



HM Revenue
& Customs

Deduction of income tax from savings income: implementation of the Personal Savings Allowance

Summary of Responses
December 2015

Contents

	Executive Summary	3
1	Introduction	5
2	Responses	8
3	Conclusions and next steps	17
Annex A	List of respondents	19
Annex B	Responses to the “ <i>Deduction of income tax from interest: peer-to-peer lending</i> ” consultation	20

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Executive Summary

Context

At the March 2015 Budget, the government announced the introduction of the Personal Savings Allowance (PSA) in April 2016. This will mean that the vast majority of taxpayers will have no tax liability on their savings income. In recognition of this, from the same date, banks and building societies will no longer deduct (or “withhold”) tax from payments of interest to account holders under the Tax Deduction Scheme for Interest (TDSI).

The *Deduction of interest from savings income: implementation of the Personal Savings Allowance* consultation was subsequently launched in July 2015 to explore the possibility of changes to withholding rules applying to savings income more widely than bank and building society interest.

The consultation sought to establish which, if any, of a series of options would effectively balance four key drivers:

- making it as easy as possible for recipients of savings income to pay the right tax;
- risks to the Exchequer if the right tax is not paid;
- administrative burdens and costs for payers of interest and other amounts; and
- costs to HMRC of operating and policing the tax system.

In addition to the general questions addressed, the consultation recognised that implementation of the PSA and cessation of deduction of tax under TDSI may have particular implications for certain sectors of the savings industry. It invited comment on any such sector-specific issues.

Responses and way forward

The PSA was welcomed as benefiting the UK financial services industry and savers alike, and there was general support for the aims of the consultation. However, there was no overall consensus on the most appropriate outcome. Responses from payers of savings income tended to stress what was seen as a need for a level playing field in the market for different types of savings product and minimising administrative costs of operating the withholding and reporting rules. On the other hand, responses on behalf of recipients of savings income emphasised simplicity for taxpayers and minimising the need to interact with HMRC.

At the March 2015 Budget, the government also announced its intention to modernise the tax system, replacing tax returns with digital tax accounts for millions of individuals and businesses. This will represent a major modernisation of the way in which taxpayers interact with HMRC and will transform the way in which information is gathered and processed by HMRC, including data from payers of interest and other savings income. Information on such payments will be processed directly into digital tax accounts for individual taxpayers. The government will shortly publish a roadmap setting out its plans, and a range of consultations will take place in 2016.

This project, entitled “Making Tax Digital” will help to resolve many of the issues raised in this consultation. In particular, the automatic provision and processing of data is expected to make it much easier for recipients of savings income to pay the right tax. It will reduce the administration required from HMRC and will minimise risk to the Exchequer from taxable income not being reported to HMRC.

In the absence of a clearly favoured option, and in the context of the changes anticipated under Making Tax Digital, as a general approach the government does not intend to make immediate changes to non-TDSI withholding arrangements. Rather, the government will review the need to retain withholding requirements as Making Tax Digital develops.

Sector-specific issues were raised by the collective investments (or funds), peer to peer lending (P2P) and life insurance industries. Outside the general approach outlined above, the government is continuing to consider the case for early changes to withholding rules on interest from authorised investment funds, investment trusts and P2P loans, and expects to make an announcement as soon as possible. However, it is not intended to make particular changes in respect of life insurance gains.

In addition to the questions posed in this consultation, there are particular issues, not related to the introduction of the PSA, with the way in which withholding rules operate in the particular circumstances of the P2P sector. A separate consultation document exploring these P2P issues was published on 15 July 2015¹. However, changes to the withholding rules in respect of the P2P sector will not be necessary if the existing rules are abolished. If, on the other hand, the obligation to deduct is retained for P2P lending, HMRC will continue to explore these issues with the industry. Meanwhile, responses to the separate P2P consultation are summarised in Annex B to this document.

¹ The consultation document “*Deduction of income tax from interest: peer-to-peer lending*” can be found at:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/444951/Deduction_of_income_tax_from_interest_-_peer-to-peer_lending.pdf

1. Introduction

- 1.1 The government announced in the March 2015 Budget that a new Personal Savings Allowance (PSA) would be introduced with effect from 6 April 2016. It will be applied to individuals' 'savings income' as defined in section 18 of the Income Tax Act 2007 (ITA 2007). Broadly, the PSA will apply a new 0% income tax rate for up to £1000 of savings income received by a basic rate (20%) taxpayer, or up to £500 of savings income received by a higher rate (40%) taxpayer.
- 1.2 The new PSA will mean that around 95% of taxpayers will have no tax to pay on their savings income. Because of this, it was also announced that from 6 April 2016, banks and building societies will no longer be required to deduct income tax at source from interest paid to account holders. The arrangements under which banks and building societies currently deduct tax from such interest are called the Tax Deduction Scheme for Interest (TDSI).
- 1.3 However, "savings income" is wider than just interest from bank and building society accounts. It also includes:
- interest from other sources, for instance authorised investment funds and investment trusts;
 - interest included in payments of compensation for mis-sold financial products, such as payment protection insurance;
 - payments from certain purchased life annuities;
 - profits from deeply discounted securities;
 - profits from the accrued income scheme; and
 - gains from certain life insurance contracts.
- 1.4 These types of savings income are not covered by TDSI, but in some cases there is nonetheless a duty on payers to deduct tax on payment. In particular, there is a duty², subject to a number of exceptions, in respect of yearly interest paid by a company, a local authority, a partnership of which a company is a member, and by any person, including an individual, to another person outside the UK.
- 1.5 The government was interested to understand whether there might be a case for making changes to withholding requirements more widely than the cessation of TDSI. The purpose of this consultation was therefore to explore options for the future of non-TDSI withholding following the end of TDSI.
- 1.6 This document provides a summary of the responses and comments on how the government intends to proceed. The consultation document³ contained a full account of the issues and options considered, and this summary of responses should be read in conjunction with it.

² Under section 874 Income Tax Act 2007.

³ The consultation document can be found at:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/444945/Deduction_of_income_tax_from_savings_income_-_implementation_of_the_Personal_Savings_Allowance.pdf

General options

1.7 In considering whether changes to non-TDSI withholding may be appropriate, a number of factors are important. Because those various factors may be best served by different outcomes, the consultation was aimed at establishing which, if any, of the six options shown in Box 1 below might achieve an acceptable balance between:

- making it as easy as possible for recipients to pay the right tax;
- risks to the Exchequer if the right tax is not paid;
- administrative burdens and costs for payers of interest; and
- costs to HMRC of operating and policing the system.

1.8 The consultation document posed a series of questions aimed at exploring this in general terms.

Consultation options

- Option 1: retain the current rules for deduction of tax from non-TDSI interest.
- Option 2: remove the obligation to deduct income tax from all non-TDSI interest.
- Option 3: remove the obligation to deduct income tax from non-TDSI interest paid to individuals only.
- Option 4: remove the obligation to deduct income tax from non-TDSI interest below a specified amount.
- Option 5: allow individuals to elect to receive interest with or without deduction of tax.
- Option 6: modify the obligation to deduct income tax from non-TDSI income, as part of wider changes to deduction of tax obligations in Part 15 ITA 2007.

Sector-specific issues

1.9 In addition to the general questions posed, the consultation recognised that the introduction of the PSA might have particular implications for savings from certain types of savings product. In particular, it suggested that there might be specific considerations for the collective investments (or funds) and life insurance sectors and for peer to peer (P2P) lending.

1.10 The government was keen to understand the extent to which such sector-specific issues exist around withholding, how important they are and what changes might be made, taking account of the factors listed at paragraph 1.7 above. In addition to welcoming responses to the consultation in this area, HMRC also invited direct discussions with relevant representative bodies and other interested parties.

Peer to peer lending – separate consultation

1.11 In addition to the issues raised in the *Deduction of income tax from savings income: implementation of the PSA* consultation, there are particular issues, not directly related to introduction of the PSA, affecting the way in which existing rules on deduction of tax from interest operate in the particular circumstances of the peer to peer (P2P) lending sector. Alongside the wider consultation on the consequences of the PSA, the government consulted separately on those P2P issues. Accordingly, a separate consultation document exploring these P2P issues was published⁴ on 15 July 2015.

1.12 Changes to the existing withholding rules as they apply in the P2P sector will only be necessary to the extent that the existing rules are retained. If, following the wider consultation on implementing the PSA, the obligation to deduct tax from interest on P2P loans is removed, the issues raised in the separate P2P consultation will no longer be relevant. If, on the other hand, the obligation to deduct is retained for P2P lending, HMRC will continue to explore those issues with the industry. Responses to the P2P consultation are summarised in Annex B to this document.

⁴ The consultation document “*Deduction of income tax from interest: peer-to-peer lending*” can be found at:
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/444951/Deduction_of_income_tax_from_interest_-_peer-to-peer_lending.pdf

2. Responses

2.1 51 written responses were received; many of these were detailed, and all were helpful. Responses were received from companies, individuals, professional advisers, professional bodies, industry representative bodies and local authorities. A list of respondents to the consultation is provided at Annex A.

2.2 Although the summaries necessarily omit much of the detail in individual responses, all contributions have been fully considered. The Government is grateful to those who have contributed to and supported this process, and continue to do so.

2.3 The consultation document included six specific questions.

Consultation Questions

Question 1: *Other than the issues identified in this consultation, are there other key issues that need to be considered in relation to the interaction of the PSA and rules on deduction of income tax from interest and other savings income?*

Question 2: *Which of the issues identified in this consultation do you consider most important, and why?*

Question 3: *Which of those options do you think is likely to provide the best balance between:*

- *making it as easy as possible for recipients to pay the right tax;*
- *risks to the Exchequer if the right tax is not paid;*
- *administrative burdens and costs for payers of interest and other amounts; and*
- *costs to HMRC of operating and policing the tax system?*

Question 4: *which is your preferred option or combination of options?*

Question 5: *Are there are other options that should be considered?*

Question 6: *Do you have any comments on the assessment of impacts*

2.4 Summaries of responses to these questions are grouped below as follows:

- Key issues (Questions 1 and 2)
- Preferred options (Questions 3, 4 and 5)
- Impacts (Question 6)

Key issues

2.5 Parity of treatment between different forms of savings income was cited as a key issue by most respondents within, or associated with, the savings industry. There was concern about possible impacts on commercial competition between different savings products if withholding is applied to some, but not others. This crystallised around the fact that deduction from interest on bank and building society accounts will cease in April 2016, while no equivalent change has been announced for interest from other sources or other savings income. Respondents thought this would not represent a level playing field and might lead to distortion in the UK savings market where products are aimed at broadly similar, or at least overlapping, sets of customers, and particularly retail customers.

“We believe the tax treatment should not influence the choices individuals make in selection of savings products...”

2.6 Additionally, the UK funds industry noted that funds domiciled in certain jurisdictions outside the UK can be sold freely within the UK (subject to regulatory rules which prohibit the availability of certain funds to retail investors) without deduction of tax on interest paid. It was not suggested that removing the duty to deduct tax would in itself be decisive in making UK funds more attractive in the market or the UK a more attractive domicile for funds. However, some respondents felt that tax changes which might make UK funds appear less attractive (such as the increased need for customers with no tax liability to reclaim amounts deducted) might accelerate acceptance of offshore funds in the UK retail market. The government notes that these issues of international competitiveness are not new, or primarily the result of the introduction of the PSA or the cessation of TDSI, but nonetheless recognises this as a concern for the industry.

2.7 The life insurance industry welcomed the fact that gains from life insurance contracts are to fall within the definition of “savings income” so that policyholders will benefit from the PSA. It was noted that, while gains from life insurance contracts are received by policyholders as having suffered tax at the basic rate, that credit is not repayable to recipients with no liability to tax. It was suggested that this would inevitably make such policies comparatively less attractive as investments. However, the government notes that this is not in principle a new situation. Although the PSA will increase the number of policyholders with no tax to pay on life insurance gains, it is a long-standing feature of the tax system that such credits are not repayable to non-taxpayers, and not a consequence of the new relief.

2.8 Institutions which make use of existing exceptions to obligations to deduct tax (such as, for example, the “quoted Eurobond exception” at section 882 ITA 2007) were concerned that those exceptions should continue, notwithstanding any changes to existing obligations.

2.9 Almost all responses supported the general aim of simplification and stressed the desirability of a tax system that is easy to negotiate and to comply with. However, there was a tendency for different categories of respondents to interpret this differently. While some payers of interest and other savings income did make

reference to impacts on taxpayers, on the whole they tended to be concerned with potential reductions in the administrative burdens and costs to themselves of complying with withholding obligations.

“For business, the cost of complying with the withholding tax regime is the most important issue.”

“The most important issue is that the option chosen should not create undue additional administrative work and complexity for interest payers and that there should be a level playing field between different types of payer.”

2.10 On the other hand, responses representing the views of recipients of savings income (along with some payers) placed emphasis on minimising complexity for the greatest possible number of recipients, especially lower income groups, who are less likely to have access to professional advice. These respondents tended to emphasise the importance of individual taxpayers being aware of, and understanding, their tax position and responsibilities. Education of taxpayers was seen as a key issue, whatever option might ultimately be adopted. Respondents suggested that some taxpayers may be confused if some types of savings income are subject to withholding, while others are not. The government shares this view of the importance of taxpayer education and will continue to work with the financial services industry to improve customer understanding.

“The key issue is making sure it is as easy as possible for recipients to pay and HMRC to collect the right amount of tax...”

“...the consultation notes the importance of taxpayers being aware of and understanding their tax position and associated responsibilities. We think this is the most important issue.”

Preferred options

2.11 The consultation asked which of the identified options would best balance the factors mentioned at paragraph 1.7 and, separately, which option respondents preferred. Generally, individual respondents gave the same answer to both these questions.

2.12 Respondents' preferences tended to follow the assessment of key issues in that there was a broad split between those which focused on impacts on payers of interest and those primarily concerned with the implications for recipients. Respondents found it difficult to identify any of the options as fully meeting the needs of both these sets of interested parties, and that difficulty was explicitly recognised by some.

“We agree with the key aims set out at paragraph 1.5 of the consultation document. There is a need to balance them and it should be noted that a tension might arise between them.”

Payers of interest

2.13 In numerical terms, the most commonly expressed preference overall was for general removal of withholding obligations on interest generally, in line with the treatment of bank and building society interest (Option 2). This reflected the fact that the majority of responses came from bodies bearing the bulk of the obligation to withhold, report and account for tax – that is, financial institutions and their advisers or representative bodies.

2.14 Among financial institutions, professional firms and industry representative bodies, Option 2 was the clear favourite, being selected as first preference by around 70% of respondents in this category for two main reasons. First, this option was seen as providing parity of treatment between interest on bank and building society accounts and other forms of savings income. Second, it was favoured on the grounds of administrative simplicity and cost for payers of savings income. In addition some interest payers expressed the view that cessation of deduction at source from interest generally would be simpler for individual investors to understand.

“Option 2 is the preferred option – it is the simplest and provides a level playing field between both banks and others paying interest.”

“Option 2 is the simplest solution as it doesn’t require systems development.”

“Option 2, the removal of the obligation to pay tax from all non-TDSI Interest, is the only viable option.”

2.15 Within this category of respondent, the next most popular choice was Option 5 (13% of all respondents), under which individuals would be permitted to elect to receive interest either with or without deduction of tax. However, those selecting Option 5 were heavily concentrated in the P2P sector.

2.16 Overall, payers of interest did not favour options which would require them to distinguish between groups of recipients and to treat them differently. Thus, there was little support for Option 3, Option 4 or, outside the P2P sector, Option 5. Under these options payers would need to distinguish between recipients on the basis of their circumstances, the amount of interest paid or elections made. Generally these options were seen as more complicated and costly to operate and more difficult for customers to understand in comparison to Option 2.

2.17 Option 6 would involve considering wider reform of the withholding obligations in Part 15 of ITA 2007, perhaps extending beyond interest and savings income to royalties and annual payments. The consultation document did not go into detail

about what such wider changes might entail – that would require further consideration. Perhaps partly for this reason, very few respondents expressed a preference for pursuing wider change in the short term. However, a number did favour a more general review of withholding obligations as a longer term objective. Those expressing this view thought that either Option 1 or Option 2 (retaining or removing existing withholding rules on non-TDSI interest) should be adopted in the short term.

Recipients of interest

2.18 In line with the key issues identified for individual recipients of savings income, responses from or representing this group preferred options seen as providing the most clarity to taxpayers about their tax obligations, especially where savings income is received from more than one source. They favoured options that would minimise interaction with HMRC for the maximum number of savers.

2.19 There was however no clear consensus as to which option best achieved these aims. This reflects the fact that the varying circumstances of different groups of taxpayers mean that no single option exactly meets the needs of all. For example continuation of current rules may suit basic rate taxpayers with tax to pay on savings income, and would involve no change to the obligations of higher rate taxpayers with tax to pay. On the other hand, those with no tax liability on savings income might prefer cessation of deduction, removing the need to claim repayments of tax. These various impacts were discussed in Chapter 5 of the consultation document.

2.20 Perhaps reflecting this variety of tax circumstances which may apply to different recipients of interest, responses from or on behalf of recipients tended to favour options which take a more tailored approach than simply retention or abolition of existing withholding rules, or which would permit flexibility.

2.21 Most respondents in this category wanted individuals to be able to opt for, or out of, deduction of tax at source (Option 5), while others preferred removal of withholding for payments to individuals only (Option 3). It was noted however that deduction at the option of taxpayers would rely heavily on their having sufficient information and understanding of the tax system to make an informed choice. They would also need to be aware of the potential implications of their decision, for example, the possibility of having tax to pay if it is not deducted at source.

“Option 5 is favoured as long as taxpayers are made aware of the potential liability if they opt out [of deduction of tax].”

“Option 3 would have the advantageous result of a more accurate outcome for many recipients of interest, meaning less of a burden for taxpayers and HMRC. It would be more complex for payers of interest, but would create less opportunity for confusion among taxpayers. For individuals, the message would be the same as for TDSI interest, so taxpayer education would be more straightforward.”

2.22 As noted above however, neither of these options found favour with payers of savings income, who saw them as administratively complicated and costly.

Other options

2.23 Although all respondents expressed a preference for at least one of the proposed options, other possibilities were also suggested, including:

- Abolishing withholding on certain defined types of interest, such as interest paid by insurers on late paid claims.
- No tax deduction from any income that falls within the PSA.
- Following the system used in France under which no tax is withheld on interest payments except where they are made to recipients in “non-cooperative states or territories”.
- Reclassifying reward payments arising on bank accounts, currently treated as annual payments, as savings income within the PSA with no withholding.
- Not implementing the PSA or any changes to withholding in order to avoid the need to change tax legislation and payers’ IT systems.
- Bringing forward the implementation of HMRC’s digital tax accounts for collection of tax on savings income, building on existing requirements for reporting of information to HMRC by payers.

Particular types of savings and investment income

2.24 The consultation document acknowledged that the issues raised might have particular implications for certain types of savings product. It therefore invited representations from, and direct discussions with, the industry sectors concerned. The savings products it particularly identified were collective investment schemes, life insurance contracts and P2P lending. Responses from all of these sectors welcomed the PSA as benefiting both the UK financial services industry and savers.

Collective investment schemes

2.25 As noted above, the funds industry strongly favoured abolition of tax deductions from interest distributions made by authorised investment funds and investment trusts, whether or not withholding on non-TDSI interest generally were to continue. This was seen as a significant issue for the industry, and in line with the government’s commitment to simplify and streamline taxes on the sector in its Investment Management Strategy⁵. As noted above, the industry expressed concerns about competitiveness with non-UK funds, but more particularly with other UK savings vehicles. It suggested that general ending of withholding on interest would be the most straightforward outcome for investors with savings income from more than one

⁵ The Investment Management Strategy, published in March 2013, can be found at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/258952/uk_investment_management_strategy_amended.pdf

type of vehicle, for example, interest from bank savings accounts and distributions from authorised investment funds.

“Limiting removal of [withholding] to bank and building society interest only will create an unlevel playing field for savings products in the UK and in Europe, add significant burdens for regular UK savers in authorised funds and overlook one of the most significant opportunities for simplifying the tax regime for UK authorised funds in many years.”

2.26 It was pointed out that authorised funds, being open ended, need to carry out daily pricing calculations, in which tax withheld is a factor. Where some distributions are, as now, paid with and some without deduction of tax it is therefore necessary to maintain, and price, separate net and gross share classes. Cessation of withholding for all interest distributions would permit rationalisation into a single share class, representing simplification and cost savings for both funds and investors.

2.27 Representations for the funds industry suggested that generally basic rate taxpayers investing in funds are unlikely to have any tax liability on savings income, either because the investment is held in a tax exempt Individual Savings Account (ISA) or because the income is covered by other allowances or exemptions, including, from April 2016, the PSA. It was further suggested that the vast majority of those who would have tax to pay on savings income will already be completing tax returns, so that removal of withholding would result in no increased administrative burden for taxpayers and minimal risk to the Exchequer.

Life insurance contracts

2.28 On the whole, withholding of tax on non-TDSI savings income was not considered a major issue for the life insurance industry. The preference was for either Option 1 or Option 2, that is, for retention of the current non-TDSI withholding rules or their general abolition.

“We favour options 1 and 2 over the other options. The other options have the potential to confuse customers and add complexity to systems and processes.”

2.29 The main point raised was the longstanding fact that, whilst gains from life insurance contracts issued by UK insurers or UK branches of non-UK insurers are currently treated as having suffered basic rate tax, no repayment is available to non-taxpayers, as is the case for interest paid with tax deducted, for example. There was concern that this could make life insurance products less attractive as investments.

2.30 However, the government notes that this is not in principle a new issue arising as a result of the PSA or the cessation of TDSI withholding. The existing treatment of life insurance gains does not amount to withholding in the sense that it applies to interest. No deduction is made from the sum paid to individual policyholders, to be subsequently paid to HMRC. Rather, the current arrangements reflect the unique

regime applying to life insurance companies, under which part of the corporation tax paid is regarded as relating to investment gains made in the company for the benefit of policyholders. In addition, attaching repayable tax credits to life insurance gains would be expected to carry a cost to the Exchequer.

2.31 It was noted that interest paid by life insurance companies arises typically on late paid claims. It is therefore generally a one-off event, meaning that is not subject to withholding under section 874 CTA 2009, which applies only to “yearly” interest paid under an obligation extending over more than one year.

Peer to peer lending

2.32 Overall, the P2P industry considered deduction of tax an important issue. Responses generally favoured abolition of non-TDSI withholding, with some preferring that investors should be allowed to elect for deduction.

2.33 The key themes cited were simplicity for investors and a perceived need for a level playing field across the savings industry. The latter point was seen as particularly significant as this young sector seeks to develop and grow. Responses to the separate P2P consultation “*Deduction of income tax from interest: peer-to-peer lending*” referred to at paragraphs 1.11 and .12 are summarised in Annex B.

Impacts

2.34 Question 6 in the consultation document invited comment on the assessment of impacts in Chapter 5.

2.35 Generally respondents’ comments on key issues and preferred options were largely based on their view of the impacts on, in particular, payers or recipients of savings income. Accordingly, responses to Question 6 tended to summarise and reinforce comments made in answering other questions rather than introducing new points.

2.36 A few responses challenged assessments and assumptions made in Chapter 5 of the consultation document. For example, one disagreed that retaining current withholding arrangements would have an insignificant effect on taxpayers with savings income above the PSA, although other responses agreed with that statement.

2.37 The consultation document anticipated no wider economic impacts from changes to non-TDSI withholding. A small number of responses suggested that removing withholding requirements would have a positive effect on the UK economy generally.

“We think the impact on the UK economy generally of abolishing withholding tax would be positive and make the UK a more competitive jurisdiction.”

2.38 Some payers of interest stressed the need for certainty over the government’s intentions in order to allow time for any changes to be implemented, although in most cases these comments were in the context of the introduction of the PSA itself and the cessation of TDSI, rather than potential changes to non-TDSI withholding.

2.39 For banks and building societies any changes in respect of non-TDSI withholding would add to the work needed to implement the cessation of TDSI deductions. P2P platforms anticipate changes to the way withholding rules apply to the sector in any case because of the existing issues referred to in paragraphs 1.11 and 1.12, and responses from the funds industry indicated that, in the event that non-TDSI withholding were to cease, implementation should not be a significant difficulty.

3. Conclusions and next steps

3.1 This chapter explains the government's view of the consultation and outlines the way forward. It deals first with non-TDSI tax withholding obligations generally and, secondly considers the particular representations made on behalf of the funds, life insurance and P2P industries.

Non-TDSI withholding

3.2 The aim of the consultation was, as explained in paragraph 1.7, to determine which, if any, of the proposed options best balanced the requirements of:

- Making it as easy as possible for recipients of savings income to pay the right tax;
- Minimising risks to the Exchequer if the right tax is not paid;
- Minimising administrative burdens and costs for payers of interest and other amounts; and
- Minimising costs to HMRC of operating and policing the tax system.

3.3 Responses to the consultation, taken together, have not identified any one of the options as clearly reconciling all these objectives.

3.4 At the March 2015 Budget, the government announced its intention to modernise the tax system, replacing tax returns with digital tax accounts. Pursuing that intention, it will shortly publish the "Making Tax Digital Roadmap" setting out its plans to transform tax administration, making it more effective and efficient and easier for taxpayers. Consultations will take place in 2016 on the range of issues covered in the roadmap.

3.5 This will represent a major modernisation of the way in which taxpayers interact with HMRC. Over the course of this Parliament (up to 2020), it will also progressively transform the way in which information is gathered and processed by HMRC. This is likely to include how HMRC collects and processes data from payers of interest and other savings income. The broad intention is that information on such payments, provided by payers, will be processed directly into digital tax accounts for individual taxpayers, and thereby automatically subject to tax as appropriate.

3.6 Making Tax Digital will contribute to resolving the issues raised in this consultation. In particular, the automatic provision and processing of data by payers and HMRC is expected largely to achieve the consultation's aim of making it as easy as possible for recipients of savings income to pay the right tax. Under Making Tax Digital most taxpayers should need to do no more than to check the information which appears in their digital tax account, reducing the risk of taxable income not being

reported to HMRC. At the same time, the digitalised process envisaged will reduce the administration required from HMRC.

3.7 This work will therefore have a major impact on each of the four objectives of this consultation. In these circumstances, and given the lack of consensus on a clearly favoured consultation option, the government believes that in the short term there is little value in pursuing general changes to non-TDSI withholding arrangements. Rather, the government intends to keep under review the need to retain withholding requirements as Making Tax Digital develops. Changes to the withholding rules can thus be made in step with wider developments in the way tax liabilities are identified and paid.

Collective investment schemes, P2P and life insurance

3.8 The government has noted carefully the points made specifically in respect of these sectors, and is grateful for the input received. The question is whether the case made warrants more immediate changes to withholding in those sectors, outside the general approach outlined above.

3.9 The government has not yet reached a decision on this question 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.

3.10 In the case of life insurance, the government has not identified a compelling case for specific changes, and does not intend to amend the existing arrangements as a result of this consultation. The rules implementing the PSA will however ensure that the allowance is applied to other types of savings income before life insurance gains. This will minimise situations in which no repayment is available in respect of non-taxable gains treated as taxed at the basic rate, as explained in paragraph 2.30 above.

Annex A: List of respondents

Below is a list of those who provided written responses to the consultation:

Arundales	Investment and Life Assurance Group
Association of Accounting Technicians	International Financial Data Services
Association of British Insurers	KPMG
Association of Financial Mutuals	Lancashire County Council
Association of Investment Companies	Leicester City Council
Association of Tax Technicians	LendingCrowd
BDO	LendingWorks
British Bankers' Association	Loan Market Association
British Land	London Society of Chartered
Building Societies Association	Accountants
CIOT	Low Incomes Tax Reform Group
Co-Operatives UK	M&G Investments
Co-Op Bank	Mazars
Deloitte	Nationwide Building Society
Eversheds	Old Mutual
EY	P2PFA
Fidelity Worldwide Investments	PWC
Funding Circle	Ratesetter
FundingKnight	Standard Life
GLI Finance Limited	ThinCats
Institute of Chartered Accountants of Scotland	UK Crowdfunding
International Financial Data Services	West Bromwich Building Society
International Capital Market Association	Zopa
Investment Association	Zurich Insurance

In addition, a number of responses were received from individuals.

Annex B: Responses to the “*Deduction of income tax from interest: peer-to-peer lending*” consultation

This annex gives a brief summary of responses to the questions posed in the separate P2P consultation described in paragraphs 1.11 and 1.12.

Q.1 – *Do you agree that the rules should be amended so that a borrower should treat all of the interest they pay on a P2P loan in the same way even when that loan is funded by investment from multiple lenders? Please explain why.*

All of the respondents thought that the rules should be amended for tax simplification purposes and to ensure that the P2P industry is on a level playing field compared to other finance options.

Q.2 – *Do you agree that the rules should be amended so that a lender will receive all of the interest that they receive from their P2P portfolio in the same way? Please explain why.*

All of the respondents agreed that the rules should be amended so that a lender will receive all of the interest that they receive from their P2P portfolio in the same way. This would avoid unnecessary complexities, such as the lender having to work out how much of their interest has already been taxed.

Chapter 3 proposed changes

Q.3 – *Do you agree that the rules should be amended so that any deduction of tax should be made by the P2P platform and not by the borrower? Please explain why.*

Most respondents agreed that the responsibility for deducting tax should fall on the P2P platforms. The main reason was that the platform (rather than the borrower) would have all the relevant information and have the resources to comply with and manage the withholding regime.

Some accounting bodies expressed concern that shifting the responsibility to platforms could act as a barrier to new entrants to the rapidly growing P2P industry.

Q.4 – *Do you think that it would be appropriate for any change to the rules to also allow for any obligation to deduct tax to apply to other intermediaries? Please explain why.*

Although most respondents agreed with this suggestion, they tended to emphasise that the rules need to be explicit in stating who is legally responsible for the deduction of tax, and whether, for example, the deduction function can be outsourced.

Of those respondents that disagreed with the application of withholding tax to P2P income in general, several commented that intermediaries should nonetheless be required to deduct tax if they are aware that lenders are based overseas.

Q.5 – *Do you agree that the rules should be amended so that the test for whether tax should be deducted on P2P interest payments should only be the identity of the lender and not the identity of the borrower? Please explain why.*

All of the responses agreed with this proposition. It was felt that this would remove an imbalance within the current tax regime which, if left alone, would restrict the growth of the P2P industry. It would also help simplify the deduction process.

Q.6 – *Do you think that the rules should be amended so that whether tax should be deducted on P2P interest payments is no longer linked to the duration of the loan? Please explain why.*

Most responses agreed with this proposal on the basis that as P2P platforms have lenders with a diverse portfolio of P2P loans with varying durations, receiving some interest payments net and some gross would be confusing.

However a few responses disagreed, also on the basis that P2P platforms offer a diverse range of loans with varying durations. They thought that, as some lenders specifically invest in short term lending on which interest can be paid gross, removing the link to loan duration completely could mean that this type of lending would be less competitive when offered through a P2P platform.

Q.7 – *If you do not agree with these amendments [Q.4, Q.5 and Q.6], what other criteria do you think the obligation to deduct tax should depend on? Please explain why.*

The majority agreed with the amendments. However, some in the P2P industry suggested that P2P platforms should be responsible for informing their customers about the tax rules and assist them in understanding their tax obligations where P2P lenders' savings income exceeds the PSA. Only in the case where P2P platforms have lenders overseas should they be required to deduct tax at source.

Q.8 – *Would allowing the return and payment of tax deducted on P2P interest on an annual basis rather than a quarterly basis make it easier to deduct the correct amount of tax (from the total amount of interest that the lender is treated as having received from their P2P portfolio in the year)? Please explain why.*

Those who responded to this question were from the P2P industry. They pointed out that an annual process would be administratively less burdensome and that another consideration would be how the proposed reliefs for bad debts in the P2P sector would be implemented. If this could be granted at source and carried across platforms then an annual payment would be easier.

Q.9 – *Alternatively would it be simpler if parties responsible for deduction of tax on P2P interest were subject to the same quarterly return and payment requirements as those responsible for deduction of tax from other forms of interest? Please explain why.*

The responses were unanimous and agreed that administratively an annual return would be easier.