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GENERAL ANTI-AVOIDANCE RULE

In December 2010 the Government asked Graham Aaronson QC to lead a study group to establish if a General Anti-Avoidance Rule (GAAR) could be given statutory framework in the UK.

The study group is due to complete its task by 31 October 2011, when it will inform the Government of its conclusions and, if a GAAR is to be implemented, exactly how it is to be implemented.

The Treasury has now seen fit to publish a letter from Graham Aaronson QC to David Gauke, Exchequer Secretary, on the progress the study group is making. The letter speaks in general terms, sometimes repeating the remit given by the Government. There is no indication of what the conclusions of the group's deliberations will be. It seems that the likely outcome will be that the group concludes that a statutory GAAR is feasible and should be implemented. However, we will have to wait until the autumn for a clear view.

STATE PENSION AGE CHANGES STILL ON COURSE

Although the Pensions Bill has passed its second reading in the House of Commons there is still some doubt as to whether the State Pension Age (SPA) changes will go ahead.

During that debate Iain Duncan Smith, the Secretary of State for Work and Pensions, stressed that there would be no change to the timetable set out for bringing forward the increase in State Pension Age (ie. to age 65 by November 2018 for women, and to age 66, by April 2020 for males and females), as any delay would result in a cost to the taxpayer of £10 billion. He did, however, go on to indicate *"I repeat that the Bill that we have presented on Second Reading will retain the dates that we announced, but as I said earlier, I will quite happily discuss transitional arrangements with anyone who wants to do so. I do not rule out discussions, but we plan to press ahead with the dates that I set out at the beginning of the process."*

In his summary at the end of the debate, Steve Webb, the Minister for Pensions, commented: *"On that issue, which has clearly been the focal point of the debate, let me sum up the position. We heard a number of hon. Members raise their concerns about the state pension age. The Government's position is clear. We are not simply living longer; we are living longer at a faster rate. The improvement of five years in life expectancy at pension age took 70 years between 1920 and 1990. The next similar improvement happened in 20 years. The improvement in longevity is like a runaway train. We must address that. Those who vote against Second Reading are not just deficit deniers, but longevity deniers. They need to recognise the real changes.*

My right hon. Friend the Secretary of State, in his characteristically resolute way, confirmed that the Government believe that we need to equalise more rapidly and reach age 66 as the retirement age more rapidly, but he also said that he recognised that we need to implement that fairly and manage the transition smoothly. He went on to say that he heard the specific concerns about a relatively small number of women and that he was willing to work to get the transition right. I am committed to doing the same, together with him."

It certainly appears that those women most affected by the bringing forward of the SPA will be compensated in some way. It will be interesting to watch these developments.

CONSULTATION ON THE REFORM OF SECTIONS 31 AND 32 OF THE TRUSTEE ACT 1925

On 26 May 2011 the English Law Commission published consultation paper No 191 (Supplementary) entitled "Intestacy and Family Provision Claims on Death: Sections 31 and 32 of the Trustee Act 1925". This consultation paper is supplementary to the one issued in October 2009 on amending section 32 and responses to the consultation are invited by 21 July.

Section 31 Trustee Act 1925 deals with the application of trust income where the beneficiary is a minor; section 32 deals with the advancement of capital to beneficiaries.

Section 32 is considered particularly restrictive, given that it limits advancements of capital to one half of the beneficiary's vested or prospective share of the trust fund. The main problems with the application of section 32 arise with trusts created on intestacy as well as with implied trusts, including trusts created for minor children where funds are simply designated for their benefit.

As indicated above, there was a previous consultation on amending section 32. However, at that stage the proposal was only to remove the "one half" restriction for statutory trusts established through intestacy. Most of the responses to that consultation paper agreed with the proposal to remove it but in fact suggested that it should be removed for all trusts. The current consultation paper indeed extends the abolition proposal to all Will trusts and to lifetime trusts.

As far as section 31 is concerned, this gives trustees the power to use trust income for the benefit of minor beneficiaries but imposes restrictions on when and how that power may be exercised. The current consultation paper proposes to relax these rules, or even entirely remove them, leaving the use of trust income to be determined entirely at the trustees' unfettered discretion – a provision that would typically be included in a professionally drafted trust.

If implemented, the new rules would apply only to newly created trusts and it is not yet certain how the rules would be applied to Will trusts, ie. whether the new rules should apply only to trusts in Wills executed after the law has changed or to trusts in Wills where the testator died after the law has changed. One way or another it is expected that the law will be changed in due course.

FURTHER DRAFT 'AGE 75' REGULATIONS ISSUED

HMRC has issued three further draft regulations regarding the 'age 75' changes in the Finance (No.3) Bill 2011. The proposed changes include a reduction of the maximum income that can be taken from a variable lifetime annuity and a requirement that where a member taking a capped drawdown pension is aged over 85 the annual review of his maximum income will be undertaken on the assumption he is aged 85.

There are significant changes to the variable lifetime annuity provisions. At present, very broadly, an individual must take an income each year from a variable lifetime annuity of between 50% and 120% of the annuity rate determined at commencement (or subsequent review date). The annuity rate used for this purpose is either the provider's own annuity rate for a level single life pension, or the average of the best three such rates on the open market where the provider does not offer such annuities. The minimum and maximum income levels must be reviewed at least every 5 years. These draft regulations reduce the maximum income that can be taken to 100% of the annuity rate and require a review of the minimum and maximum income to be undertaken at least every 3 years.

The draft regulations provide that these changes will not apply to any variable lifetime annuity set up before the regulations and so that level of annuity will apply until the next review date of the annuity. Therefore, assuming the regulations come into effect on 6 April 2011, a variable lifetime annuity which commenced on, say, 1 March 2011 could continue to provide income based on 120% of the annuity determined at that time until the next review as at 1 March 2016.

This change is presumably being made to bring the income available from a variable lifetime annuity broadly into line with the new capped drawdown limits. It is unclear when these regulations will come into force. However, if this is from a future date this may give scope to set up a variable lifetime annuity now, based on the current rules, enabling a higher maximum income to be taken for up to 5 years. It might also be possible for a member already in receipt of such an annuity to request the provider to bring forward the review date to lock in the higher maximum income for a further five year period.

PENSION SCHEMES NEWSLETTER 47 ISSUED

HMRC has issued Pension Schemes Newsletter 47. The main subjects covered are:

- Annual allowance calculation for DB benefits

- Pension Input Periods - our May 2011 Bulletin provided details of how the new pension input period end date provisions, set out in the Finance (No.3) Bill 2011, will be applied. This Newsletter confirms the information in our May Bulletin.

- Draft Regulations - Our May 2011 Bulletin provided details of draft regulations issued by HMRC in conjunction with the 'age 75', annual allowance and lifetime allowance changes included in the Finance (No.3) Bill 2011. It is confirmed that it is intended to lay these regulations immediately after the Bill has received Royal Assent, with them coming into force 21 days later.

- Fixed Protection - It is indicated that the fixed protection election form will not be available until around the middle of August 2011.

THE MOVE TO CPI INCREASES BY PRIVATE SECTOR SCHEMES

The Government has confirmed in its response to the consultation on the use of CPI for private sector occupational schemes that it will not provide legislation to assist such schemes to move to a CPI increasing basis. For detail of the consultation see our January 2011 Bulletin.

CONSULTATION ON CHARITABLE LEGACIES

HMRC has published a consultation paper on the policy detail and implementation of a lower rate of inheritance tax where people leave a charitable legacy of 10% or more of their estate when they die. This change was announced in the 2011 Budget.

For deaths occurring on or after 6 April 2012, estates that include charitable legacies of at least 10% of the net estate will benefit from a 36% rate of IHT (compared with the main IHT rate of 40%).

Whether or not the 10% threshold rule has been met will be determined by comparing:

- the total value of charitable legacies for IHT purposes; and

- the value of the net estate for IHT purposes as reduced by:

  - Any available nil-rate band;
  - The value of assets passing to a surviving spouse or civil partner; and
  - The value of assets that qualify for IHT reliefs and exemptions – apart from the charitable legacy itself.

If this 10% test is passed, the estate will qualify for the reduced rate of IHT.

The paper gives a number of examples. The first of these examples, set out below, shows how to calculate whether the minimum charitable legacy passes the 10% test.

Example

An estate is valued at £850,000 and the available nil-rate band is £325,000. On the basis that the minimum charitable legacy to pass the 10% test was bequeathed, the position before 6 April 2012 and from 6 April 2012 would be as follows:

		Before April 2012		From 6 April 2012
Estate value		£850,000		£850,000
Less charitable legacy		- £52,500		
Less available nil-rate band		-£325,000		-£325,000
Net estate for 10% test purposes				£525,000
Less minimum charitable legacy to pass 10% test				-£52,500
Taxable estate		£472,500		£472,500
	@40%	£189,000	@36%	£170,100

The amount left for distribution to non-charitable beneficiaries, (ie. the estate value less any charitable legacy and IHT due) would be:

Before April 2012	From 6 April 2012
£608,500	£627,400

With no charitable legacy, the amount available for beneficiaries would be £640,000 (the estate value less IHT due (£210,000) on the estate. The charitable legacy results in a reduction in the amount left to other beneficiaries of:

	Before April 2012	From 6 April 2012
	£31,500	£12,600
As a proportion of the charitable legacy	60%	24%

The consultation paper asks for views on aspects of the policy that have not yet been decided and how HMRC can best implement the policy. It covers the following areas:

- Application of the 10% test and the reduced IHT rate; and whether the reduced rate should be limited to the free estate or extended to other components of the estate;
- The nature of the legacy, including some practical issues around the valuation of assets, types of charitable legacies, claims and avoidance;
- Instruments of variation, including notifying charities about legacies; and
- Administration issues such as those connected with forms, guidance and Wills.

The consultation runs until 31 August 2011.

FSA WARNING ON 'PENSION UNLOCKING'

The FSA has issued a warning over loan-based pension unlocking schemes. Its main comments are:

- On costs, the FSA says *'The promotional material for the schemes we have seen does not state the exact level of fees or charges, so there is a good chance that you are likely to end up with less money than you started with'*.

- On whether there is a tax charge, the regulator observes that *'The schemes claim that no tax is payable from the money you take as cash. However, it is not clear what rules the schemes are relying on to make this claim'*. The FSA reminds would-be borrowers that unauthorised payment charges could be up to 70% of the value of the loan and, to reinforce the risks involved, says *'We are working closely with HM Revenue & Customs and the Pensions Regulator to find out more information'*.

- The FSA recommends that before taking any action people should seek independent advice and *'ensure you and your financial adviser understands how these schemes work and what they mean for you'*. It also points to a need for *'independent legal advice on the risks involved with any firm taking sole control of your pension fund'*.

These FSA comments emphasise that anybody thinking of using such a scheme should make sure they understand all the risks and fees involved.

PENSIONS MISCELLANY

- In its consultation on removing a further 36 tax reliefs the Treasury is considering the removal of the income and capital gains tax reliefs granted in respect of compensation payments arising out of the Pension Mis-selling Review.

- The DWP guide to automatic enrolment and workplace pension reform has been updated. This provides an excellent summary of the changes and the current amendments being included in the Pensions Bill 2011.

CONSULTATION ON THE REFORM OF THE TAXATION OF NON-DOMICILED INDIVIDUALS

In the 2011 Budget the Government announced that it would reform the tax treatment of non-domiciled individuals ("non-domiciles") by:

- increasing the existing £30,000 annual remittance basis charge (RBC) to £50,000 for non-domiciles who claim the beneficial tax regime ("remittance basis") in a tax year and who have been UK resident for 12 or more of the 14 years prior to the year of claim (it should be noted that the £30,000 RBC will remain for shorter term "long-term residents");

- enabling non-domiciles to remit overseas income and capital gains tax free to the UK for the purpose of commercial investment in UK businesses; and

- making technical simplifications to some aspects of the current remittance basis rules to remove undue administrative burdens.

The Government has issued a consultation paper and seeks views from interested parties by 9 September 2011. It intends that the measures will be implemented from April 2012.

CONSULTATION ON UK TAX RESIDENCE STATUS

Most would accept that the current rules that determine tax residence for individuals are complicated and unclear. The number and frequency of cases going to court on the subject provide further corroboration for this view. In its Budget 2011 the Government announced that it would introduce a statutory definition of tax residence. Consultation has now begun and runs to 9 September 2011. Its aim is to create clear rules that provide greater certainty for taxpayers and are simple to use.

The first chapter of the consultation document includes the statement that the existing rules are *" ..vague, complicated and perceived to be subjective."*

It is also stated that *".. the Government agreed that this lack of certainty is unsatisfactory"*. A statutory residence test should be designed, say HM Treasury in chapter 3, to provide a simple process and clear outcomes for the vast majority of people whose affairs are relatively straightforward. In keeping with this, three categories of individual have been proposed:

- conclusive non-resident, where the individual is present in the UK for fewer than 10 days or has been non-resident in the UK in each of the previous 3 tax years and is present in the UK for fewer than 45 days in the current tax year, or leaves the UK to work full-time abroad and is present in the UK for fewer than 90 days in the tax year and no more than 20 days are spent working in the UK in the tax year

- conclusive resident, where the individual either spends more than 183 days in the UK, or has only one home which is in the UK or carries out full-time work in the UK

- individuals who are neither conclusive non-resident nor concl usive resident.

The first two categories appear to be relatively straightforward - well at least the rules are clearly stated. The more detailed changes to the rules on residence are in relation to the third category.

For the third category the new test will take into account both time spent in the UK and the other connections that the individual has with the UK. It is also intended that very clear rules will be set out for so-called "arrivers" and "leavers". This new "category three" test will effectively involve running through a checklist. Whereas working out residence currently involves weighing up different factors, in the future it will be necessary to do "day counting" and to take into account other relevant factors. These will include the presence of a UK resident family, substantive UK employment (that is employment in the UK for 40 or more days in the tax year), having accessible accommodation in the UK; and spending 90 days or more in the UK in either of the two tax years prior to the tax year in question.

The Government's intention is to implement these measures from April 2012.

GOVERNMENT SETS OUT ITS PUBLIC SECTOR PENSIONS AGENDA

In a speech to the Institute for Public Policy Research, Danny Alexander, Chief Secretary to the Treasury, indicated the proposed changes to public sector pensions following the Hutton Report.

The main changes proposed are as follows:

- The normal pension age under public sector schemes will in future replicate State Pension Age, including increasing as and when State Pension Age increases. There will, however, be an exception for the uniformed services (armed forces, police and firefighters) whose pension age will be 60.

- Although the normal pension age will be increased any benefits accrued up to the date of the change will still be payable from the current scheme pension ages.

- The benefit accrual basis will be changed from final salary to career average for future scheme service from an as yet unspecified date. Benefits accrued up to the date of change will continue to be based on final salary.

- From April 2012 an increase in member contributions will be phased in. The final average increase will be 3.2%. However, this will not be spread evenly. There will be no percentage increase in contributions for those earning less than £15,000, while a maximum increase of 1.5% will apply for those with earnings between £15,000 and £18,000. In addition the increased contributions will be phased in over three years, with 40% of the increase being met in year 1, 80% in year 2 and 100% in the third year.

These changes would be on top of the move in the pension increase/revaluation from an RPI to CPI basis.

INCOME WITHDRAWAL RATE FOR JULY 2011

The appropriate gilt yield, used to determine the 'relevant annuity rate' from HMRC's tables for an adult member commencing income withdrawals (or reaching an income withdrawal review date), in July 2011 is 3.75%.