HM Revenue & Customs

Life insurance: time apportioned reductions

Who is likely to be affected?

Policyholders who have been resident outside the UK at any time during the life of their life insurance policy.

General description of the measure

This measure will provide a greater alignment between the treatment of policies issued by insurers inside and outside the UK, and ensure that the rules on time apportioned reductions provide a more appropriate reduction to chargeable event gains.

Policy objective

This measure supports the Government's objective of promoting fairness in the tax system by aligning the treatment of policies issued by UK insurers with that of insurers outside the UK. It also will provide a calculation methodology that more accurately reflects relevant periods of non residence.
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Background to the measure

The Government announced at Budget 2012 that there would be a consultation on reforming rules within the chargeable event gain regime that are designed to reflect a policyholder's period of residence outside the UK.

Formal consultation opened on 13 August 2012 and closed on 5 November 2012. A summary of responses was published on 11 December 2012.

Detailed proposal

Operative date

The measure will have effect on and after 6 April 2013.

Current law

The current law is set out in Chapter 9, Part 4 Income Tax (Trading and Other Income) Act 2005 (ITTOIA). This is known as the chargeable event gain regime. These rules ensure that gains made by individuals from their policies are subject to income tax at the individual's marginal rate.

Section 528 ITTOIA provides that a chargeable event gain from a policy issued by a foreign insurer is reduced proportionately if the policyholder has been resident outside the UK at any time during the life of the policy.

Proposed revision

Legislation will be introduced in Finance Bill 2013 to extend time apportioned reductions to life policies issued by UK insurers. The legislation will also amend the methodology used to calculate the reductions.

Summary of impacts

Exchequer impact (£m)	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
	-	nil	negligible	negligible	negligible	negligible
	This measure is expected to have a negligible impact on the Exchequer. Any impact will be set out at Budget 2013.					
Economic impact	The measure is not expected to have any economic impacts.					
Impact on individuals and households	The proposed changes are expected to impact on a relatively small number of individuals who have periods of residence outside the UK during their ownership of a life insurance policy.					
Equalities impacts	HM Revenue & Customs (HMRC) has no data about the type of people who hold UK or overseas policies but no negative equalities impacts are expected.					
Impact on business including civil society organisations	This measure is expected to have a negligible impact on businesses and civil society organisations. The proposed changes will only affect insurers and advisers, who currently provide marketing material and guidance on the impact of the chargeable event gain rules. UK businesses will face negligible one-off costs in familiarising themselves with the new rules and producing new marketing material. Insurers outside the UK will face negligible one-off costs to make initial changes to their product material. There will be no change in ongoing administrative burdens as no further changes are required.					
Operational impact (£m) (HMRC or other)	Other than providing revised guidance, it is not anticipated that implementing this change will incur any additional costs for HMRC.					
Other impacts	Small firms impact test: the impact on small firms has been considered and is expected to be negligible because very few firms will be affected. Other impacts have been considered and none have been identified.					

Monitoring and evaluation

HMRC has an established programme of liaison with the industry, which will capture issues around implementation and ongoing compliance and administrative costs. In addition, individuals are required to prepare tax returns which will provide data to inform any such evaluation.

Further advice

If you have any questions about this change, please contact David Moran on 020 7147 2612 (email: david.moran@hmrc.gsi.gov.uk) or Elizabeth Ward-Penny on 020 7147 3037 (email: elizabeth.ward-penny@hmrc.gsi.gov.uk).

1 Gains from contracts for life insurance etc

Schedule 1 amends Chapter 9 of Part 4 of ITTOIA 2005 (gains from contracts for life insurance etc).

SCHEDULES

SCHEDULE 1

Section 1

GAINS FROM CONTRACTS FOR LIFE INSURANCE ETC

1 Chapter 9 of Part 4 of ITTOIA 2005 (gains from contracts for life insurance etc) is amended as follows.

2 In section 476 (special rules: foreign policies) in subsection (2)—
(a) after the entry relating to section 474(3) to (5) insert "and",
(b) omit the entry relating to section 528,
(c) omit the "and" after the entry relating to sections 531 to 534, and
(d) omit the entry relating to section 536(6).

3 For section 528 substitute—

"528 Reduction in amount charged on basis of non-UK residence where individual liable for tax

(1) This section applies if—
(a) an individual is liable for tax charged on a gain from a policy of life insurance or a capital redemption policy, and
(b) there are one or more days in the material interest period on which the individual is not UK resident.

(2) In determining the individual's liability for tax, the gain on which the tax is charged in the case of the individual is to be reduced by the appropriate fraction.

(3) The appropriate fraction is—

$$\frac{A}{B}$$

where—
A is the number of days in the material interest period which are days falling within subsection (1)(b), and
B is the number of days in the policy period.

(4) In this section "the material interest period" means so much of the policy period as during which the individual meets condition A, B or C in section 465 in relation to the policy.

(5) For this purpose, in section 465(2) to (4) references to the rights under the policy are to be read as including references to a share of those rights.

(6) In this section "the policy period" means the period for which the policy has run before the chargeable event occurs.

(7) If the policy is a policy of life insurance which is a new policy in relation to another policy, for the purposes of subsection (6) the new policy is to be taken to have run—

(a) from the issue of the other policy, or

(b) if it also was a new policy in relation to an earlier policy, from the issue of the earlier policy,

and so on; and in subsections (4) and (5) references to the policy are to be read accordingly as including any relevant earlier policy.

(8) In subsection (7) "new policy" has the meaning given in paragraph 17 of Schedule 15 to ICTA.

(9) Subsection (10) applies if—

(a) the individual would not have been liable for any tax charged under this Chapter as a result of the chargeable event but for having been assigned rights, or a share of rights, under the policy,

(b) the assignor was the individual's spouse or civil partner with whom the individual was living when the assignment occurred, and

(c) no consideration was given by the individual for the assignment.

(10) In relation to times before the assignment occurred, in subsections (1)(b) and (4) references to the individual are to be read as references to the assignor.

528A Reduction in amount charged on basis of non-UK residence of deceased person

(1) This section applies if—

(a) personal representatives are liable for tax charged on a gain from a policy of life insurance or a capital redemption policy, and

(b) there were one or more days in the material interest period on which the deceased was not UK resident.

(2) This section also applies if—

(a) by virtue of section 467(4)(b) (deceased settlor), trustees are liable for tax charged on a gain from a policy of life insurance or a capital redemption policy,

(b) there were one or more days in the material interest period on which the deceased was not UK resident, and

(c) the deceased was UK resident when the deceased died.

(3) In determining the liability for tax of the personal representatives or trustees, the gain on which the tax is charged in the case of the personal representatives or trustees is to be reduced by the appropriate fraction.

(4) The appropriate fraction is—

$$\frac{A}{B}$$

where—

A is the number of days in the material interest period which are days falling within subsection (1)(b) or (2)(b) (as the case may be), and

B is the number of days in the policy period.

(5) In this section “the material interest period” means so much of the policy period falling before the deceased’s death as during which the deceased met condition A, B or C in section 465 in relation to the policy.

(6) For this purpose, in section 465(2) to (4) references to the rights under the policy are to be read as including references to a share of those rights.

(7) In this section “the policy period” means the period for which the policy has run before the chargeable event occurs.

(8) If the policy is a policy of life insurance which is a new policy in relation to another policy, for the purposes of subsection (7) the new policy is to be taken to have run—

(a) from the issue of the other policy, or

(b) if it also was a new policy in relation to an earlier policy, from the issue of the earlier policy,

and so on; and in subsections (5) and (6) references to the policy are to be read accordingly as including any relevant earlier policy.

(9) In subsection (8) “new policy” has the meaning given in paragraph 17 of Schedule 15 to ICTA.”

4 Omit section 529 (exceptions to section 528).

5 (1) Section 536 (top slicing relieved liability: one chargeable event) is amended as follows.

(2) In subsection (6) for the words from “from” to the end substitute “reduced under section 528 in the case of the individual.”

(3) For subsection (7) substitute—

“(7) If in the case of the individual the gain is reduced under section 528, for steps 1 and 3 in subsection (1) N is reduced by the number of complete years in the material interest period during which the individual was non-UK resident.

“The material interest period” has the same meaning as in section 528.”

6 In section 552 of ICTA (information: duty of insurers) after subsection (13) insert—

“(14) For the purposes of this section no account is to be taken of the effect of sections 528 and 528A of ITTOIA 2005.”

7 (1) The amendment made by paragraph 3 above has effect in relation to—

(a) any policy of life insurance issued in respect of an insurance made on or after 6 April 2013, or

(b) any contract constituting a capital redemption policy made on or after that date,

and the other amendments made by this Schedule have effect accordingly.

(2) The amendment made by paragraph 3 above has effect in relation to any insurance or contract made before 6 April 2013 if on or after that date—

(a) the policy or contract is varied so as to increase the benefits secured,

(b) there is or was an assignment (or assignation) of rights, or a share of the rights, conferred by the policy or contract (whether or not for money's worth) to the individual or deceased, or

(c) some or all of the rights conferred by the policy or contract become or became held as a security for a debt of the individual or deceased,

and the other amendments made by this Schedule have effect accordingly.

(3) For the purposes of sub-paragraph (2)(a)—

(a) an exercise of rights conferred by a policy or contract is to count as a variation of the policy or contract, and

(b) the reference to an increase in the benefits secured by a policy or contract includes an increase in the benefits secured by another policy or contract with which the policy or contract is connected (within the meaning given by section 473A of ITTOIA 2005).

EXPLANATORY NOTE

GAINS FROM CONTRACTS FOR LIFE INSURANCE

SUMMARY

1. This clause and Schedule amend the rules for time apportioned reductions from gains made on life insurance policies for periods when the policyholder is resident outside the UK. Current rules only provide for time apportioned reductions where a life insurance policy has been issued by a foreign insurer. Time apportioned reductions will be extended to life insurance policies issued by UK insurers. Time apportioned reductions will be calculated by reference to the residence history of the person liable to income tax on the gains and not by reference to the residence history of the legal owner of the policy.

DETAILS OF THE SCHEDULE

2. Paragraph 1 of Schedule 1 amends Chapter 9 of Part 4 of Income Tax (Trading and Other Income) Act 2005 (ITTOIA) (gains from contracts for life insurance etc).

3. Paragraph 2 of Schedule 1 amends section 476 ITTOIA by removing references to section 528 and section 536 (6) ITTOIA.

4. Paragraph 3 of Schedule 1 replaces section 528 ITTOIA with new sections 528 and 528A.

New section 528 Reduction in amount charged on basis of non-UK residence where individual liable for tax

5. New section 528(1) provides that this section applies to individuals who are liable to chargeable event gains and who have not been resident in the UK during the material interest period (defined in new section 528(4)). From 6 April 2013, when the statutory residence test applies, a day will only fall in new subsection (1)(b) if the individual is not resident in the UK for the whole of the relevant tax year. For information on how new section 528 applies to a year that, for the individual, is split between a UK part and an overseas part, see the Explanatory Notes on the Statutory Residence Test.

6. New section 528(2) provides that an individual's liability to tax on a gain on life insurance policy is to be reduced by the appropriate fraction.

7. New section 528(3) provides details of that fraction.

8. New section 528(4) defines 'material interest period' for the purposes of this section.

9. New section 528(5) provides that references to rights in section 465(2) to (4) ITTOIA include references to a share of those rights.

10. New section 528(6) defines the term 'policy period' for the purposes of new section 528.

11. New section 528(7) and (8) provides that where a new policy is issued for another policy (policy 'A') the 'policy period' in subsection (6) includes the period for which (A) was in existence. If A itself is a new policy issued for another policy (policy 'B') the 'policy period' in subsection (6) includes the period for which both A and B are in existence.

12. New section 528(9) and (10) explains how time apportioned reductions are to apply where a policy is assigned between spouses or civil partners and the individual assigning the policy is living with the spouse or civil partner when the assignment is made. When a chargeable event crystallises, the material interest period is extended to take into account the residence histories of both the assignor and the assignee for that part of the material interest period in which they, respectively, met the conditions of new section 528(1).

New 528A Reduction in amount charged on basis of non-UK residence of deceased person

13. New section 528A(1) applies to reduce the amount of a personal representative's or trustee's tax liability on a chargeable event gain where the deceased has not been resident in the UK during the material interest period.

14. New section 528A(2) applies to reduce trustee's liability to tax on a chargeable event gain under section 467 ITTOIA in respect of a deceased settlor where the deceased was not resident in the UK during the material interest period.

15. New section 528A(3) explains that the liability to tax of personal representatives or trustees on a gain on a life insurance policy is to be reduced by the appropriate fraction.

16. New section 528A(4) provides details of the fraction for new section 528A.

17. New section 528A(5) defines 'material interest period' for the purposes of new section 528A.

18. New section 528A(6) provides that references to rights in section 465(2) to (4) ITTOIA include references to a share of those rights.

19. New section 528A(7) defines the term 'policy period' for the purposes of new section 528A.

20. New sub-sections 528A(8) and (9) provides that where a new policy is issued for another policy (policy 'A') the 'policy period' in new sub-section (7) includes the period for which (A) was in existence. If A itself were a new policy issued for another policy (policy 'B') the 'policy period' in new sub-section (7) will include the period for which both A and B are in existence.

21. Paragraph 4 of Schedule 1 repeals section 529 ITTOIA.

22. Paragraph 5(1) of Schedule 1 amends section 536 ITTOIA (top slicing relief).

23. Paragraph 5(2) of Schedule 1 amends section 536(6) to ensure that time apportioned reductions are available to policies issued by UK insurers as well as policies issued by foreign insurers.

24. Paragraph 5(3) of Schedule 1 amends section 536(7).

25. New section 536(7) ensures that time apportioned reductions are available both to policies issued by foreign insurers and policies issued by UK insurers. It also provides that in computing top-slicing relief the number of complete years for which the policy has run before the chargeable event gain arises will be reduced by the number of complete years in the material interest period during which the individual was non-UK resident.

26. Paragraph 6 of Schedule 1 inserts a new sub-paragraph (14) into section 552 of ICTA (information: duty of insurers).

27. Paragraph 7(1) and (2) of Schedule 1 sets out the effective dates for the changes made to Schedule 1.

28. Paragraph 7(3) of Schedule 1 defines 'variation' and 'increase in the benefits secured' for the purposes of new sub-paragraph (2)(a).

BACKGROUND

32. Special rules apply income tax to investment profits (gains) realised by individuals from life insurance policies and capital redemption policies. The rules are known as the chargeable event gain regime.

33. Provision is made within the regime to ensure that chargeable event gains arising on policies issued by foreign insurers are reduced in proportion to the policyholder's period of residence outside the UK at any time during the life of the policy. Very broadly, this means that

gains accruing during an individual's period of residence outside the UK are excluded from the charge to UK tax.

34. Time apportioned reductions are currently not available to policies issued by UK insurers even though individuals with such policies may also have periods of residence outside the UK.

35. In addition, the amount of the reduction provided by the current rules may be inappropriate in some circumstances. For example, relief is given by reference to the residence history of the legal owner of the policy rather than the person liable to income tax on the gains (generally the beneficial owner).

36. A consultation document was issued 13 August 2012 to invite views on reforming the rules to allow time apportioned reductions to be made available to individuals with policies issued in the UK, who have a period of residence outside the UK and to develop a more appropriate method to calculate time apportioned reductions that also interacts effectively with the new statutory residence rules.

37. If you have any questions about this change, or comments on the legislation, please contact David Moran on 020 7147 2612 (email: david.moran@hmrc.gsi.gov.uk), or Elizabeth Ward-Penny on 020 7147 3037 (email: elizabeth.ward-penny@hmrc.gsi.gov.uk).