Personal Portfolio Bonds - Reviewing the Property Categories

Consultation document
Publication date: 9th August 2016
Closing date for comments: 3rd October 2016

Subject of this consultation:	The property categories listed at section 520 of the Income Tax (Trading and Other Income) Act 2005 (ITTOIA 2005) which the terms of a life insurance policy can allow to be selected without that policy becoming a personal portfolio bond
Scope of this consultation:	At the March 2016 Budget, the government announced it would review the property categories at section 520 ITTOIA 2005. This consultation invites views on the current property categories and further property types that may be included. Throughout this document the term "life insurance policies" includes capital redemption policies and life annuity contracts.
Who should read this:	The life insurance industry, policy administrators for the industry, the funds industry, financial advisors and individual investors.
Duration:	9th August to 3rd October 2016
Lead official:	The lead official is Marie Madden of HM Revenue and Customs (HMRC).
How to respond or enquire about this consultation:	Responses should be sent by email to marie.madden@hmrc.gsi.gov.uk or by post to Marie Madden HM Revenue and Customs Corporation Tax, International and Stamps (CTIS) Financial Services Team Room 3c/06 100 Parliament Street London SW1A 2BQ
Additional ways to be involved:	HMRC welcomes discussions with interested parties, especially policyholders and their representatives, members and representatives of the life insurance and funds industries and life insurance policy administrators for whom the changes may have a material impact.
After the consultation:	Options will be reviewed in the light of representations received. The government expects to publish its response at Autumn Statement 2016. Any draft legislation will be published in advance of Finance Bill 2017.
Getting to this stage and previous engagement	The consultation follows from the announcement made at Budget 2016 that the government will review the property categories that the terms of a life insurance policy can permit the selection of without the policy becoming a personal portfolio bond. Prior to this, the government has received representation from funds representative bodies proposing additional property categories.

Contents

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1. Introduction

The personal portfolio bond legislation.

1.1. Taxable gains can only arise from life insurance policies (other than those held by companies) when value is taken from a policy. Typically this takes place when a policy matures or is wholly or partly surrendered.

1.2. This allows individuals to make investments within a life insurance policy knowing that they will only be chargeable to tax when cash is taken from the policy.

1.3. This feature of life insurance policy taxation had been exploited by individuals who introduced personal property, such as shares in their own company, into their life insurance policy thereby deferring any tax charges on the income or gains arising from that property. In 1999 HMRC introduced the personal portfolio bond rules in order to deter the holding of personal assets within a life insurance policy.

1.4. The definition of a personal portfolio bond includes a life insurance policy, the terms of which allow the policyholder (or, essentially, those acting for the policyholder) to select some or all of the property which their premiums will be invested in. If a life insurance policy is a personal portfolio bond an annual gain ordinarily arises which is chargeable to income tax.

1.5. To prevent the rules applying unnecessarily widely a life insurance policy is not a personal portfolio bond merely because its terms permit property selection if all of the property which may be selected falls within certain categories. These property categories (are listed at section 520 ITTOIA 2005 (see annex B) and, subject to certain conditions, include

- Property in an insurers internal linked fund.
- Units in an authorised unit trust.
- Shares in an investment trust.
- Shares in an open-ended investment company.
- Cash.
- Life insurance policies.
- An interest in certain non-UK collective investment schemes.

1.6. Selection of such property does not make a life insurance policy a personal portfolio bond because its structure or nature ensures that individuals cannot use them to select personal property under the terms of their life insurance policy. For example each of the investment funds in the list have a professional manager making the decisions on where the funds are ultimately invested. The investor has no control over the underlying investments.

1.7. The property categories at section 520 ITTOIA 2005 (hereafter referred to as “permitted property”) have not materially changed since 1999, despite the investment landscape having evolved considerably over that period.

1.8. At Budget 2016, the government announced its intention to review these permitted property categories.

1.9. It is essential that any changes to the permitted property categories do not allow policyholders the ability to select personal assets under the terms of their life insurance policy.

1.10. The next chapter explores three types of investment vehicle that the fund representative bodies have suggested may be included in the section 520 ITTOIA 2005 permitted property categories :

- Real estate investment trusts
- Overseas equivalents of UK approved investment trusts
- Authorised contractual schemes

1.11. The government also welcomes suggestions for any additions to the current permitted property categories, as well as any areas where the categories should be narrowed.

2. Extending the scope

2.1. This chapter sets out three types of investment vehicle that the fund representative bodies have suggested may be included in the permitted property categories. These are:

- real estate investment trusts (both UK and foreign equivalents);
- overseas equivalents of UK approved investment trusts; and
- UK authorised contractual schemes.

For each type of vehicle, the government would be grateful for views on the following questions.

Questions

Question 1 – Should any or all of the vehicles discussed be added to the permitted property categories? In each case, what would the impact of inclusion or non-inclusion be on investment and what one-off and/ or ongoing costs or savings do you anticipate will arise as a result in both the vehicles themselves and insurance policies?

Question 2 – For each of the three investment vehicles discussed, do you consider that their structure or nature means individual policyholders would be effectively prevented from introducing personal assets into their life insurance policy?

Question 3 – In addition to the three types of investment vehicle discussed, do you consider that there are other types of property that should be included in the permitted property categories? If so please describe the property in detail and explain why individual policyholders would be effectively prevented from introducing personal assets into their life insurance policy.

Question 4 – Are there any categories of asset currently within the permitted property categories where changes in their structure or nature means there is now a risk that they could be used by individual policyholders to introduce personal assets into their life insurance policy?

Question 5 - Do you have any comments on the assessment of impacts, either generally or in relation to the specific options set out below?

Real Estate Investment Trust [REIT]

Description

2.2. REITs were introduced in the UK on 1st January 2007 and have not, to date, been added to the permitted property categories. A REIT is a limited company (or a group of such companies), which invests mainly in property. Its shares must be widely held. Whether the vehicle is a single company or a group, it is referred to in the legislation as a REIT. In this document, we use the term UK-REIT in relation to both.

2.3. Investors own shares in the UK-REIT and the company makes and manages the underlying investments. The UK-REIT is exempt from UK tax on the income and gains of its property rental business. It is required to distribute 90% of such income to its investors, who are taxed as receiving property income. The investor thus obtains broadly similar returns as if they had invested directly in the property.

2.4. In addition to UK-REITs, the government is also considering the case for including foreign equivalents of UK-REITs within the list of permitted property categories. These are companies that qualify for REIT status in a jurisdiction that has a REIT regime that is substantially similar to the UK's. The foreign equivalent of the UK-REIT has been considered for the purposes of the UK-REIT regime. The characteristics which identify a foreign REIT as substantially similar to the UK-REIT are that it is widely held, deriving income mainly from long term investment in immoveable property, it distributes the majority of its property income annually and is tax exempt on that income. To date, this includes Australian REITs and most US REITs.

Overseas equivalent of approved investment trusts

Description

2.5. As noted in Chapter 1, investment trusts are already included within the permitted property categories. Despite the name, they are listed companies. They invest in a broad range of shares and securities and use professional managers to oversee their investments. Buying shares in investment trusts offers investors one way to diversify their portfolios, spread risk and gain access to this professional management. These features suggest a policyholder could not select shares in an investment trust that held personal assets of that policyholder.

2.6. The government has received representations requesting that overseas equivalents of investment trusts are also included within the permitted property categories. Unlike the position with UK REITs, it has not been necessary to date for HMRC to consider how an overseas equivalent of a UK investment trust should be defined.

2.7. An approved UK investment trust is a company that has confirmed to HMRC that it meets (and will continue to meet) certain conditions, and to which HMRC has then issued a letter confirming its approval. Those conditions are set out at section1158 CTA 2010 (S1158 hereafter) and in the Investment Trust (Approved Company) (Tax) Regulations 2011 (Statutory Instrument 2011/2999).

2.8. The government would like to consider whether there is an appropriate and practical way in which an overseas equivalent of a UK investment trust could be identified. This could be based on certain legal or regulatory requirements or there may be other, more appropriate and/or practical ways of identifying equivalent regimes. The government welcomes views on this.

Question

Question 6 - How do you consider the overseas equivalent of a UK investment trust could be defined?

Authorised contractual schemes

Description

2.9. Authorised contractual schemes (ACS) were introduced in 2013, and to date have not been included in the permitted property categories. An ACS is a type of investment fund, which may take the form of a limited partnership or a co-ownership contractual arrangement.

2.10. An ACS is authorised and regulated by the Financial Conduct Authority. It has an authorised manager responsible for managing the fund and making investment decisions. These features suggest individual policyholders could not select an investment in an ACS that held their personal property.

2.11. Overseas tax transparent funds are already included in the permitted property categories in S520 ITTOIA 2005 (at Category 7).

3. Assessment of Impacts

Potential impacts of the options proposed will be assessed in the light of this consultation.

Summary of impacts

Exchequer impact

2016 to 2017	2017 to 2018	2018 to 2019	2019 to 2020	2020 to 2021
£Nil	Negligible	Negligible	Negligible	Negligible

Impact expected to be negligible, but this will be reviewed. The final costing will be subject to scrutiny by the Office for Budget Responsibility, and will be set out at Autumn Statement 2016 and Budget 2017.

Economic impact

Expected to be negligible, but will be reviewed following the consultation.

Impact on individuals, households and families

This measure will impact on individuals that hold life insurance policies which allow them to select the underlying assets. It may allow a wider selection of property for those policyholders. The overall impact is expected to be negligible.

The measure is not expected to impact on family formation, stability or breakdown.

Equalities impacts

This measure will impact on individuals within the protected equality groups that tend to be represented amongst those with above average income. The overall impact is expected to be negligible.

Impact on businesses and Civil Society Organisations

This measure will have an impact on wealth managers and insurance companies. Business will incur one-off costs including familiarisation with the new rules. The number of businesses affected and the impacts on them will be explored as part of the consultation.

Impact on HMRC or other public sector delivery organisations

It is not anticipated that implementing this change will incur any additional costs / savings for HMRC, but we will keep that under review as the measure develops.

Other impacts

Other impacts have been considered and none have been identified.

Monitoring and evaluation

This measure will be monitored through communication with affected taxpayer groups through information collected from tax receipts and returns.

4. Summary of Consultation Questions

Question 1 – Should any or all of the vehicles discussed be added to the permitted property categories? In each case, what would the impact of inclusion or non-inclusion be on investment and what one-off and/ or ongoing costs or savings do you anticipate will arise as a result in both the vehicles themselves and insurance policies?

Question 2 – For each of the three investment vehicles discussed, what is it about their structure or nature that means individual policyholders would be effectively prevented from introducing personal assets into their life insurance policy?

Question 3 – In addition to the three types of investment vehicle discussed, do you consider that there are other types of property that should be added to the permitted property categories? If so please describe the property in detail and explain why individual policyholders would be effectively prevented from introducing personal assets into their life insurance policy.

Question 4 – Are there any category of asset currently within the permitted property categories where changes in their structure or nature means there is now a risk that they could be used by individual policyholders to introduce personal assets into their life insurance policy?

Question 5 - Do you have any comments on the assessment of impacts, either generally or in relation to the specific options set out in chapter 2?

Question 6 - How do you consider the overseas equivalent of a UK investment trust could be defined?

5. The Consultation Process

This consultation is being conducted in line with the Tax Consultation Framework. There are 5 stages to tax policy development:

Stage 1	Setting out objectives and identifying options.
Stage 2	Determining the best option and developing a framework for implementation including detailed policy design.
Stage 3	Drafting legislation to effect the proposed change.
Stage 4	Implementing and monitoring the change.
Stage 5	Reviewing and evaluating the change.

This consultation is taking place during stage 2 of the process. The purpose of the consultation is to seek views on the detailed policy design and a framework for implementation of a specific proposal, rather than to seek views on alternative proposals.

How to respond

Responses should be sent by 3rd October, by e-mail to:

marie.madden@hmrc.gsi.gov.uk

or by post to:

Marie Madden
HM Revenue and Customs
Corporation Tax, International and Stamps (CTIS)
Financial Services Team
Room 3c/06
100 Parliament Street
London
SW1A 2BQ

Paper copies of this document or copies in Welsh and alternative formats (large print, audio and Braille) may be obtained free of charge from the above address. This document can also be accessed from HMRC's GOV.UK pages. All responses will be acknowledged, but it will not be possible to give substantive replies to individual representations.

When responding please say if you are a business, individual or representative body. In the case of representative bodies please provide information on the number and nature of people you represent.

Confidentiality

Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes.

These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004.
If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentially can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HMRC.

HMRC will process your personal data in accordance with the DPA and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties.

Consultation Principles

This consultation is being run in accordance with the government's Consultation Principles. HMRC welcomes direct discussions on issues that impact on particular financial institutions or sectors.

The Consultation Principles are available on the Cabinet Office website: http://www.cabinetoffice.gov.uk/resource-library/consultation-principles-guidance

If you have any comments or complaints about the consultation process please contact:

John Pay, Consultation Coordinator, Budget Team, HM Revenue & Customs, 100 Parliament Street, London, SW1A 2BQ.

Email: hmrc-consultation.co-ordinator@hmrc.gsi.gov.uk

Please do not send responses to the consultation to this address.

Annex A: Relevant (current) Government Legislation

Personal Portfolio Bonds Legislation

Chapter 9 Part 4 Income Tax (Trading and Other Income) Act 2005

Real Estate Investment Trusts

Part 12 Corporation Tax Act 2010

Investment Trust Company

S1158 Corporation Tax Act 2010 and Investment Trust (Approved Company) (Tax) Regulations 2011 (Statutory Instrument 2011/2999).

Authorised Contractual Schemes

The Collective Investment in Transferable Securities (Contractual Scheme) Regulations 2013

Annex B: Section 520 ITTOIA 2005

520 The property categories

(1) The table in subsection (2) sets out the categories of property referred to in section 517(2).

(2) This is the table—

Category	*Property*		
Category 1	property which the insurance company has appropriated to an internal linked fund		
Category 2	units in an authorised unit trust		
Category 3	shares in an investment trust		
Category 4	shares in an open-ended investment company		
Category 5	cash		
Category 6	a policy or contract to which this Chapter applies, other than an excluded policy or contract (see subsection (3))		
Category 7	an interest in a collective investment scheme constituted by—		
		(a)	a company which is resident outside the United Kingdom (other than an open-ended investment company),
		(b)	a unit trust scheme the trustees of which are non-UK resident, or
		(c)	any other arrangement which takes effect by virtue of the law of a territory outside the United Kingdom, and which under that law creates rights in the nature of co-ownership (without restricting that term to its legal meaning in any part of the United Kingdom)

(3) A policy or contract is "excluded" if—

(*a*) the policy or contract is itself a personal portfolio bond,

(*b*) the value of any benefits under the policy or contract is or has at any time been capable of being determined directly or indirectly by reference to a personal portfolio bond, or
(*c*) a personal portfolio bond is related property in relation to the policy or contract.
(4) In this section—
"cash"—
(*a*) includes any sum which is deposited—
(i) in a building society account (including a share account) or similar account, or
(ii) in a bank account or similar account, but
(*b*) does not include cash which is acquired wholly or partly for the purpose of realising a gain from its disposal,
"collective investment scheme" has the meaning given by section 235 of FISMA 2000, and "interest", in relation to such a scheme, means the beneficial entitlement of a participant in such a scheme,
"internal linked fund" has the meaning given by—
(*a*) the Interim Prudential Sourcebook for Insurers made by the [Prudential Regulation Authority][3] under FISMA 2000, or
(*b*) rules made by the [Prudential Regulation Authority][3] under FISMA 2000 and having effect for the time being in place of the Sourcebook,
["investment trust" has the meaning given by [section 1158 of CTA 2010][2],][1]
"open-ended investment company" has the meaning given by section 236 of FISMA 2000, and
"related property" has the same meaning as in section 625 (see subsection (5)).