

DRAFT EXPLANATORY MEMORANDUM TO

THE INDIVIDUAL SAVINGS ACCOUNT (AMENDMENT NO. XX) REGULATIONS 2017 2017 No. [XXXX]

1. Introduction

- 1.1 This explanatory memorandum has been prepared by HM Revenue and Customs (HMRC) on behalf of HM Treasury and is laid before the House of Commons by Command of Her Majesty.

2. Purpose of the instrument

- 2.1 The instrument establishes a new Individual Savings Account (ISA), the Lifetime ISA, from 6 April 2017. It sets out eligibility conditions for opening and paying into the new account; the amount and type of payments that can be made; and which investments can be held in the account. It also provides for a 25% government bonus to be payable on amounts paid to the account; specifies circumstances in which sums may be withdrawn from an account without a charge; and provides for the application of a 25% charge to other withdrawals. The instrument also sets out rules for how an account provider claims a bonus that is due, and for the collection and payment of withdrawal charges or other amounts due to HMRC. In addition, the instrument increases the overall ISA subscription limit (currently £15,240) to £20,000.

3. Matters of special interest to Parliament

Matters of special interest to the Select Committee on Statutory Instruments

- 3.1 None.

Other matters of interest to the House of Commons

- 3.2 Disregarding minor or consequential changes, the territorial application of this instrument includes Scotland and Northern Ireland and is not a financial instrument that relates exclusively to England, Wales and Northern Ireland.

4. Legislative Context

- 4.1 An ISA is a tax-advantaged savings product providing relief from tax to individuals. The ISA rules are set out in the Individual Savings Account Regulations 1998 (S.I. 1998/1870) (ISA Regulations), which this instrument further amends.
- 4.2 ISA Regulations currently provide for three different types of ISA (cash ISA, stocks and shares ISA and innovative finance ISA). They specify the investments which can be held in each of these accounts and other account features and requirements.
- 4.3 This instrument is made under existing powers in the Income Tax (Trading and Other Income) Act 2005 (c.5), and the Taxation of Chargeable Gains Act 1992 (c.12), and under new powers in the Savings (Government Contributions) Bill.

5. Extent and Territorial Application

- 5.1 The extent of this instrument is the United Kingdom.
- 5.2 The territorial application of this instrument is set out in Section 3 under “Other matters of interest to the House of Commons”.

6. European Convention on Human Rights

- 6.1 The Financial Secretary to the Treasury, has made the following statement regarding Human Rights:

“In my view the provisions of the Individual Savings Account (Amendment [No.XX]) Regulations 2017 are compatible with the Convention rights.”

7. Policy background

What is being done and why

- 7.1 At Budget 2016 the government announced that it would introduce the Lifetime ISA from April 2017. Lifetime ISA is designed to help young people save for the long-term throughout their lives by enabling them to simultaneously save for a first home and for their retirement. A government bonus will be paid on amounts saved in a Lifetime ISA, and it will be possible to make withdrawals from an account without any charge, in certain circumstances. These include after an account holder reaches a specified age (to be set at 60 by this instrument) or, subject to certain conditions, when an account holder is buying their first home, transfers their savings to another Lifetime ISA or becomes terminally ill. Other withdrawals from a Lifetime ISA will be subject to a charge of 25%.
- 7.2 The instrument amends the ISA Regulations to establish and define the Lifetime ISA as well as certain terms in relation to the new account. It updates ISA Regulation 4ZA to provide a £4,000 limit on ‘current year payments’ (defined in new ISA Regulation 10A) that can be made to a Lifetime ISA each year. An amount held in a Help to Buy: ISA on 5 April 2017, can also be transferred to a Lifetime ISA during 2017-18 and earn a government bonus, without this transferred amount counting towards the £4,000 Lifetime ISA limit.
- 7.3 ISA Regulation 4ZA is also amended to increase the overall ISA subscription limit (currently £15,240) to £20,000 from 6 April 2017.
- 7.4 New ISA Regulation 10A sets out eligibility conditions for paying into a Lifetime ISA (including residency requirements and that, subject to specified exceptions, an individual can only pay into a Lifetime ISA if they are below 50 years old). The instrument also provides (by amending ISA Regulation 4 concerning the general conditions for accounts), that, subject to specified exceptions, an eligible individual may only make payments to one Lifetime ISA each year.
- 7.5 New ISA Regulation 12B sets out the conditions for opening a Lifetime ISA, including a requirement that, subject to specified exceptions, an account can only be opened by an eligible individual aged between 18 and 40 years old. This new regulation also sets out the information, authorisations and declarations required at

account opening, the process that applies where an application is made other than in writing, and arrangements for where an application is made on an individual's behalf because they lack capacity.

- 7.6 New ISA Regulation 8ZA sets out the investments that can be held in a Lifetime ISA. These will be investments which currently qualify to be held in a cash ISA or a stocks and shares ISA.
- 7.7 The instrument also provides, at new ISA Regulation 5DAA, for 'defaulted Lifetime ISA subscriptions' to be made to an account without counting towards the Lifetime ISA or overall ISA subscription limit, following a default by an account provider.
- 7.8 Consequential changes are made throughout the ISA Regulations to provide for the new account. These include modifications to current arrangements at ISA Regulation 4A for the repair of accounts and excess subscriptions. Modifications are also made to the arrangements for account transfers, including in relation to the information that must be provided between account providers on the transfer of a Lifetime ISA. The information requirements for account providers at ISA Regulation 31 are also amended to take into account the Lifetime ISA.
- 7.9 New ISA Regulation 37 introduces a Schedule to the ISA Regulations, making further provision in relation to Lifetime ISA, relating, in particular, to the government bonus and withdrawals.
- 7.10 The new Schedule defines certain terms in relation to a Lifetime ISA, and sets out how a bonus due to an account holder is to be determined. The bonus is calculated at 25% of the qualifying additions (as defined in paragraph 1) made to an account. Qualifying additions are current year payments (as defined in new ISA Regulation 10A) and payments made under the arrangements for transfer of sums held in a Help to Buy: ISA on 5 April 2017, as described above (and set out at new ISA Regulation 10A(4)(c)).
- 7.11 The Schedule also provides detailed arrangements for claims of bonus amounts to be made to HMRC by account providers, including by specifying the claim periods for 2017-18 and subsequent years, and the due date for claims. It also provides a requirement upon account providers to amend claims, and powers for HMRC to enquire into claims. Arrangements are also set out for cases in which a claim is rejected by HMRC, including the right of an account holder to apply to HMRC for the payment of a bonus. Review and appeal arrangements are provided in relation to HMRC's decisions on such an application.
- 7.12 Arrangements are also set out for the recoupage by HMRC of wrongly paid bonus amounts, including who is liable to repay such amounts.
- 7.13 The withdrawal charge that applies to certain withdrawals from a Lifetime ISA is specified at 25% of the withdrawn amount. The Schedule also provides requirements and details concerning withdrawals that can be made without a withdrawal charge being due. It provides that withdrawals can be made without charge after an account holder reaches 60, and the requirements that must be met for a withdrawal on terminal illness of an account holder, or transfer of Lifetime ISA investments to another Lifetime ISA, not to be subject to a withdrawal charge.

- 7.14 The Schedule sets out details of conditions that must be satisfied for a withdrawal in relation to the first-time purchase of a residence not to be subject to a charge. This includes the withdrawn amount must be paid to the account holder's conveyancer, and requirements in relation to the value of the residence (which must be no greater than £450,000); the use of the funds (which must be applied to the house purchase); what constitutes a first-time purchase; and the process and information requirements that must be met by an account holder and their conveyancer in relation to such a withdrawal.
- 7.15 Withdrawn funds must be returned to a Lifetime ISA if a purchase has not been completed within 90 days of these funds being received by the conveyancer. The Schedule provides that a withdrawal charge is due on any such funds not returned. The Schedule also provides definitions of terms used within these rules, with reference to other legislation where appropriate.
- 7.16 The Schedule also specifies circumstances in which removal of sums from a Lifetime ISA will not be considered to be a withdrawal for the purposes of a withdrawal charge, including where the removal is from an invalid Lifetime ISA; is made to settle account fees charged by an account provider; or arises from a default, act or omission not attributable to the account holder.
- 7.17 Arrangements are also set out for the collection and payment of withdrawal charges by account providers, as well as the information returns account providers must give to HMRC. These include a requirement to amend incorrect returns, and powers for HMRC to enquire into returns.
- 7.18 The Schedule also provides for an account holder to apply to HMRC for the repayment of a wrongly made withdrawal charge, and for review and appeal arrangements in relation to HMRC's decisions on such an application.
- 7.19 Finally, the Schedule also makes provision concerning the application of late payment interest on amounts payable to, or by, HMRC; and sets out detailed rules in relation to reviews and appeals in relation to rejections of bonus claims, the application of withdrawal charges, and the recoupment of bonus amounts by HMRC. These include the dates by which appeals must be made and the powers of the Tribunal in relation to these appeals.

Consolidation

- 7.20 There are no plans to consolidate the ISA Regulations

8. Consultation outcome

9. Guidance

- 9.1 HMRC Guidance Notes for ISA providers will be amended to reflect the changes to the ISA rules. The Guidance Notes are available at <http://www.hmrc.gov.uk/isa/isa-guidance-notes.pdf>

10. Impact

- 10.1 The impact on business, charities or voluntary bodies is mainly for financial institutions who choose to offer Lifetime ISA accounts. These businesses will face one-off and ongoing costs from complying with the Lifetime ISA rules. As with other ISAs, the Financial Conduct Authority will regulate the Lifetime ISA and will publish a consultation that will inform the regulatory framework and, therefore, any impacts on businesses above and beyond those set out in the ISA Regulations. There will also be an impact upon conveyancers who handle account withdrawals from a Lifetime ISA in connection with a residential purchase.
- 10.2 The impact upon the public sector is that Exchequer costs for the Lifetime ISA are estimated to reach £830m in 2020-21. HMRC will face additional costs associated with the payment of government bonuses and collection of withdrawal charges. This will require the development of systems to check and pay claims for bonus amounts from account providers, and compliance activity in relation to withdrawal charges. It is also anticipated that there will be additional customer contact for HMRC as a result of the introduction of the new account, as well as costs associated with the approval of account providers. Total additional costs to HMRC are currently estimated to be around £3-3.5 million.
- 10.3 An Impact Assessment has not been prepared for this instrument. An Impact Assessment in relation to Lifetime ISA more generally was published alongside the Savings (Government Contributions) Bill at <https://www.gov.uk/government/collections/the-savings-government-contributions-bill>.

11. Regulating small business

- 11.1 The legislation applies to activities that are undertaken by small businesses.
- 11.2 No action is proposed to minimise regulatory burdens on small businesses.
- 11.3 The basis for the final decision on what action to take to assist small business is that no business will be required to make any changes as result of this instrument. Whether or not a business chooses to offer a Lifetime ISA will be a commercial decision.

12. Monitoring & review

- 12.1 HMRC will monitor the impact of these changes on an ongoing basis using the information provided by Lifetime ISA providers.

13. Contact

- 13.1 Helen Williams at HM Revenue and Customs - Telephone: 03000 512336 or email: savings.audit@hmrc.gsi.gov.uk can answer any queries regarding the instrument.