Technical Connection

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WILL AID SURVEY

The 2012 Will Aid survey reveals that (roughly) two thirds of people in the UK do not have a will.

Of these two thirds, some have just not bothered, some will be (as the report says) ‘procrastinating’, some will be under a misapprehension about what the intestacy provisions provide, and some (probably a relatively small, well-informed segment) will be happy with what the intestacy provisions provide.

These latest findings provide a tremendous opportunity to ‘audit’ clients to ascertain:

- their estate planning aspirations
- whether they have a will
- whether they have the ambition/assets to plan
- whether any financial services/trust-based solutions might be appropriate.

This can also offer a potentially attractive means of collaboration with solicitors.

BE CAREFUL HOW BONDS ARE ENCASHED

Single premium investment bonds can be very tax efficient investments. For example, they offer the following qualities:-

- they are non-income producing and therefore no taxable income is generated each year

- there is an ability to switch between different investment funds without any tax charge

- a 5% withdrawal facility exists whereby funds of up to 5% of the premium paid can, each year, be accessed without any immediate tax charge

- there is an ability to transfer ownership of the bond – by assignment – with no capital gains tax or income tax charge at that time

However, there can be traps – particularly on encashment. If a client wishes to access a substantial part of the bond, whilst it may seem convenient to use the part surrender/ withdrawal facility, this can lead to a bad tax result. For example, if the surrender proceeds exceed the available 5% withdrawal allowance, a chargeable event gain may arise. This is very likely to occur if the bond withdrawal is substantial and/or it happens early in the lifetime of the bond. This means that a tax charge could arise on a deemed taxable profit in cases where there is in fact no economic profit.

This potential problem can often be avoided by using a system known as "segment encashment". A single premium investment bond is generally made up of a number of individual policies known as "segments". By encashing whole segments, the individual will pay tax on the actual profit under those segments which will frequently be much less than any "deemed" profit that arises on a large part surrender of the whole bond.

CHILD BENEFIT AND CHILD TAX CREDIT – THE ZAMBRANO CASE

The Child Benefit and Child Tax Credit (Miscellaneous Amendments) Regulations 2012 SI 2012 No. 2612 were laid on 16 October 2012 and come into effect from 8 November 2012. The amendments aim to maintain the Government's current position regarding third country nationals accessing child benefit and the child tax credit. To be eligible for child benefit a person must be in Great Britain/Northern Ireland and for the child tax credit must be in the United Kingdom.

Third country nationals (ie persons from outside the EU/EEA) have a right to stay in the United Kingdom under leave to enter or remain which is granted under the Immigration Act 1971. Many third country nationals are granted leave which is conditional on them having no recourse to "public funds" (which includes items such as child benefit and the child tax credit).

Some third country nationals may have a right to reside by virtue of EU law, for example third country nationals who are family members of EU/EEA nationals with their own right to reside, such as the spouse or child of an EU/EEA worker or self- employed person. However, they would not be entitled to claim public funds (as stated above).

However, in the case of Gerardo Ruiz Zambrano v Office National d'Emploi, the CJEU ruled on 8 March 2011 that a third country national with a right to reside under EU law has to be treated as a citizen of the EU with all of the rights and duties which this brings. These would include (in the UK) the right to claim child benefit and the child tax credit.

The effect of the amendments is that those persons who are within the scope of the Zambrano ruling are treated as not being in Great Britain/Northern Ireland for the purpose of eligibility for child benefit and are treated as not being in the United Kingdom for the purpose of eligibility for the child tax credit.

A QUICK REMINDER ABOUT SEX

On December 21 the distinction between men and women will officially disappear as far as insurance companies are concerned, whatever the type of insurance. This is the result of a European Court of Justice decision in March of last year and will affect all *new* policies.

For a man about to retire…

A man can expect annuity rates to drop on 21 December, all other things being equal. Women live longer than men and 'unisex' annuity rates will therefore be somewhere between the male and female rates. It is likely some companies will make the change before 21 December, so somebody who is planning to spend their pension pot on an annuity will need to act fast. It could even pay to bring forward a retirement date a few weeks.

For a woman needing life assurance…

Because women live longer, their life assurance premiums are currently less than those of men of the same age. Unisex life assurance rates are therefore likely to be higher for women than current rates. Once again the message is that deferral could be expensive.

EXCEPTED ESTATES

HMRC is piloting a change in the way it monitors excepted estates

For IHT purposes, an excepted estate is one where (subject to various other conditions being satisfied) the total gross value of the estate before death does not exceed a specified amount which is fixed from time to time.

If an estate qualifies as an excepted estate the personal representatives of that excepted estate do not have to deliver a full account (form IHT 400) to HMRC before obtaining a grant of representation. Instead, in the case of an excepted estate, form IHT 205 (Return of estate information which runs to 4 pages) has to be submitted when the grant of representation is applied for. The form IHT 205 is a slimmed down version of form IHT 400. In appropriate cases, this can considerably speed up the administration of an estate.

It has been reported that HMRC is currently piloting a change in the way it monitors excepted estates and tackles non-compliance. Previously it examined a selection of estates at random and contacted the taxpayer within the 35 (England) or 60 (Scotland) day statutory clearance period if it had any questions in relation to those grants.

Now HMRC is comparing the data provided on death with data provided by the deceased during their lifetime and information from other sources. Armed with this information, HMRC will concentrate its efforts on estates where the information it has suggests an estate does not satisfy the various conditions to be an excepted estate. If an estate does not satisfy the conditions it will not be an excepted estate with the result that the statutory clearance period will not apply. This will allow HMRC to write to the taxpayer after the 35/60 day statutory clearance period has expired. In applying this new practice, though, HMRC will only take action in cases where evidence strongly suggests that the estate was never an excepted estate.

ADVISER CHARGING AND VAT

HMRC has very recently pronounced on VAT and charges for ongoing reviews. It has said:

'The HMRC position on review/ongoing services has not changed from that published in its guidance. The services of an IFA signing up a client to a periodic review service at the time the client buys their exempt financial products will be an ancillary part of the exempt supply of intermediation. This is on the understanding, however, that the periodic review service is a relatively minor element of the overall supply in terms of both what is provided and what is charged for it'

'In any other circumstances - i.e. where the review services are not transacted as part of the original intermediation supply and form a supply in their own right - the VAT treatment will follow from the nature of the services being supplied. If a charge is made for a one-off review then the VAT treatment will be determined on exactly the same basis as the original advised sale as per the steps laid out in our RDR guidance. If, however, ongoing charges are made for portfolio review/management services that are provided on an ongoing rather than periodic basis, then the VAT treatment outlined in section 7 of Notice 701/49 will apply currently and, once it is implemented into the UK, the treatment outlined by the ECJ in Deutsche Bank will apply going forwards.'

While clearly helpful, this latest piece of guidance from HMRC requires some further clarification in relation to the meaning of "a relatively minor element of the overall supply". This would appear to be a re-emergence of a form of "predominant purpose" test with its inherent subjectivity. If the "review service " turns out not to be "relatively minor" then it would seem to require some intermediation (ie a customer specific act between the adviser and the product provider with a view to bringing about the sale of a retail financial product") in order to be a VAT exempt supply.

As was discussed in relation to the assumed position before this additional HMRC clarification, some may take the view that in light of the inherent uncertainty over what constitutes "a relatively minor element of the overall supply", (and of course this may be further clarified) in order to be certain small actual re-balancings may take place so as to ensure that intermediation and resulting VAT exemption takes place. Aside from the FSA suitability aspects of giving this advice (it is interesting to consider whether, although "unsuitable from an investment standpoint", an otherwise unnecessary re-balancing could be justified as "suitable" overall as it saves VAT) there is also the possibility that over time and based on inspections, HMRC may seek to tighten the rules to prevent this means of avoiding the payment of VAT. One way of doing this could be to introduce a form of the previously-discussed "predominant purpose" rules. It is stressed, however, that there has been no suggestion so far that this is under consideration.

In the light of this uncertainty, further expressions of disquiet were made to HMRC who responded (to the PFS) with this latest statement in relation to the VAT status of charges for a review service:

'Ordinary VAT rules on single/multiple supplies will apply where a periodic review service is provided with an initial service of intermediation. It is not possible to cover all possible scenarios and all the relevant factors (such as contractual arrangements, pricing structures, customer requirements etc) will need to be taken into account when determining the VAT treatment. However, as a general rule, HMRC will see a periodic (usually annual) review to check asset allocation and risk profile, which is contracted for at the same time as the initial intermediation, as being ancillary to the principal supply of exempt intermediation.

As we've said previously, we have to agree VAT treatments post-RDR that comply with VAT law but that can be applied practically on the ground. We recognise that it would not be acceptable to base VAT treatment on something that's uncertain at the point of contracting with the client and requires the adviser to look back retrospectively and adjust the VAT treatment accordingly.'

This further elucidation is, of course, most welcome and, it would seem, be strongly indicative of a relatively benign HMRC view in relation to this very important matter. This should be read in conjunction with the fact that in many cases an actual purchase of a retail investment product will take place as a result of a review, and that £77,000 of VATable turnover is the registration threshold. With much initial financial advice representing VAT exempt intermediation (as it is likely to incorporate an actual sale of a retail investment product) this may mean that many advisers will be reassured by the position as it stands. Having said that one must keep in mind (in relation to the ongoing charges issue) that HMRC states that the likely VAT freedom of the review service when it was contracted for (as part of the initial exempt intermediation) will be "the general rule". Only the outcome of VAT inspections and practical experience will give the sector the full reassurance that it craves. But this latest statement from HMRC must be seen as positive. Advisers are encouraged to take advice from their own tax advisers as to how to deal with the VATable or exempt status of their various supplies.

PENSIONS AFTER THE FSA CHANGES

At the beginning of November the FSA issued a consultation paper CP12/29 and a policy statement PS12/17, which will have a major impact on pensions as follows:-

New illustration rates

Earlier this year the FSA launched a consultation paper on the projection rates to be produced in illustrations. Following that consultation it has now announced that with effect from 6 April 2014 the lower, intermediate and higher projections will be amended as follows:

Rate	**Current %**	**New %**
Lower	5	2
Intermediate	7	5
Higher	9	8

The wording about appropriate return rates (below the maxima) will also be revised to require that firms use ‘rates that accurately reflect the investment potential of the product’. The FSA has also included a transitional rule to allow the new rates to be used at any time from 6 April 2013, which means firms ‘can make changes to their systems and documentation at the same time as other changes’.

The FSA has also set out proposals in CP12/29 for inflation-adjusted personal pension illustrations. The proposals, which would apply to SIPPs as well as personal pensions, are:

- Pension illustrations, including generic illustrations, should be based on real growth rates, using the standard return assumptions, discounted by a single inflation assumption (2.5% - the same as applies to Statutory Money Purchase Illustrations [SMPIs]).

- Providers would no longer be able to supply any other deterministic (assumed growth rate) projections not required by the FSA. Although the paper focuses on personal pensions, the FSA proposes that this restriction should apply to *all* life and pensions Key Features Illustrations (KFIs).

- As now, stochastic projections (probability-based) can be provided, but only if there are 'reasonable grounds for believing that a consumer will be able to understand them'. To be consistent with the new inflation-adjusted deterministic KFIs, stochastic projections for pensions would have to be in real terms.

- For projections on existing business, it would no longer be possible to omit the intermediate growth rate (7% going down to 5% before inflation adjustment).

- Income drawdown illustrations would remain as they are now, with the proviso that COBS 13 Annex 2. 2.9R would be amended to place an age limit of 99 on the analysis where the pension fund will not be exhausted at the higher rate of return.

The FSA says, 'There are other types of projection or quotation where a consumer may find it helpful to see the possible impact of inflation on the value of the benefits. These are transfer value analyses and conventional and investment-linked annuities'. However, it does not make specific proposals in these areas but instead asks for 'views on whether there should be a mandatory statement of the effect of inflation on annuity quotations or illustrative examples of the buying power of the annuity after, say, 10 or 20 years'.

The consultation ends on 1 February 2013 and the new inflation adjusted illustrations will also take mandatory effect from 6 April 2014, the same date as for the change in the projection rates. Once again a transition period will permit their early use from 6 April 2013.

Although there has not yet been any announcement from the Financial Reporting Council on any changes to apply to SMPIs, it is expected that these will dovetail with the new FSA rules.

Although these changes more appropriately reflect the current economic and investment environment, they will mean that the projected benefits for new and existing pension clients will be significantly reduced. New clients may be put off pension provision by the need to pay ever increasing contributions to provide their target pension income, while existing clients may see this as further evidence of the personal pension malaise. It is clear that these changes need to be fully explained to clients, so that their introduction does not come as a nasty shock.

Alongside the consultation on projections the FSA also commented on the quality of product information, and highlighted that it was not happy with the quality of many of the KFIs it had seen.

SIPP disclosure

While the above changes apply to all types of money purchase pension arrangements, the FSA also made the following significant changes to the SIPP disclosure provisions, which will take effect from 6 April 2013.

- The current SIPP exemptions for Key Features Illustrations (KFIs), Effect of Charges (EoC) tables and Reduction in Yield (RIY) information will be removed. The FSA says that 'Given the wide scope of the 'SIPP' definition which we discussed in http://www.fsa.gov.uk/pubs/cp/cp11_03.pdf CP11/3, the growth in the SIPP market, and the poor disclosure documents identified we cannot justify maintaining the status quo'.

- As part of the KFI, SIPP providers must disclose details of the interest to be paid to clients on money invested within the scheme. They must also disclose, as part of 'the appropriate charges information', any interest on money held within the scheme that is retained by the scheme operator and/or the scheme trustee.

- A parallel requirement to require providers to disclose commissions received and retained has been put on hold while the FSA develops its rules for platforms, which ultimately will not be able to be financed product providers.

  In the interim the FSA has effectively forced such disclosure on SIPP providers by saying in the paper that 'If commissions are received, we take the view that, taking into account the information needs of their clients, firms should disclose these payments and obtain informed consent from their clients to any commission that is retained'.

PLAIN SAILING FOR AUTOMATIC ENROLMENT?

Although automatic enrolment has commenced at long last, the recent 2012 Smaller Firms Pension Survey, undertaken by the Association of Consulting Actuaries (ACA), has highlighted a number of worrying concerns about the awareness of auto enrolment among smaller employers.

Auto enrolment will largely be judged on how successfully it includes employees in smaller employers. Surveys have consistently shown that the lack of private pension provision is at its greatest among such employers. It is therefore somewhat concerning that the ACA survey shows that 82% of SMEs are unaware of the regulatory regime regarding auto enrolment. While it is true that it is still some three or more years away before such employers with 50 or less employees will need to auto enrol their employees, there is a clear need for professional advice.

INVESTMENT RETURN ASSUMPTIONS – TAX-DISADVANTAGED PRODUCTS

Following the consultation on projection rates mentioned in the "Pensions after the FSA changes" article above, with effect from 6 April 2014 the lower, intermediate and higher projections for tax-advantaged products (eg. life products) will be amended as follows:-

Rate	**Current %**	**New %**
Lower	4	1.5
Intermediate	6	4.5
Higher	8	7.5

CHILD BENEFIT TAX CHARGE

HMRC has started to issue letters about the Child Benefit tax charge

During November, HMRC will be sending out 'around one million' letters to families affected by the introduction on 7 January 2013 of the High Income Child Benefit Charge (the correct name for what is usually called child benefit tax). For reasons best known to itself, HMRC did not publish this fact on its 'What's New' web page, but buried it under press releases. The one million figure is less than the 1.2 million families that HMRC's earlier impact assessment estimated would be within the new tax charge, although no explanation why is given.

The letter (reference P113) is only a page long and is accompanied by a one page flow chart. The letter is somewhat ambiguous in saying that if 'you, or your partner have an individual income of more than £50,000 a year…then you will have to pay a tax charge on some, or all of the Child Benefit that you receive'. In practice, the tax charge is only levied on the individual with the highest income above £50,000. The flow chart perpetrates this confusion by using the same approach to say 'You or your partner can decide to KEEP receiving Child Benefit payments' in which case 'You will have to register for Self Assessment (unless you are already registered) [and] fill in a Self Assessment Tax Return every year'.

The impact assessment estimated that about 70% of those who face a tax charge will have an income of £60,000 or more and thus lose the full value of their Child Benefit. From HMRC's viewpoint, it would like that 70% to stop receiving Child Benefit from 7 January 2013. The HMRC Child Benefit charge website has an online form to 'request not to receive Child Benefit payments'. The website also has a restart form. Where the restart is because of a drop in income below £60,000, the form can be lodged up to two years after the end of the tax year in which income dropped below the £60,000 threshold.

For the 30% subject to a partial tax charge, the first port of call should be tax planning strategies, although HMRC does not suggest this. Otherwise there is no alternative but to continue with receipt of Child Benefit and deal with the Self Assessment Tax Return each year. HMRC's impact assessment was that it would end up issuing an extra 500,000 returns every year to gain the necessary data – hence its correspondence encourages the £60,000+ group to stop benefit receipt.

COMMENT

Stopping receipt of Child Benefit is not the same as revoking a claim to Child Benefit. It will still be necessary to complete a Child Benefit claim form for any new children to protect entitlement to NIC credits and certain benefits such as Guardian's Allowance.

INCOME WITHDRAWAL RATE FOR NOVEMBER 2012

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 November 2012 is 2.0%.