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Matters of current interest

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Topics

New life tax regime

- Commercial allocation
- Tax reporting and modelling

Changing tax environment

- Tax rates, tax transparency & General Anti-Abuse Rule

Commercial allocation

- Actuaries, tax and finance working together
- Requires appropriate granularity and agreement with HMRC
- Tax does not distort commercial result, need to factor any lost synergies into product pricing
- MCEV modelling easier

Tax reporting and modelling

Drivers which are transforming tax profiles

- Single 20% rate from 2015
- Post RDR new business
- Run off of BLAGAB
- Final determination of transitional adjustments
- No XSE from new protection business
- BLAGAB and non-BLAGAB taxed independently

Combine to define a new tax profile for many companies

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Tax reporting and modelling

Modelling opportunities

- Simplify models and processes with proportionate approaches.
- Reduce validation effort around tax.
- Improve accuracy of internal model calibration.
- Reduce capital requirements (though recognition of loss absorbency of tax).
- Improved transparency, management information and governance.

Tax reporting and modelling

Alignment of policyholder and shareholder rates

- From 1 April 2015 but will be enacted in 2013 so can be anticipated in 2013 YE results
- BLAGAB trade profit computations will soon have no practical effect in an XSI company and often no impact in an XSE office (if there are sufficient non-taxable dividends)
- Carried forward BLAGAB trade losses may have no value in an XSI company
- Further narrowing of circumstances where second order/iterative effects may be relevant to deferred tax
- Rather than blended rates can BLAGAB be now be excluded from shareholder tax modelling?

Capital modelling: financial and process benefits

	Correct , enhance and simplify		Optimise	Validate	Future-proof
	Get BEL models to do elementary I-E tax well	**Ensure Internal Model is adequate for shareholder DTAs**	**Develop pragmatic I-E DTA recognition policy and process**	**Implement efficient and well-reasoned tax validation approach**	**Understand how LADT will run down**
Key benefits	▪ Eliminate any spurious tax credit for XSE. ▪ BEL withstands scrutiny. ▪ Rely on as source of validation evidence.	▪ Simplified process reduced time and cost. ▪ Avoid booking unsupportable DTAs	▪ Proportionate practices. ▪ Clarity on whether to impair I-E DTA	▪ More focussed validation. ▪ Less data/modelling. ▪ Rely on expert tax technical analysis rather than pure modelling.	▪ Identify any mitigating actions. ▪ Measure and articulate risks in more optimistic stances.
Key considerations	▪ Design and calibration of any XSE cap.	▪ Internal Model may be adequate for GRB tax. ▪ BLAGAB trade DTAs may be immaterial. ▪ Dividend income	▪ I-E tax profile ▪ Are IFRS DTA's impaired? ▪ Asset stresses ▪ Key economic assumptions ▪ Capital losses	▪ Can MI from BEL models contribute validation evidence? ▪ Ambitious automation and tax modelling solutions may not be best approach.	▪ 10 year transition. ▪ Prospective fund mergers. ▪ Can future profits be identified and modelled more comprehensively?

Solvency II / ICA+ ?

Some possible actions

- Identify differences between IFRS and FSA profits and consider how these can be captured in modelling if material
- Use basic I-E tax logic in Internal and BEL models rather than offline “tax validation model”
  - Allow extraction of better management information
- Test assertion that BLAGAB trade profits are irrelevant and allow conclusion to drive simplification in models, process and validation
  - Measure run off of BLAGAB items
  - Establish drivers of IFRS volatility
- Ensure capital modelling also meets FSA tax agenda of transparency and validation.

Changing tax environment

- UK corporate tax rates continue to fall: now 23% from 1 April 2013; then 21% from 1 April 2014 and 20% from 1 April 2015.
- But increased scrutiny of tax by Government and Press – where are profits generated, where is tax paid and how is it reported.
- General Anti-Abuse Rule (GAAR) in addition to existing Disclosure of Tax Avoidance Schemes (DoTAS)

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