Volume 29 Issue 4 – January 2016

Technical Connection

CONTENTS

Published by Technical Connection Ltd,
7 Staple Inn, London, WC1V 7QH.
Tel: 020 7405 1600 Fax: 020 7405 1601
E-mail: enquiries@technicalconnection.co.uk
www.techlink.co.uk

ANOTHER RECORD BREAKING YEAR FOR SELF-ASSESSMENT RETURNS

HMRC has revealed that 10.39 million self-assessment tax returns were completed ahead of the 31 January deadline; that's over 92% of the total returns expected, and 150,000 more than last year.

Over 89% of customers, 9.24 million, opted to use HMRC's online self-assessment service to calculate and pay the tax they owe, continuing the growing trend of dealing with the tax authorities electronically.

This year HMRC's online self-assessment service saw some changes together with more up-to-date online tools and the launch of the Personal Tax Account, which was accessed by more than 825,000 customers as they completed their tax returns. These changes have made the process simpler and easier than ever before.

And, by using new technology, HMRC has successfully checked 3.4 million returns and intercepted more than £96 million worth of fraudulent or incorrect repayment claims. This technology prevents criminal attacks and ensures that customers with legitimate claims are protected.

PENSION BENEFITS WITH A GUARANTEE AND THE ADVICE REQUIREMENT

Between 23 November 2015 and 15 January 2016 the government held a call for evidence on the valuation process for pensions with a guaranteed annuity rate (GAR) for the purposes of the advice requirement. This call for evidence was held in response to concerns that pension providers and pension scheme members were finding it difficult to understand when members were required to take advice before transferring such benefits, or accessing them flexibly.

The DWP noted that the majority of consultation respondents were in favour of a change to the current valuation method and the government is now considering how best to simplify the current valuation process, and is planning to consult on draft regulations later in 2016. The DWP broadly welcomed comments along these lines.

In connection with this, the DWP has now published a consultation on the valuation process for pensions with a GAR for the purposes of the advice requirement.

The DWP has also published a factsheet entitled 'Pension benefits with a guarantee and the advice requirement'. This factsheet is intended to help pension scheme providers determine whether certain types of pension benefits which contain a promise, including those with a GAR, are safeguarded benefits for the purposes of the new advice requirement; and when the exception to the requirement to take independent advice for those with safeguarded benefits worth £30,000 or less applies.

DIVIDENDS AND LIFE COMPANIES

HMRC has confirmed that there will be no change to dividend taxation for UK life companies

We have commented earlier that following the publication of the draft clauses for the Finance Bill 2016 we were still no nearer an answer on the tax treatment of dividends within the policyholders' funds of UK life companies. We made enquiries of HMRC and we have now received a reply from HMRC that states

'…it is not the intention for the proposed changes to affect the taxation of UK Life Companies. Where those companies receive income that is affected by section 102(3) Finance Act 2012, that income is taxable at the Basic Rate (currently 20%), not at the dividend ordinary rate. The abolition of the dividend tax credit and the amendment of the dividend ordinary rate should have no effect on that income. Where the company receives dividend income not affected by section 102(3), it will continue to be taxed on that income as any other company (i.e. the income will be exempt) and so the abolition of the dividend tax credit should have no effect.'

The net result in terms of effective tax rates is summarised by us in the table below:

Investor tax rate	**20%**		**40%**		**45%**	
	Direct	**Bond**	**Direct**	**Bond**	**Direct**	**Bond**
Within dividend allowance	0%	0%	0%	20%	0%	25%
Above dividend allowance	7.5%	0%	32.5%	20%	38.1%	25%

- *For basic rate taxpayers* Dividends within UK investment bonds will be taxed in the same way as dividends within the dividend allowance, but will be more favourably taxed within a bond once the allowance is exhausted as a basic rate taxpayer will have no tax to pay on a chargeable event gain (assuming the top-sliced gain keeps him/her within basic rate tax) . Above the dividend allowance a basic rate taxpayer suffers 7.5% on directly received dividends.

- *For higher and additional rate taxpayers* All dividends within UK investment bonds will ultimately be taxed at 20% (higher rate) or 25% (additional rate) because of the treatment of chargeable event gains on encashment. The bond wrapper also offers tax deferral on the underlying dividend income. The bond is thus less attractive where the dividend allowance is available, but beneficial if the allowance is exhausted by other dividend income the investor receives.

COMMENT

This "no change" approach is inconsistent with the planned treatment of interest in the context of the Personal Savings Allowance, but nonetheless welcome for that.

LONG-TERM CARE – THE DEPRIVATION OF ASSETS RULES AND GIFTS OF PROPERTY

There is anecdotal evidence that local authorities are paying closer attention to lifetime gifts of property where a subsequent application for assistance with care is made. Here we review the rules regarding the so-called "asset deprivation".

A recent case involved a widow who went into residential care. Three years earlier her husband died and because their home was owned jointly as tenants in common, it was possible for the husband's half of it to be transferred into a trust for their children under his Will. The family decided at that time to transfer the mother's half of the property into a trust as well "to make things easier" knowing that it may or may not be assessed for the mother's care needs.

Upon assessment they received a letter from the council's legal department stating that because the mother was receiving home care at the time of the transfer to the trust she had a reasonable expectation that she would need care and support in the future and, as a result, they would class the gift to the trust as deprivation.

It is well known that when carrying out the financial assessment for care home funding the council will ask a question similar to: "Do you or have you ever owned a property?" If the answer is "Yes" and you have given it away they would then make enquiries as to the reasons why you gifted the asset.

The key point is that if the gift is treated as deliberate deprivation, the local authority will treat it as "notional capital" which will affect the eligibility for local authority funding.

So how does the local authority decide whether there was a deliberate deprivation?

There may be more than one reason for disposing of a capital asset, only one of which is to avoid a charge for care. Avoiding the charge need not be the main motive, but it must be a significant one.

When deciding if deprivation was 'deliberate' the local authority might look at the following:

- **Motive/intention:** when disposing of assets, was the main reason to avoid care charges?

- **Timing:** there is no set time limit, although local authorities are unlikely to investigate too far back. Most importantly, they will look at the time between the person realising that they needed care and the disposal of the assets.

- **Amount:** was the gift a significant amount that would make a difference to a relative's capital limit? The asset would have to be worth a significant amount for the local authority to pursue this action. Giving away a £300,000 property, for example, would significantly affect the individual's total capital whereas smaller 'gifts' – such as giving a £300 ring to a granddaughter – are unlikely to prompt further investigation.

It all boils down to intention. When the person made the gift, could they have reasonably known that they might need care? For example, if the individual was already ill when they signed their property over to a relative, that would look suspiciously like 'deliberate deprivation'.

Guidance on applying the principles of notional capital are included in the Care and Support Statutory Guidance 2014 (which supplements the Care and Support (Charging and Assessment of Resources) Regulations 2014 and which has superseded the Charging for Residential Accommodation Guide (CRAG)). The guidance incorporates the notion of reasonableness. For example, paragraph 12 of Annex E states that 'it would be unreasonable to decide that a person had disposed of an asset in order to reduce the level of charges for their care and support needs if at the time the disposal took place they were fit and healthy and could not have foreseen the need for care and support.'

It is important to bear in mind the rule that if a transfer is made within 6 months of going into care, it is treated as made for the purpose of deliberate deprivation.

COMMENT

Although the transfer of the property into the trust in the circumstances described above was made for a number of reasons (and a desire to hold the entire property in a trust rather than having the ownership split between the trust and the mother may well have made perfect practical sense), since the lady in question was already in receipt of some social security benefits at the time of the transfer to the trust, it is probably unsurprising that the council decided there had been a deliberate deprivation. Indeed, in this case, there was probably no need for the mother to make the transfer of her part to the children because her half, being a tenancy in common in half of the property with the other half owned by others, would have had only a small open market value. Cleary, the timing is important. Some individuals have used the so-called "asset protection trusts", normally set up well in advance of needing any assistance. Unfortunately, these have had rather bad press recently following the conviction and jailing of eight people last year for mis-selling such arrangements.

DOMICILE – INCOME TAX AND CAPITAL GAINS TAX

Draft legislation has been published for consultation

At Summer Budget 2015 the Chancellor announced the government's intention to reform the taxation of UK resident individuals who are non-domiciliaries (non-doms).

Broadly, it was announced that a deemed domicile rule for long-term residents would be amended to 15 out of 20 (from 17 out of 20) tax years for inheritance tax purposes from 6 April 2017. This rule would then also apply for income tax and capital gains tax purposes.

Following this announcement, draft legislation has now been published for consultation regarding the position of those who would otherwise be non-domiciled in the UK as a matter of general law and, who it is proposed, should be treated as being deemed domiciled in the UK for the purposes of income tax and capital gains tax as well as IHT. Comments are invited by 2 March 2016.

The two deeming provisions are given by Conditions A and B of the draft legislation. Condition A applies to anyone born in the UK with a UK domicile of origin and whilst they are UK resident; and Condition B applies to anyone who has been resident in the UK for at least 15 out of the previous 20 tax years.

Currently, the main UK tax advantage of being a "non-dom" is that, despite being resident in the UK, such an individual can arrange to pay tax on income and gains earned outside the UK only when these are remitted to the UK by electing the remittance basis of taxation. This requires the payment of a Remittance Basis Charge (RBC) which is set at £30,000, £60,000 or £90,000 per annum depending on the length of UK residence. However, the new provisions will restrict access to the remittance basis so that anyone deemed UK domiciled by virtue of either Condition A or B above will not be able to elect for the remittance basis.

In addition, these provisions amend other aspects of income tax and capital gains tax law that offer advantages to non-doms but which do not directly rely on part of the remittance basis to be amended.

NATIONAL SAVINGS - INTEREST RECEIVED ON THE 65+ GUARANTEED BONDS

The new personal savings allowance could save tax on interest for a number of those who invested 65+ Guaranteed Bonds

The National Savings & Investments' one-year and three-year Guaranteed Bonds were first launched in early 2015 and were open to everyone aged 65 and over. The interest rates were set at 2.8% for the one-year Bond and 4% for the three-year Bond. With the three-year Bonds, interest is added yearly and taxed yearly but is only paid out at maturity.

Currently, and up until 6 April 2016, savers will pay tax on interest that the Bonds pay at their usual tax rate. However, those whose Bond matures after 5 April 2016 could receive their interest tax free provided they remain within the new personal savings allowance (PSA) which will be £1,000 for basic rate taxpayers and £500 for higher rate taxpayers.

Essentially, a saver who put £10,000 (the maximum) in a one-year Bond would earn £280 (i.e at 2.8%) in interest which would be taxable if the Bond matures before 6 April 2016. If, on the other hand, a one-year Bond matures after 5 April 2016 this interest is likely to be tax free provided the investor has no other interest to cause them to exceed their PSA.

The position could be even more favourable for a saver who put £10,000 (the maximum) in a three-year Bond. They would earn £1,249 (£400 in year one, £416 in year two and £433 in year three) total interest. The interest on the three-year Bond is added to the account annually which means that, even with the maximum amount deposited, a basic rate taxpayer who receives the interest after 5 April 2016 could receive that interest tax free provided they have no other interest to cause them to exceed their PSA.

The introduction of the PSA is, however, still subject to consultation so there are still some questions which remain unanswered. Despite this, it appears that the tax position on interest can vary significantly for two individuals who took out their Bonds on different days where maturity is for one before 6 April 2016 and after 5 April 2016 for the other.

DISCLOSURE OF TAX AVOIDANCE SCHEMES – THE HALLMARK REGULATIONS

In the March 2015 Budget the government announced a package of measures to ensure that the Disclosure of Tax Avoidance Schemes (DOTAS) regime keeps pace with the current avoidance market.

The government has now laid regulations changing the DOTAS hallmark regulations following the technical consultation (published on 16 July 2015) on draft changes.

The regulations will make it harder for would-be promoters and users of avoidance schemes to go undetected and unchallenged. The regulations will have effect from Tuesday 23rd February 2016.

Alongside this, a response document to the technical consultation has also been published. This document summarises the responses received and the regulations which are being laid following the consultation. This document also announces that the government intends to develop a revised draft inheritance tax hallmark for further consultation in 2016.

HMRC PUBLISHES PENSION SCHEMES NEWSLETTER 75

HMRC has recently published Pension Schemes Newsletter 75. The newsletter covers the following areas:

1. The inheritance tax treatment of pension scheme drawdown funds on death
2. Pension flexibility
3. The Scottish rate of income tax
4. Tax relief at source – annual returns of individual information
5. The lifetime allowance reduction
6. The annual allowance

We think that it is worth highlighting the following aspects of the newsletter:

IHT on drawdown pensions

HMRC has confirmed that due to the legislative drafting there is an unintended consequence in the interaction between the pensions legislation and the IHT legislation that means in circumstances where an individual has designated funds into a drawdown pension but not drawn the income, the undrawn income could technically be treated as being in the member’s estate for IHT purposes.

Legislation will be included in Finance Bill 2016 to cover cases where the scheme member elects to draw down funds from a registered pension scheme, but the drawdown funds are not used up before death, so that the undrawn funds aren’t subject to an IHT charge.

The Finance Bill 2016 legislation will apply to deaths occurring on or after 6 April 2011.

Pensions flexibility

There is a drafting error in the way in which Defined Benefits Lump Sum Death Benefits (DBLSDB) on the death of a member before age 75 are taxed and reported. This will be corrected in legislation such that if the payment is not made within the relevant two-year period, the DBLSDB will be subject to PAYE and will not be an unauthorised member payment.

Scottish rate of income tax

HMRC has reiterated the fact that even though the Scottish rate of income tax is the same as for the rest of the UK, Scottish taxpayers my still have their PAYE operated under the relevant S code.

Lifetime allowance reduction

It appears that a number of taxpayers have been contacting HMRC asking to elect for FP16 prior to 6 April 2016. HMRC has reminded that this can't be done until mid-July 2016. HMRC also confirmed that to be eligible to elect for FP16, the individual will have had to 'not breached the FP16 requirements from 6 April 2016.' (In other words not had further contributions paid for his benefit or enjoyed further pension accrual.)

LEGAL ENTITY IDENTIFICATION – THE ISSUES FACING TRUSTS

With effect from January 2017, non-natural persons investing in financial markets will be required to obtain a Legal Entity Identifier before they can trade. What does this mean for trusts?

The Global Legal Entity Identify Foundation (GLEIF), based in Switzerland, is introducing a system whereby every 'legal entity' will need to register and obtain a unique 20-character, alpha-numeric identification number – a Legal Entity Identifier (LEI) - before it can engage in financial transactions.

LEIs are already being issued but the new regulations will come into force in January 2017, and after that date an LEI will be required by all non-natural persons who invest in financial markets.

In the UK, acquiring an LEI will involve paying a fee of £115 plus VAT (renewable annually at a cost of around £70) to the London Stock Exchange (LSE). LEIs issued by the LSE will be known as International Entity Identifiers (IEIs).

Problematically, while trusts are within the definition of a 'legal entity' for these purposes, the process for acquiring an LEI or IEI does not lend itself readily to trust applications. Not only must the applying entity provide the address of its 'headquarters' (a nonsense as far as trusts are concerned), the issuing body is required to validate the details of the entity against available public records and resources before an LEI can be issued. While this is fairly straightforward where the entity is a company, trusts will not usually have publicly available records and information against which their application can be validated - and if the entity cannot be issued with an LEI it will be left unable to trade in financial markets (even if acting through a third party fund manager).

Fortunately, the Financial Conduct Authority and the Wealth Management Association have recognised that some modification is needed to take account of the 'quirky nature' of trusts and both bodies are working closely with the LSE to ensure that the application process for trusts will be as smooth and straightforward as possible. In the meantime, the LSE appears to be taking a pragmatic approach to this problem and has confirmed that it has already issued IEIs to a number of trusts, having 'partially corroborated' the trust details from the trust documents or deeds.

The requirement for an LEI or IEI only exists where the trust or other entity is investing in investments that have to be 'transactionally reported' (such as stocks, shares, derivatives and similar) and it is expected that investment firms (such as discretionary fund managers) will apply for LEIs on behalf of trusts where they are required.

The requirement for an LEI will not apply where the trust or other entity is investing in collective investments such as bonds, unit trusts or pooled funds.

OVER £2BN COLLECTED FROM ACCELERATED PAYMENT NOTICES

Over £2 billion has been collected from users of tax avoidance schemes as a result of government measures to collect disputed tax up-front via accelerated payment notices.

In September 2015 this figure stood at £1 billion – so a dramatic increase in the last 4 months.

Jennie Granger, Director General for Enforcement and Compliance HMRC said:

"Accelerated Payments continue to turn the tables on individuals looking to avoid paying their fair share of tax. Those who take part in tax avoidance now have to pay up-front and dispute later. It really is time to get out of avoidance – HMRC wins the vast majority of cases that people litigate, with many more settling before litigation.

HMRC is now issuing over 3,000 Accelerated Payment Notices a month, and has issued over 41,000 notices since Accelerated Payments were introduced. By the end of 2016, HMRC expects to have completed issuing notices, bringing forward over £5 billion in payments for the Exchequer by March 2020."

INCOME WITHDRAWAL RATE FOR FEBRUARY 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 February 2016 is 2.0%.