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Dear Sirs,

Creating a secondary annuity market

We welcome the opportunity to make representations. We confine ourselves to commenting on the following technical tax issues:

- The corporation tax treatment of an insurance company that is an annuity provider;
- Requirements of an annuity provider to withhold income tax;
- Annuity providers' obligations under FATCA/CRS/AEOI;
- The corporation tax treatment of a UK-resident company that has acquired an annuity income stream, and which is not exempt in respect of that investment return.

Corporation tax treatment of an insurance company that is an annuity provider

Before the income stream is sold, the annuity contract will most likely be "pension business" as defined by section 58 of the Finance Act 2012. In our view, this treatment should be maintained after the income stream has been assigned so as to ensure the insurance company's tax position is unaffected. This will require an amendment to section 58 of the Finance Act 2012 to provide that where an income stream of an annuity in a registered pension scheme is sold, or if it is later re-sold, it, together with any reinsurance of it, will still be pension business.

If the annuity contract ceases to be pension business, it is likely to become basic life assurance and general annuity business ("BLAGAB") as defined by section 57 of the Finance Act 2012. BLAGAB is taxed on I – E profits per section 68 of the Finance Act 2012. Non-BLAGAB, which includes pension business, is taxed on trade profits under section 71(1) of the Finance Act 2012 and section 35 of the Corporation Tax Act 2009, unless it is mutual business, in which case it is not taxed at all per section 71(3) of the Finance Act 2012.

The need for an amendment to section 58 of the Finance Act 2012 arises because under current law business ceases to be pension business if the registered pension scheme has its registration withdrawn. Absent this, we believe current law would mean the contract retains its status as pension business. Whilst withdrawal of registration would remain relevant for pension business in build-up, and for pension annuitants, we do not believe breaches of pension rules should affect the purchaser of an income stream or the annuity provider, especially if it were to become the case that registration may be withdrawn if all remaining annuity income streams have been sold.

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Whether an annuity provider is required to withhold income tax

Our reading of existing legislation is that the payment to the assignee is a "purchased life annuity" as defined in section 423 of the Income Tax (Trade and Other Income) Act 2005 ("ITTOIA"). In this regard, we note that once the annuity income stream has been sold, section 366 of ITTOIA, which gives priority to the pension charging provisions in Part 9 of the Income Tax (Earnings and Pensions) Act 2003 over the savings and investment income charging provisions in Part 4 of ITTOIA (which includes section 432), would no longer be in point.

The obligation to withhold income tax on purchased life annuity payments is in section 930(1),(2)(c) of the Income Tax Act 2007, although that obligation is disapplied in respect of an "excepted payment". To be an excepted payment, the assignee would have to be a person referred to in sections 933-937 of the Income Tax Act 2007. As such, for example:

- A payment to a UK resident company would not attract withholding;
- A payment to a non-UK resident company (which does not fall within the exceptions in sections 934 and 936 of the Income Tax Act 2007) would attract withholding, unless that non-UK resident company can claim relief under a Double Taxation Agreement.

HMT may consider this to be the appropriate result, although we note that a withholding charge for non-UK acquirers may restrict the development of a secondary market in annuities. If not, unless we have misunderstood current law, the rules on withholding would need to change.

Regardless of whether tax law on withholding is changed, we would wish to see HMRC guidance explicitly covering the withholding obligations of annuity providers where the income stream has been sold.

The annuity providers obligations under FATCA/CRS/AEOI

We would wish to see HMRC guidance explicitly outlining the annuity provider's obligations under the Foreign Account Tax Compliance Act ("FATCA"), Common Reporting Standard ("CRS") and Automatic Exchange Of Information ("AEOI") in respect of annuity income streams that have been sold.

Specifically, we would wish the following points to be covered:

1) Whether a pension annuity the income stream of which has been sold remains an Exempt Product for FATCA purposes and, if not, whether it would be considered an Annuity Financial Account;
2) The practical FATCA compliance steps that an annuity provider would be required to take when the income stream from a pension annuity is sold on the secondary market; and,
3) Whether any differing treatment is envisaged under CRS.

The corporation tax treatment of a UK corporate that has acquired an annuity income stream, and which is not exempt in respect of that income

The Call for Evidence proposes that, where the investment into an annuity income stream is a trading investment, then profits and losses would be taxed within the trade profit/loss measure. We note that section 46 of the Corporation Tax Act 2009 provides that it is profits or losses calculated under generally-accepted accounting practice that will be taxed/relieved. We agree that this is appropriate.

This rule will not apply where trade profits are not taxed under section 35 of the Corporation Tax Act 2009. This would be the case where:

- The company is not trading;
- The company's trade is a mutual trade; or

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- In respect of an insurance company's BLAGAB charged to tax on I – E profit under section 68 of the Finance Act 2012.

The Call for Evidence proposes that, where trade profits are not an appropriate basis of taxation, the annuity income stream is taxed as miscellaneous income. The Call for Evidence does not suggest how the tax measure of miscellaneous income should be calculated so as to:

- allow for relief for the costs of acquiring the income stream;
- cater for losses that may arise;
- tax (or not tax) profits and losses on re-sales of the income stream.

Nor does it say whether all income stream profits will be taxed as a single item of miscellaneous income, or whether a separate charge will be calculated in respect of each acquired income stream.

We believe it is appropriate to tax profits and losses on re-sales of the income stream, and give relief for the costs of acquiring the income stream, under income provisions rather than as capital. In that case, sections 37 to 39 of the Taxation of Chargeable Gains Act 1992 should mean no chargeable gains or allowable losses would arise, though this could be put beyond doubt by amending section 210 of that Act so that acquired pension annuity income streams are exempt.

We suggest adopting one of the following two possible approaches for taxing the return as income:

(1) Bring profits as calculated by generally accepted accounting practice into charge. This could be achieved by deeming the investment in the annuity income stream to be a loan relationship, similar to the measures on investment life insurance contracts in Chapter 11 of Part 6 of CTA 2009. Such a rule should automatically address all three bullets above. It could apply to both the trading and non-trading scenarios.

(2) Introduce a new head of charge for annuity income streams (taken together). Outgoings, such as acquisition costs, should be immediately deductible. Receipts of annuity income and profits on re-sales would be brought within the charge to tax on income. Losses could be carried forward against future profits under the head of charge, or provisions could be introduced to permit greater flexibility.

Since the Call for Evidence proposes that retail investors will not be able to acquire annuity income streams, we do not consider potential income tax rules for investors.

Yours faithfully,

Tax Policy Group