Technical CONNECTION

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THE SPECIAL ANNUAL ALLOWANCE

HMRC has issued a draft of pages it will be including in the RPSM regarding the special annual allowance. This updates the guidance given on the anti-forestalling rules released at the time of the 2009 Budget.

ISA SUBSCRIPTION LIMITS RAISED

The opportunity for some to increase their annual subscription with effect from 6 October 2009

The ISA subscription limit has been raised to £10,200, of which up to £5,100 can be invested in cash. These new limits will apply to people who are or will be aged 50 or over in tax year 2009/10, and to all qualifying investors, irrespective of age, from tax year 2010/11 onwards.

The commencement date of the new limit for the "over 50" group is 6 October 2009, and ISA providers will not need to obtain fresh applications from such investors before they make subscriptions based on the new higher limits. The options available to "over 50" investors between 6 October 2009 and 5 April 2010 are as follows:-

- Those who have not made any ISA subscription for 2009/10 can put up to £5,100 into a cash ISA and the balance of up to a combined amount of £10,200 into a stocks and shares ISA. A cash and stocks and shares ISA can be taken with different providers (ie. one for each type of ISA).

- Those who have already subscribed the pre 6 October 2009 maximum of £7,200 can subscribe a further £3,000, subject to holding a total maximum of £5,100 in cash.

  - For example, Bill subscribed £2,500 to a cash ISA and £4,700 to a stocks and shares ISA. For future investments, he has decided to reduce his exposure to risk so he invests £2,600 in his existing cash ISA (top- ups must be made with the same provider) and puts the remaining £400 in his stocks and shares ISA.

  - Conversely, Jean subscribed £3,600 to a cash ISA with provider X on 6 April 2009 because, in view of the then state of the investment markets, she had decided it was not yet the time to invest in equities. With the recent improvements in the markets she is now less risk averse and decides to invest £6,600, ie. up to the increased maximum of £10,200, with provider Y in a stocks and shares ISA.

  - Henry has always used his ISA subscription to make the maximum investment in stocks and shares. He invested £7,200 (the maximum) with provider W in May 2009. He now wishes to take advantage of the increased subscription limit but is unhappy with provider W's investment performance. In light of this he wishes to invest the £3,000 top-up with provider V who offers a very attractive new commodities fund. Unfortunately for Henry, as he can only have one provider at a time for his stocks and shares ISA, this means that he must either invest a further £3,000 with provider W, or transfer the whole of his 2009/10 subscription to provider V so that he can then pay his £3,000 top-up into the new commodities fund.

COMMENT

Before making an investment which would take an existing 2009/10 ISA subscription over the pre 6 October 2009 limit of £7,200 for a stocks and shares ISA (£3,600 for a cash ISA), it is important to check that the provider is willing to accept the further subscription(s).

AN INEFFECTIVE PENSIONS-RELATED AVOIDANCE SCHEME

In its latest edition of "Spotlights", HMRC has highlighted the following pensions-related avoidance scheme, which it deems to be ineffective.

"*We are aware of schemes that purport to enable a member of a registered pension scheme to remove funds from the scheme tax-free. These involve contriving to create a funding surplus through the surrender of rights by a member. They sometimes involve cases where provision is made under a separate unconnected trust for the surviving spouse or other dependants of the member.*

A surplus created by a reduction in liability caused by a member surrendering rights in a scheme, and the consequential payment made in these circumstances, will be regarded as an unauthorised payment in respect of the member, and will attract tax charges on the member on the amount paid by the scheme administrator."

BENEFITS PAID AS AUTHORISED PAYMENTS

Earlier this summer HMRC made a number of changes to the circumstances where benefits could be paid as authorised payments. Using powers set out in the Finance Act 2008, the government has extended the range of small payments which do not attract unauthorised payment charges beyond those covered by the then existing trivial commutation rules. These new authorised payments are set out in the Registered Pension Schemes (Authorised Payments) Regulations 2009 – SI 2009/1171 under section 164(1)(f) of the Finance Act 2004, newly created by Schedule 29 Finance Act 2008. These set out details of the payments involved. They include the conditions to be met for the new £2,000 de minimis triviality payment applicable under occupational schemes. The new trivial commutation provisions will apply to any such payments made on or after 1 December 2009.

The DWP is now consulting on draft regulations to ensure that the rules relating to contracted out benefits will fully mirror those introduced by the HMRC changes with effect from 1 December 2009.

CORPORATE SHARE PURCHASE

The Companies Act 2006
Corporate share purchase
Relaxation of the rules which enable a private company to purchase its own shares out of capital

The Companies Act 2006 (the Act) has replaced the company law provisions of the Companies Act 1985, the Companies Act 1989 and the Companies (Audit, Investigations and Community Enterprise) Act 2004. The Act extends to the whole of the UK which means that there is no longer a separate regime for Northern Ireland.

The Act has been implemented in tranches starting from 8 November 2006. The final provisions to be implemented took effect from 1 October 2009. Amongst the provisions that took effect from that date are sections 713 to 723 of the Act which deal with the requirements to be satisfied for a private company to purchase its own shares out of capital.

In the context of life assurance, sections 713 to 723 can be relevant when a private company establishes a corporate share purchase arrangement. Under such an arrangement a company arranges to buy back its own shares, typically to ensure that on the death of a shareholder his or her family receive cash compensation for his or her shares which enables the company to remain in the ownership of the continuing shareholders.

In some cases a company will fund the purchase through an appropriate life assurance policy effected on the shareholder's life. If in the circumstances it can be argued that the policy proceeds can be treated as distributable profits the purchase of shares will be made out of such profits and not capital. If, however, the payment is treated as made out of capital then sections 713-723 will apply.

Before 1 October 2009 one of the requirements for a purchase out of capital was that the directors had to make a statutory declaration, to be delivered to the Registrar of Companies, specifying the amount of the capital payment for the shares in question and stating that the payment could be made without prejudice to the company's creditors. In particular, they had to confirm that they could see no grounds on which the company would be unable to pay its debts or continue as a going concern for a period of at least one year after the purchase. This declaration had to be accompanied by an auditor’s report stating that they had looked into the company's affairs and were not aware of anything that would render the directors' opinion in the statement unreasonable.

This could have been a significant issue to take into account when considering the corporate share purchase route as an option if the proceeds of any policy paid to the company on the death of a shareholder were to be treated as a capital receipt. The requirement for a statutory declaration meant that if the company were wound up within one year of the declaration and proved to be insolvent then both the seller of the shares and the directors of the company may have been liable to contribute to the financial deficiency of the company.

Under the Companies Act 2006 provisions, which came into effect on 1 October 2009, there is no longer a need for a statutory declaration. A simple statement by the directors (without the need to swear it) about the solvency of the company is all that is required. However, there has been a change in the description of liabilities that must be taken into account – the directors must now take account of all the company’s liabilities rather than just those relevant under the Insolvency Act 1986.

There is still the requirement for a report from the company’s auditors stating that they have inquired into the company’s affairs and that they are not aware of anything to indicate that the directors’ opinion expressed in their statement is unreasonable.

COMMENT

This is a change for the better and makes it slightly less onerous to make a purchase out of capital.

PERSONAL ACCOUNTS DELIVERY AUTHORITY

The Personal Accounts Delivery Authority (PADA) is embarking on a ‘myth busting’ programme to explain how the personal accounts scheme will fit in to the pensions landscape from 2012. The initiative, led by PADA’s market engagement team, will consist of an ongoing meetings programme with key audiences, including pension advisers, trade bodies and employers, to explain the likely features of the pension scheme, clarify misunderstandings about its role and explore how the personal accounts scheme might be used.

To support this programme PADA has made available updated versions of its “Myth buster” and “Key facts” documents.

Among the myths addressed in the "Myth buster" leaflet is that personal accounts can be used by employers of all sizes. Confirmation is also given that personal accounts are on track to be introduced in 2012 at the same time as the new employer duties (auto enrolment).

IHT – CALCULATION OF THE TEN-YEAR ANNIVERSARY CHARGE

Transfers made in the seven years before a trust commenced
The situation when details of transfers made within the seven years preceding creation of the trust are not available

Under trusts subject to the IHT relevant property regime an IHT charge can arise on each tenth anniversary of the creation of the trust. This charge is known as the ten-yearly or periodic charge.

In calculating the amount of this charge, the trust is treated as an assumed transferor making a transfer of the value of the trust fund at the ten-year anniversary taking account of chargeable lifetime transfers in the seven years preceding the creation of the trust equal to those made by the settlor (creator) of the trust during that period. If this notional transfer by the assumed transferor does not exceed 80% of the then nil rate band ignoring any liabilities, exemptions or reliefs from IHT, then no return has to be made to HMRC.

If a return does have to be made to HMRC then forms IHT 100 and 100d have to be completed whether or not any tax is actually due. In addition, if the trust assets include a life assurance policy then form D34 has to be completed.

Form 100 is the inheritance tax account for a number of transactions including charges under the relevant property regime. Form 100d is the event form for a periodic charge, and question 1.7 on the form 100d reads as follows:

"State the total of chargeable transfers made by the settlor during the seven years immediately before the trust was set up".

If the settlor is still alive at the ten-year anniversary he or she should be able to provide this information to the trustees. If it is not the first ten-year anniversary charge then the information should have already been gathered for the first ten-year anniversary charge.

If the trust was created by Will then the personal representatives of the deceased should have checked the position on lifetime transfers within the seven years preceding death to establish the IHT position on death. If the trust was established during the settlor's lifetime and the settlor died within seven years of establishing the trust then again the personal representatives should have checked the position at that time.

If the settlor died more than seven years after setting up the trust there is no reason for the personal representatives to have enquired into the position but, of course, earlier transfers may well affect the IHT payable by the trust. Nevertheless they should be contacted and/or any solicitor involved in the creation of the trust to see whether the information is available from these sources.

The trustees should use their best endeavours to establish the position. If the answer to question 1.7 on form 100d is left blank the inference would be that no transfers had taken place. If it later transpires that transfers did take place and, as a consequence, some IHT was unpaid then there would be the prospect of exposure to penalties as well as the payment of tax and interest.

If the trustees' enquiries draw a blank they could explain the position to HMRC – it may be that HMRC has records of previous transfers.

COMMENT

This potential problem could be obviated if, at creation of the trust, a note is made of the position on cumulative transfers made by the settlor in the preceding seven years. It should be borne in mind that the cumulative total is not the only information required – for example, the amount of any added property (after the trust was established) and any exit charges within the previous ten years will be required.

THE REGULATORY RESPONSIBILITIES OF SIPP OPERATORS

The FSA included an analysis of pension transfer advice in its Retail Thematic Work for 2008/09. The results of that review were set out in the FSA's report "Quality of advice on pension switching" in December 2008.

Following that review the FSA asked approximately 60 small firms (ie. firms supervised by the Small Firms & Contact Division "holding the permission of establishing/ operating/ winding up a personal pension scheme") to complete a questionnaire covering a broad range of SIPP operator activities. This was to determine the extent to which they were adhering to the FSA's principles and rules. This was followed up by a telephone assessment of around 50% of the firms concerned with visits to a number of these firms.

While the FSA indicated it did not feel that, taken as a whole, small SIPP operators posed a significant threat to its statutory objectives, the review did highlight a number of concerns about how some firms conduct their business. The FSA has written to the senior management of every small SIPP operator explaining its findings, in particular in the areas of Treating Customers Fairly (TCF), relationships with firms that give SIPP advice, systems and controls, disclosure of fees and charges, and the production of illustrations.

The FSA has produced the following:

- A copy of the letter sent to the senior management of every small SIPP operator

- A factsheet setting out the standards all SIPP operators should be achieving and the key rules they should be following

- A series of 6 case studies containing examples of good and poor practice to help firms assess whether there are any changes they need to make to their practices

- A report on the findings of this thematic review of SIPP operators

"MANSWORTH –V- JELLEY" LOSSES

Sale of shares acquired under an unapproved share option scheme
Court of Appeal finds in favour of the taxpayer in Mansworth v Jelley December 2002
Tax position as originally understood reinstated from 10 April 2003
Inland Revenue issues on 17 March 2003 guidance for the period to 9 April 2003
Revenue Customs Brief 30/09 explains legal advice received now by HMRC finds that the guidance was incorrect

The impact of the decision in Mansworth -v- Jelley 2002, in brief, was as follows:-

(i) Under an unapproved share option scheme, on exercise of an option the difference between the market value of the shares at the date of exercise and the cost of those shares is treated as a gain subject to income tax.

(ii) Before the decision in Mansworth -v- Jelley it was well understood that on subsequent disposal of the shares the base cost for capital gains tax (CGT) purposes was the market value at the date of exercise not the acquisition cost – this was to prevent a charge to both income tax and CGT on part of the capital gain.

(iii) The decision in the Mansworth case fixed the base cost for CGT as the market value at the date of exercise **plus** the gain charged to income tax at the date of exercise. This change often resulted in no capital gain arising and in many cases gave rise to a loss.

(iv) From 10 April 2003 legislation was introduced to prevent these "Mansworth-type" losses arising. For disposals before 10 April 2003 Inland Revenue guidance issued after the Court of Appeal ruling was that the market value at the date of exercise plus the gain charged to income tax (as in (iii) above) was to be used in the CGT calculation.

The legal advice received now is that only the market value at the date of exercise should have been taken into account.

In Revenue & Customs Brief 30/09 HMRC describes the situation thus *"Those affected by the change may need to make or amend a Self Assessment return or loss claim provided they are in time to do so. HMRC will apply our new understanding of the law in cases where there is an open enquiry or appeal"*.

COMMENT

This situation is somewhat bizarre. Those clients who exercised options under an unapproved share option scheme and realised the shares before 10 April 2003, and as a result claimed loss relief, should review their position carefully and take professional advice if thought necessary.

NON-STATUTORY CLEARANCES FOR IHT BUSINESS PROPERTY RELIEF

HMRC has announced a new clearance service for business owners on the application of inheritance tax business property relief to particular transactions. The details of this new clearance service are set out in a guidance note on http://www.hmrc.gov.uk/cap/clearanceiht.htm.

COMMENT

*Notably it is made clear that this new non-statutory clearance will **not** be available "where you ask HMRC to give, or comment on, tax planning advice-in particular, HMRC do not "approve" tax planning arrangements".*

Nonetheless, even though, in most cases, it will be relatively clear whether business property relief is available for an asset or not, this new service is to be welcomed as a means of giving business owners and their advisers certainty over the IHT effects of relevant transactions.

STATE PENSION CHANGES

The Social Security (State Pension and National Insurance Credits) Regulations 2009-SI 2009/2206 make amendments to existing legislation consequential to changes to state pension benefits introduced by the Pensions Acts 1995 and 2007. These changes begin to take effect from 6 April 2010. In particular, the amendments:

- specify the amount of basic state pension a person is entitled to if he does not satisfy the new contribution condition in full;

- provide for the gradual phasing-out of automatic National Insurance credits for men who are within five years of state pension age; and

- provide for men and women to be treated equally with respect to the calculation and inheritance of graduated retirement benefit.

PENSIONS MISCELLANY

- The Pensions Regulator and the FSA have jointly produced a guide for employers, "Talking to your employees about pensions", which explains what information an employer can provide to his employees regarding the employer pension arrangements. This also covers where an employer must be careful to ensure that any such information is not regarded as giving financial advice.

- The increasing number of articles/comments concerning the cost of public sector pensions and for the need for such benefits to be cut back has led the TUC to issue a hard hitting defence of such arrangements in its paper "Decent Pensions for All".