) in determining whether there is a reduction in the amount of the lump sum subject to tax.

15. New subsection 554Z4(7A) provides that there is no reduction in the amount of a lump sum subject to a tax charge in relation to employment income provided through third parties (under Part 7A of ITEPA 2003) in respect of pension rights built up on or after 6 April 2017, even if the lump sum is paid in respect of foreign service.

16. New subsection 554Z4(7B) provides that for a reduction in the amount of a lump sum subject to a tax charge under Part 7A of ITEPA 2003 in respect of pension rights as far as they were built up before 6 April 2017 in respect of foreign service.

17. Amendments 25 and 26 amend paragraph 10 of the Schedule so that step 2 of subsection 3 in the inserted section 574A of ITEPA 2003, which reduces the amount of a lump sum that is subject to tax, applies only to the value of the rights built up before 6 April 2017. If the payment is in relation to a payment under a scheme that was an employer-financed retirement benefits scheme (EFRBS) before 6 April 2017, then the reduction is calculated under new subsection (5A) inserted by amendment 27.

18. Amendment 27 amends paragraph 10 of the Schedule by inserting new subsection 574A(5A) in ITEPA.

19. New subsection 574A(5A) ensures that a UK resident who receives a lump sum under an EFRBS, as far the value of the lump sum is represented by rights built up before 6 April 2017, will be entitled to the tax treatment that would have been available if they had received the lump sum before 6 April 2017. This limits the relief to the value of the rights immediately before 6 April 2017.

20. Amendment 28 amends paragraph 10 of the Schedule so that where the term foreign service is used in section 574A of ITEPA 2003, the definition in section 395C of ITEPA 2003 applies.

21. Amendment 29 inserts new paragraph 13 to the Schedule. This paragraph amends subsection 393B(2)(a) of ITEPA 2003 to ensure that a deduction for foreign service relief under new section 574A will not lead to a lump sum paid on or after 6 April 2017 being a relevant benefit. This prevents a tax charge arising under section 394 of ITEPA 2003 for the part of a lump sum reduced by foreign service relief.

Background note

22. Clause 17 and Schedule 3 of Finance (No. 2) Bill 2016/17 as published on 20 March 2017 make a number of changes to the UK taxation of foreign pensions, in order to provide closer alignment of the UK tax treatment of payments out of "foreign pension schemes" with the UK's domestic tax regime and pension schemes used for those employed abroad.

23. More specifically, the changes will:

- Ensure that funds in a registered pension scheme based outside the UK are subject to UK taxation consistent with the tax treatment of a UK-based registered pension scheme
- Tax the full foreign pension of UK residents, instead of 90%
- Close specialist "section 615 schemes" to new pension saving if individuals wish to continue to be able to receive relief from tax in respect of annuity payments from those schemes.
- Tax foreign pension lump sums paid to UK residents that are not already liable to UK tax, whilst ensuring that lump sums paid out of funds built up as a result of foreign service before 6 April 2017 retain the tax treatment available at the time the funds were accrued (known as grandfathering).

24. These amendments ensure that the grandfathering of lump sums paid to UK residents out of specialist pension schemes for those employed overseas (section 615 schemes) works properly, and ensures that the entitlement under all types of section 615 scheme can receive this beneficial treatment.