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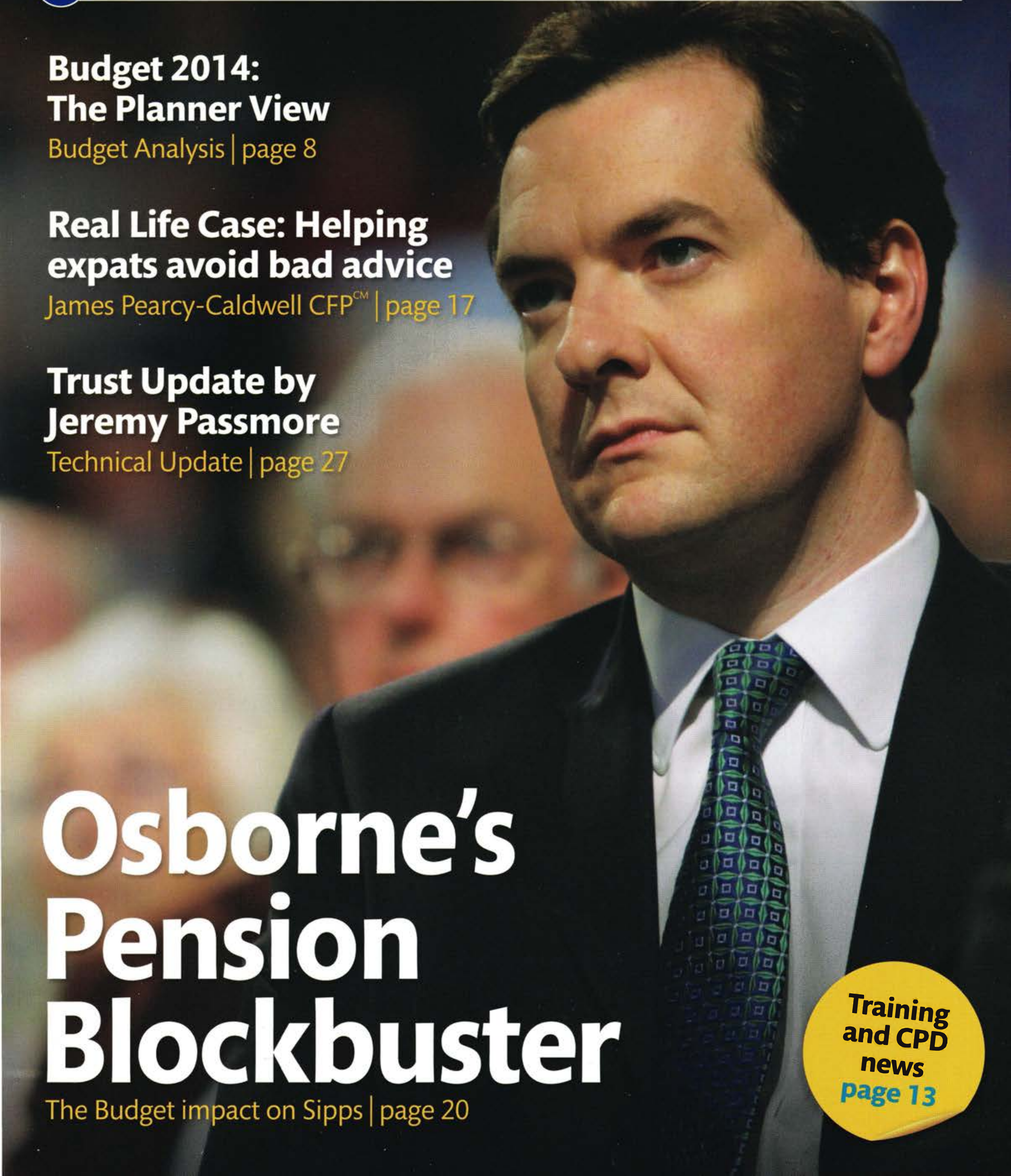

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Tee-time in the sun

James Pearcy-Caldwell CFP^CM explains how he tackled a case of a retired couple living in Cyprus who were confused about how to make the most of their pension and to realise their Florida dream.

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The harbour and the old town in Kyrenia (Girne) on the Island of Cyprus

CASE STUDY BRIEF

Gavin and Ruth, both aged 53, moved out of the UK in 2010 to Cyprus, where they have lived in rented accommodation since. They return occasionally to the UK, but no longer have any financial connections to the UK except Gavin's pension scheme of around £1,000,000. They have declared themselves as non-resident and pay taxes in Cyprus.

They have been considering moving to Florida, as they are keen golfers, or staying in Cyprus.

They've been considering their pension scheme and have already received advice from two overseas advisers who have discussed a QROPS, citing additional benefits such as being able to take benefits now, and higher "tax-free cash" available. However. both firms of advisers they spoke to had no UK qualifications and seem "sketchy" on detail, merely advocating that an investment bond placed into a QROPS is much better for them for future benefits.

This is a real life case study. Names and some other details have been changed to protect confidentiality.

JAMES PEARCY-CALDWELL CFP^CM OF AISA

James operates as a Financial Planner both in the UK and overseas from various companies he operates around the world. He was a military pilot and instructor, has a full airline licence, and his new hobby is learning to fly helicopters. His firms are regulated overseas and he has recently created OpesFidelio, a European-based network. He is a Certified Financial Planner'" Professional, Chartered Financial Planner. G60 and has won multiple awards, including being a current Money Management winner. He looks to work with other advisers who believe that running a successful business profit model is directly linked to positive client outcomes.

QROPS are a bit like marmite, advisers love them or loathe them. However, Just because an adviser has a preference does not mean they should be ignored, and just like marmite, they have to be put on the table and made available for other people. QROPS, in particular have been widely mis-sold and mis-labelled as a method of 'releasing' capital and avoiding tax. The truth is they are a useful planning tool which can benefit certain eligible clients in many ways. Gavin and Ruth contacted me via a recommendation. During our first conversation I established they'd already received two sets of advice, were speaking to a third adviser, and I was the fourth adviser engaged. They were confused and uncertain.

The initial advisers they spoke to were internet-based; one from Spain and the other from the Middle East who had helped friends in Dubai. Both adviser firms recommended Gavin and Ruth use a QROPS as this would boost Gavin's PCLS (tax free sum) and also enable an income to be taken immediately of 5 per cent, higher than the GAD rate in the UK. Further, Ruth would be able to avoid the "non-recoverable 55 per cent" income tax charge on Gavin's death. Somewhat confusingly this had been advised as a UK IHT liability. Gavin was surprised that both advisers recommended the same underlying investment bond, with identical illustrations. When I asked what he had paid to receive all advice to date, Gavin informed me it was "free" and that both advisers explained they would be paid by the bond provider.

I suggested a project fee that would provide options to Gavin and Ruth with "no sale necessary" and no obligation to proceed. They were both happy with this approach and readily sent through information via email. We arranged specific times

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where we could discuss matters further and I sent an email outlining some of the information I would be seeking.

The first questions were simple. When did they move out of the UK, what were their intentions and objectives, what were their plans and budget in retirement? When they explained that they still visited the U K but were no longer resident, I immediately sought more information; how often did they visit and how long did they stay for? Ruth had done her homework and was quick to point out that they visited infrequently each year, far less than 30 days and they had no intention of returning permanently. I explained that while it may never be their intention to return that there may be future unforeseen circumstances that may change this situation such as family crisis, the ill-health of loved ones or even a death.

Having established some rapport, I asked "why contact me?" Direct questions often obtain direct answers. In this case, they did not trust promises of 12 per cent investment growth and information received as it sounded too good to be true. Gavin wanted reassurance and realistic targets.

I understood and explained to Gavin and Ruth that, since they had only moved out of the UK on 15 April 2010, a QROPS may not be the best solution. The other advisers had been quick to cite some QROPS benefits which would be unavailable until they had remained outside the UK for five full tax years and Gavin was aged 55. I explained that Gavin should essentially follow UK rules on his existing pensions until 6 April 2016. I also explained the 5 per cent income cited was likely to be linked to recommended withdrawal levels from bonds, rather than any link to pension rates which often exceeded 5 per cent.

Additionally, the other advisers had given the impression that if Gavin died, 55 per cent of his fund would disappear. I explained that as Gavin had not actually crystallised benefits, neither lump-sum, nor taken income, that his personal pension fund would be returned to beneficiaries intact. When he said "but the advisers told me that there would be an IHT charge on this," I explained that I had checked and this would not be the case, as it was a tax-free return of fund prior to any benefits being taken. A QROPS may benefit on second death but only if they had both been out of the U K for five full tax years.

As discussions continued, it became apparent that Gavin continued earning from consulting and did not require access to his pension. In fact, it transpired they had £400,000 from the sale of their UK home, which was invested in a UK account. Their beneficiaries, their children, still lived in the UK.

I explained that as they had not been out of the UK for at least 17 in the last 20 years, they maintained British passports, retained investment assets and UK beneficiaries, that they probably would not avoid an IHT assessment. At this point, Ruth mentioned that the Spanish internet adviser stated they would lose their IHT "exemptions" now they were no longer UK resident. We agreed the "exemption" referred to was in fact the "nil rate band"; I explained the first £650,000 of combined assets had no exemption to lose; they would pay UK IHT at 0 per cenr on this and Gavin's pensions, as HMRC was likely to class them as UK citizens, irrespective of UK residency.

Gavin sent me a breakdown on his pensions which amounted to personal pensions of £850,000 and a guaranteed benefit scheme that had a transfer value of £155,000. I obtained further information and it became apparent that Gavin's pensions had high charges that could be improved upon, with no transfer penalty. Gavin was good enough to forward me a WAS - investment bond report that he had received from overseas. His WAS report did not allow for any charges on the new scheme, excluded a critical yield and most of the information you would expect- but it looked nice!

The investment bond illustrations from both advisers firms were identical for £1,005,000, and neither declared commissions. Gavin had discovered the "charging structure was called AV279." I obtained from the relevant provider, for comparison purposes, an AV279 illustration detailing 8 per cent commission and identical products with zero commission. Amazingly, the illustrations showed almost identical projected returns over 1 0 years. I therefore contacted the provider to obtain the exact charges applied. Under AV279 the commission resulted in large surrender penalties for eight years, and there was an additional 1 per cent charge applied annually forever, on top of the quarterly fees and fund charges. While charges reduced on the non-commission product, the illustrations were stubbornly similar. I therefore put the different charges into a cashflow calculator and my projections over 1 0 years were completely different. Unsurprisingly, the AV279 £80,000 commission produced lower returns than the non-commission projections. Not one offshore adviser had mentioned that any sums taken from the bond in the future would lead to all charges being levied on the original investment value if higher than the subsequent value; a serious downside for someone withdrawing benefits in a pension.

I then did a cashflow comparison against three different platforms, taking a 2 per cent initial charge. All three platforms illustrated returns that were substantially in excess of the bonds, and total annual charges were about 2.3-2.7 per cent lower (Approx. £20,000 less). There were no tax benefits of holding a bond in a pension, nor additional security or guarantees, which had all been mentioned by the internet offshore advisers but not substantiated with any facts. A UK Sipp was in fact more tax efficient.

Gavin and Ruth arranged a meeting and I took them through what I had found. They explained they had thought things through and wanted to retire in the US after 2017 and did not need benefits until then. I recommended they retain the guaranteed pension. Double taxation agreements with the US would mean that, after tax, they would be better off, as a 1 0 per cent critical yield was required to match benefits and the scheme was well funded. For the personal pension I suggested either a Sipp or platform, based in the UK until at least 2016, and probably beyond until their retirement. I explained the investment bond that had been recommended had substantial charges and surrender penalties.

At retirement we should re-review, suggesting under current legislation that a QROPS-based platform at that point would be the best solution as it would allow greater death benefit flexibility and fund/currency issues, as well as providing greater tax free cash. They raised the issue of the US residency, as they had heard that UK pensions in the US were taxed. I explained that fund growth and income within the pension would be taxed as the US did not recognise the tax status of UK pensions. However, any future lump sum taken would remain tax-free as the US recognised this benefit. The future pension trustee location would be critical to utilise US double-taxation agreements, allowing income tax offset. Not transferring to a QROPS now had advantages and disadvantages. The main advantages included no high offshore trustee fees, no high commission investments with additional charges. This allowed either greater potential growth or less risk to be taken to achieve the same returns. Also, many offshore trustees have no obligation to allow future transfers of pension assets; if Gavin and Ruth changed their circumstances it may have a big impact.

Disadvantages included future legislation changes that may impact on pensions. Also, some QROPS jurisdictions legitimately allow 70 per cent of the original transferred value to be utilised for income, thus meaning that excess "growth" could become a tax-free sum. Clearly without transferring now, they would lose the ability to "grow it" until they reached their five year qualification.

WHAT HAPPENED NEXT

Gavin and Ruth reviewed my final report, considered their risk position, and elected to leave the guaranteed pension where it was. Gavin now wishes to consider utilising a Sipp in the short term until he reaches five full tax years outside of the UK, due to more competitive charges and management. He has agreed to pay a fee to utilise a low charged platform with full explicit costs, exactly as he would have done had he remained in the UK, with no loss of benefits. He wants us to manage his investment pro-actively utilising our CIP.

We will review the QROPS position again either six months before Gavin decides to retire, or before age 74, or when they re-locate to another country.

Gavin calculated that we had saved him £234,000 in compound charges in the first 10 years. He bought us a case of wine as a thank you and recommended us to his friends.

KEY POINTS

1 Retirees overseas should consider both Sipps and QROPS and base decisions on their circumstances; neither should be automatically selected or ruled-out.

2 To benefit from "additional" pension benefits individuals have to be outside of the UK for five full tax years.

3 The use of "overseas" illustrations by sales staff outside of a regulated environment, such as the UK, can be misleading or even fraudulent.