Technical Connection

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THE PERSONAL SAVINGS ALLOWANCE

The Finance Bill 2016 draft clauses have revealed more detail about the forthcoming personal savings allowance

When the Chancellor announced the personal savings allowance (PSA) in the March 2015 Budget, we were all left guessing how it would work in practice. Very little in the way of background information appeared beyond a consultation issued in July on the implications for savings not covered by the tax deduction scheme for interest (TDSI).

The publication of the Finance Bill 2016 draft clauses, supporting papers and a response to the TDSI consultation now give us a clearer – but not yet definitive – picture of the PSA:

- First off – and most irritating – the PSA proves not to be an allowance. Once an explanation of the dividend allowance emerged, there was always a suspicion that the PSA would be another 0% tax band and this proves to be the case. To quote the Tax Information and Impact Notes on the PSA, 'Income that is within an individual's savings allowance will still count towards their basic or higher rate limits'. The result is that there will be two 0% bands for savings income, as the £5,000 starting rate band will continue, subject to its own different set of rules.

- The PSA will have two cliff edges. The basic PSA is £1,000 but

    - if *any* of an individual's income attracts higher rate tax, then the PSA is £500; and

- if *any* of an individual's income attracts additional rate tax, then the PSA is nil.

  In other words, there is no tapering.

- From 6 April 2016 banks, building societies and NS&I will no longer be required to deduct tax from interest. However, despite the Summer consultation, 'The government has not yet reached a decision on this question [of gross payments] in respect of authorised investment funds, investment trusts and P2P lending. The government is continuing to analyse information provided to understand fully the impact of potential changes, and an announcement will be made as soon as possible.' Given that the start of the new tax year is less than four months away, this means no change and a boost for offshore fixed interest funds (which pay interest gross) over their onshore (net-paying) competitors.

  In the case of interest arising in the policyholder funds of a life assurance company, the rumours that change would occur have proved incorrect: 'the government has not identified a compelling case for specific changes, and does not intend to amend the existing arrangements.'

- The government estimates that the PSA will give 18m people a tax reduction on their savings income averaging £25 a year. 'Around 95% of taxpayers' will not have any tax to pay on their savings income. However, 1.4m people will still have tax to pay on savings income and, as HMRC notes 'Most will be additional rate taxpayers or individuals with higher than average savings'.

  HMRC says that it "will introduce automated coding out of savings income that remains taxable through the Pay As You Earn (PAYE) system, on the basis of information supplied by account *providers* [our italics]". HMRC promises that "further details for customers will be provided in good time before any tax becomes due," and in the longer term is relying upon the planned digital tax accounts to deal with the issue.

  Two groups will potentially face more tax compliance: trustees and executors. Neither will benefit from the PSA, but both will have to deal with gross interest payments and accounting for the tax due on them.

COMMENT

We have used the words of former US Treasury Secretary William Simon before and it is worth repeating them now: we should have a tax system which looks "like someone designed it on purpose". It would be very hard to say that about the starting rate band for savings and the new personal savings allowance.

REDUCTION IN THE LIFETIME ALLOWANCE: FIXED & INDIVIDUAL PROTECTION 2016

Detailed provisions for Fixed & Individual Protection have been published

In line with the publication of the draft clauses of the Finance Bill 2016 the government has published detailed provisions on the reduction of the Lifetime Allowance (LTA) and the 2 new layers of transitional protection.

The reduction in the LTA affects those who could have pension wealth between the new and the old LTAs when they retire. Around 55,000 individuals are expected to have pension assets that are worth between £1 million and £1.25 million in 2016/2017.

The detailed provisions confirm that Fixed Protection 16 (FP16) and Individual Protection 16 (IP16) will work in a similar way to the two previous transitional protection regimes, Fixed Protection 14 (FP14) and Individual Protection 14 (IP14). Individuals have to obtain a reference number from HMRC if they want to rely on FP16 or IP16 before they take their benefits. Individuals with FP16 will have a personal LTA equal to the greater of £1.25 million and the standard LTA. Individuals with IP16 will have a protected LTA of the value of their pension savings on 5 April 2016 subject to an overall limit of £1.25 million.

The conditions for maintaining FP16 include the following:

- individuals in defined contribution pension schemes must ensure that no further pension contributions are received by the scheme on or after 6 April 2016

- individuals in a defined benefits scheme must not accrue further benefits above a ’relevant percentage’ after 5 April 2016. The relevant percentage for defined benefit savings will normally be either the annual rate specified in the scheme rules as of 9 December 2015 for the revaluation of accrued rights, or the CPI (if no rate is specified), although certain statutory increases will be excluded from the test.

Individuals with IP16 will be able to carry on actively saving in a registered pension scheme, should they so wish, but would be subject to the LTA charge on any excess savings over their personal LTA when they take their benefits.

Relieved members of relieved non-UK pension schemes will also be able to apply for FP16 subject to them not paying a contribution on or after 6 April 2016 to their non-UK pension scheme.

An amendment will be made to ensure that, where an individual dies before 6 April 2016, but a relevant lump sum death benefit is paid on or after 6 April 2016, the relevant lump sum death benefit will be tested against the standard LTA at the time of the individual’s death.

Individuals will be able to apply for both FP16 and IP16. Where an individual holds FP16 and IP16, FP16 will take precedence, but should this be lost the individual will revert to IP16.

Changes are also being made to Finance Act 2004 to ensure that individuals who have primary or enhanced protection, with no lump sum protection, receive the pension commencement lump sum intended by the legislation.

COMMENT

The transitional arrangements for electing FP16 or IP16 are still outstanding. The online system for elections is not expected until July 2016.

FINAL UK DISCLOSURE OPPORTUNITY EXTENDED

In the March 2015 Budget it was announced that with the coming to an end of the existing offshore disclosure facilities a new offshore disclosure facility would be made available next year to cover income tax, capital gains tax and inheritance tax which would run until mid-2017.

The final opportunity for UK taxpayers to disclose offshore tax irregularities will run from April 2016 until September 2018, a year longer than previously anticipated. It was announced in the March 2015 Budget that the existing offshore disclosure opportunities – the Liechtenstein Disclosure Facility (LDF) and Crown Dependencies Disclosure Facilities – would close at the end of 2015. At the same time, HMRC would begin receiving routine reports of UK residents' overseas accounts, from many jurisdictions, under the OECD Common Reporting Standard.

While we do not have full details of this new disclosure facility, it is expected that it will be much more restrictive than the existing facilities. Moreover, it will also coincide with the introduction of stringent new civil penalties for offshore tax evasion, including a new penalty based on the value of the undeclared assets in the most serious cases.

The draft legislation for the new civil penalty regime is included in the 2016 Finance Bill, although the relevant provisions will be subject to a commencement order to coordinate their introduction with the new last-chance disclosure regime. Once the provisions are in force, the minimum civil penalties for offshore inaccuracies involving 'deliberate' and 'deliberate and concealed' behaviour will be increased by 10% of the potential lost revenue, according to a government policy paper. Penalties for 'careless' behaviour will not increase.

The 2016 Finance Bill also includes an asset-based penalty, which will apply when inaccurate returns involving deliberate, or deliberate and concealed, behaviour are made to HMRC and the inaccuracy relates to offshore income or gains. The penalty will be based on the underlying asset from which the income or gain that was subsequently evaded was derived, for example, an offshore bank account where the interest was not declared. The government will publish draft clauses for this penalty for "informal consultation" early in 2016, according to the policy paper.

COMMENT

Advisers with clients who have sources of offshore income or gains should ensure that they are fully aware of the requirement for UK resident domiciliaries to report all income and gains from abroad ...and if they haven't to date, to see whether any of the current of forthcoming disclosure provisions may be relevant. Expert practitioner-based guidance and advice will be necessary.

DIVIDENDS – FINANCE BILL 2016 DRAFT CLAUSES

The Finance Bill 2016 draft clauses still leave unanswered questions on dividend taxation

In our July Bulletin we set out the background to, and our understanding of, the July Budget announcement on dividend tax reform. At the time we made clear that detailed information was lacking, leaving a number of questions unanswered.

While a dividend allowance factsheet, issued by HMRC in August, did give a little more insight – the allowance is *not* an allowance – we were still left waiting for the full facts. The Autumn

Statement said nothing, so our hopes then turned to the draft Finance Bill 2016 clauses and accompanying material, which emerged on 10 December. Alas, we are still scratching our heads – but see the clarification received below.

Tax Information and Impact Notes (TIIN) on dividend taxation set out the new tax rates for individuals beyond their £5,000 dividend allowance (7.5% basic rate, 32.5% higher rate and 38.1% additional rate). However, the relevant draft clause only spells out that 'The dividend nil rate is 0%' (surprise, surprise!) in a new subsection A1 to section 8 ITA 2007. Section 8 contains the dividend tax rates, but there are no changes to the existing rates made by the draft clause. Similarly, the draft clause does not reach section 9 ITA 2007, which defines the dividend trust rate.

At one level it is certainly odd that the new dividend tax rates have been omitted from the draft clauses. However, if one considers that the purpose of issuing draft clauses is to secure feedback and comment then maybe it was thought that it was unnecessary to secure comment on the rates themselves (pure numbers that the government has made clear in the TIIN and policy statements as opposed to legislative form and structure) and they will go straight into the Bill without being put out for comment.

We wrote to HMRC for clarification on these points and it has responded that clauses that 'merely change rates are published on or around Budget day…. When *the Bill* (our words in italics) is published the rates will be as you have stated'. As regards the dividend trust rate, HMRC stated …. 'it is proposed that the dividend trust rate will continue to mirror the dividend additional rate, so will be 38.1%. Similarly, it is proposed that trustees will not qualify for the new dividend allowance' (or more correctly zero rate band).

The other draft clause (12 pages long) deals with consequences flowing from the abolition of tax credits. These include the repeal of the concept of "franked investment income", which was defined in terms of tax credit entitlement. In its place we have "exempt ABGH distributions", so named because they are distributions falling within paragraphs A, B, G or H of section 1000(1) of CTA 2010.

COMMENT

The position with regard to the taxation of dividends for life companies remains unclear. The fact that the government has made no changes to the taxation of interest for life companies, despite the creation of the personal savings allowance, makes a 7.5% (basic rate) charge look more of a possibility. We have asked HMRC to clarify the position.

ADVICE REQUIREMENT FOR THE SECOND-HAND ANNUITY MARKET

The government has announced that it will be making provisions in the Bank of England and Financial Services Bill to extend the free and impartial Pension Wise guidance service to those annuity holders who wish to sell their annuity income streams.

From 2017, the government is removing the tax restrictions on people seeking to assign their annuity income to firms wishing to purchase it. Individuals who want to will be able to take the proceeds of their assignment and save or spend them as they see fit, taxed only at their marginal rate(s).

It is important that people are in a position to make an informed decision and for many people keeping their annuity income will be the right decision as it provides a stable and guaranteed income. The amendments to the Bill will:

- compel the FCA to make rules requiring certain authorised entities to check that holders of a relevant annuity have received appropriate financial advice before they may sell their annuity;
- provide the Treasury with delegated powers to determine what a 'relevant annuity' is, including what the threshold should be, how it should be calculated and whether it should take into account an individual's circumstances; and
- give the Treasury delegated powers to specify what is meant by appropriate financial advice.

The government will, in due course, consult over secondary legislation setting out details of how the advice requirement will operate – including threshold criteria.

This legislative approach is consistent with the approach used for the advice requirement for individuals considering whether to transfer from defined benefit to defined contribution pensions, as set out in the Pension Schemes Act 2015.

THE OFFICE OF THE PUBLIC GUARDIAN PUBLISHES DETAILS OF ITS INVESTIGATIONS POLICY

The Office of the Public Guardian (OPG) has published a policy document outlining its role in protecting vulnerable adults in England and Wales and its procedure for investigating the suspected misuse of powers of attorney.

The OPG was established in October 2007 by the Mental Capacity Act 2005 (MCA) to safeguard the interests of people who may lack the mental capacity to make certain decisions for themselves – including those whose affairs are managed by an attorney or deputy.

One of the ways in which the OPG does this is to raise awareness of the potential for abuse and investigate any concerns that are reported about the actions of attorneys and deputies. According to the policy document, while the following are not necessarily indicative of abuse they may excite the suspicion of the OPG and warrant further investigation:

- Changes in living conditions
- Sale of possessions
- Inability to pay bills, or an unexplained lack of money
- Money being taken out of an account without a reason
- Financial documents being lost without a reason
- Someone being cut off from family, friends or their social network
- The attorney or deputy having more money to spend on things like clothes, travel or accommodation
- Sudden changes to a bank account or how someone uses it
- New, recent authorised signatories on a client's or donor's account card
- Money being taken without permission from the vulnerable person's ATM card
- Changes in how an ATM card is being used (such as more frequently or from different locations)
- Sudden or unexpected changes to someone's Will or other financial documents

An investigation would typically involve contacting people and agencies linked to the client (including the deputy or attorney) and requesting and reviewing copies of accounts, financial transactions and other documents. An investigation could lead to the OPG applying to the Court of Protection to suspend, discharge or replace a deputy or to cancel or revoke an EPA or LPA. In extreme cases, where theft or fraud is suspected, the abuse may be reported to the police.

COMMENT

The policy document serves as a reminder that the role of attorney or deputy should not be taken lightly and the attorney/deputy must not be tempted to use the donor's account for their own purposes even if there is no deliberate intention to defraud or deceive. Good record-keeping will be essential in the event that any form of dispute arises.

EMERGENCY PAUSE IN PLACE FOR AUTOMATIC ENROLMENT

As a result of on-going testing and contingency planning an emergency pause facility has been put in place

The National Audit Office (NAO) has published a report which states that as a last resort an 'emergency pause' procedure has been put in place that can apply if automatic enrolment is unable to cope with unexpected increases in demand over the coming months.

This NAO Automatic-enrolment-to-workplace-pensions report acknowledged the good work that has been done to introduce the automatic enrolment programme and that more people are now saving for retirement. However, also highlighted is that significant risks remain as 1.8 million smaller employers are required to enrol their workers by 2018.

The report finds that while most eligible workers work for larger employers and have already enrolled, the vast majority of employers still have to start automatic enrolment and these smaller employers are expected to have different requirements and responses to the process.

Within the report it states that the Department for Work and Pensions (DWP) team '…*reviews data, providing early warnings of problems ahead, and has held contingency planning workshops. As a last resort it has set out an 'emergency pause' procedure to apply if the programme was unable to cope with unexpected increases in demand or changes in behaviour*.'

The report goes on to say that the DWP, The Pensions Regulator (TPR) and NEST are continuing to develop the range of responses they might introduce if demand rises.

COMMENT

In July we reported news that analysis from TPR showed that more business start-ups and a lower number of closures mean around half a million more SMEs will have automatic enrolment duties than previously estimated. If this 'emergency pause' is put into place then these small and micro employers who are still to stage may well find themselves with more preparation time for their automatic enrolment duties.

SCOTTISH RATE OF INCOME TAX SET AT 10% FOR 2016/17

On 16 December it was announced that the Scottish Rate of Income Tax (SRIT) will be 10% for 2016/17. Taking account of the 10% reduction, from April 2016, in the main rates paid by Scottish residents in the UK, this means that the rates of income tax paid by Scottish taxpayers will be the same as those in the rest of the UK. The absence of change must be seen as good news for pension administrators around the UK. There will be no need to change how they report or make payments for income tax to HMRC other than to apply the SRIT tax code (with the "S" prefix) to their Scottish taxpayer pensioner members.

INNOVATIVE FINANCE ISA AND PEER-TO-PEER LOANS

HMRC has published draft regulations, together with explanatory notes, establishing a new innovative finance ISA which is to be available from 6 April 2016. The draft regulations are subject to consultation until 1 February 2016.

Under this new account, interest and gains from peer-to-peer loans paid into an ISA can benefit from the ISA tax advantages. The new ISA will be offered by peer-to-peer lending platforms with the appropriate regulatory permissions. Any investment amount will count towards the maximum ISA subscription.

INCOME WITHDRAWAL RATE FOR JANUARY 2016

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 January 2016 is 2.25%.