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Shareholder tax calculation

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Non-BLAGAB trading profits – calculation basis

- Trading profit calculation (with modifications)
 - s35 CTA 2009 applies
 - Plus dividends taxed
 - Asset value changes taxed rather than capital gains
- “Gross roll up” basis
 - No tax on investment return to policyholders
 - Shareholder profits taxed at corporate tax rate
 - Applies to mutual insurers but any profit exempted from tax



Non-BLAGAB trading profits – calculation principles

- Identify non-BLAGAB accounting profits and losses
 - Use acceptable commercial method to allocate between BLAGAB and non-BLAGAB
 - Should fairly represent non-BLAGAB contribution to total profits
 - Include allocation of unmatched items
 - Apply fiscal adjustments (see next slide)
- Method must be consistent with allocation of income and gains to I-E
- To be agreed with HMRC
- Regulation making powers in FB 2012.



Non-BLAGAB trading profits – fiscal adjustments

- Include:
 - Dividends taxed notwithstanding general exemptions
 - Movement in index-linked gilt-edged securities
 - Profit/(losses) on assets moving from non-BLAGAB to BLAGAB
 - Transitional adjustments
 - Pre 2013 non-BLAGAB DAC amortisation.
- Exclude:
 - Receipts and expenses on long term business fixed capital
 - Profits/(losses) on intra-group insurance business transfer schemes



Non-BLAGAB trading profits – application to with profit funds

- Profit allocations
 - With profit funds often managed as single pool of assets
 - Time consuming to identify shareholder return by category
 - Total shareholder return is identifiable
 - Allocation needs to be consistent with form of return e.g. bonuses, management fees, guarantee fees
 - So could have several allocation bases in a single fund.



Purpose of calculating BLAGAB trade profits

Why do we need a calculation of BLAGAB trade profits?

- Only of relevance to proprietary companies, not mutuals
- I-E computation taxes both shareholders and policyholders
- BLAGAB trade profits calculation is required to:
 - Calculate the shareholders' share, or
 - Determine the minimum amount of I-E profit for the period – Minimum Profits Test
- Shareholders' share of I-E profit is taxed at CT rate (currently 23%)
- Policyholders' share of I-E profit is taxed at 20% rate
- Losses can be group relieved.



BLAGAB trade profit or loss?

Clause 136: Definitions

- A company has a BLAGAB trade profit for an accounting period, if
 - calculated in accordance with ordinary trading rules (s35 CTA 2009)
 - there are profits of the business for the accounting period that
 - but for the requirement to charge under the I-E rules
 - would be chargeable to corporation tax under s35 CTA 2009.
- This means that s46 CTA 2009 applies and tells us to calculate the profits of the trade in accordance with GAAP.

Replicated for a loss



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BLAGAB trade profit – starting point

GAAP profit before tax

- Akin to non-BLAGAB long term business profits computation
- Starting point is GAAP profit before tax – to be allocated to BLAGAB.

	£	£
Liabilities brought forward		X
Premiums		X
Investment income and gains		X
		X
Expenses and interest	X	
Claims	X	
Liabilities carried forward	X	
		(X)
GAAP profit before tax		X
Tax		(X)
Profit after tax		X



BLAGAB trade profits computation

BLAGAB trade profits computation

	£	£
GAAP profit before tax		X
Less: Profits of long term business fixed capital	(X)	
Less: Non-BLAGAB long term business profits	(X)	(X)
Profits allocated to BLAGAB		X
Add: Disallowed BLAGAB expenses	X	
Add\(\Deduct): Transitional adjustment to new regime (spread over 10 years)	X	
Add: Pre-2013 DAC amortisation	X	
Less: Capital allowances	<u>(X)</u>	(X)
Less: Policyholders' tax – current/cash	(X)	
Less: Policyholders' tax – deferred	(X)	(X)
BLAGAB trade profits		X
BLAGAB trade losses brought forward		(X)
Adjusted BLAGAB trade profit		X



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BLAGAB trade profit calculation – commercial allocation

- Accounting profit or loss and tax adjustments to be allocated between BLAGAB and other long term business under an **acceptable commercial method**



- Fairly represents the contribution made by those businesses
- See 'non-BLAGAB long term business profits' section



BLAGAB trade profit – policyholder tax adjustment

- Policyholder tax – allocable expense in arriving at shareholder profits, i.e. BLAGAB trade profits
- How is it measured?

The old

- Long and tortuous history
- Variety of methods
- Generally only current tax

The new

- **Current tax**
 - cash tax payable at 20% for that period
- **Deferred tax**
 - movement in certain account balances



BLAGAB trade profit – policyholder tax adjustment, deferred tax

Per GAAP accounts

Closing deferred tax balance for period of account	(X)
Less:	
Closing deferred tax balance for previous period of account	(X)
<hr/>	
Tax expense or receipt	(X)

Example

C/F deferred tax liability – per GAAP accounts	(200)
Less:	
B/F deferred tax liability – per GAAP accounts	(120)
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Deduction in arriving at BLAGAB trade profits	(80)



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BLAGAB trade profit – policyholder tax, deferred tax definition

What is policyholder deferred tax? (clause 108)

BLAGAB matter

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Calculated by reference to the policyholder rate of tax



- Excess BLAGAB expenses
- Spread acquisition expenses
- Other future deductible BLAGAB expenses
- BLAGAB allowable loss
- Capital losses (unit trust and OEIC deemed disposals)
- Unrealised chargeable BLAGAB gains.

- Must be shown in the GAAP accounts.

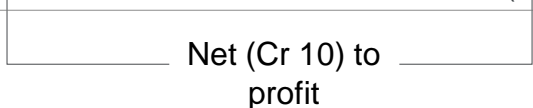


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BLAGAB trade profit – policyholder tax, deferred tax example

Example – deferred tax account

Balances – (Dr)/Cr	Year 1 Closing balance	Year 2 Adj to opening balance	Year 2 Revised opening balance	Year 2 P/L Dr/(Cr)	Year 2 Closing balance
Unrealised gains	500	(50)	450	100	550
S212 spread gains	1,000	-	1,000	(200)	800
Capital losses	(200)	100	(100)	-	(100)
DAE	(300)	(20)	(320)	20	(300)
Total	1,000	30	1,030	(80)	950
Tax at 20% (net liability)	200	6	206	(16)	190


 Net (Cr 10) to profit

What is the policyholder deferred tax deduction for BLAGAB trade profits for year 2?

Example – deferred tax deduction/income

Closing balance year 2 (liability)	(190)
Less: Closing balance year 1 (liability)	(200)
Policyholder tax receipt for year 2	10



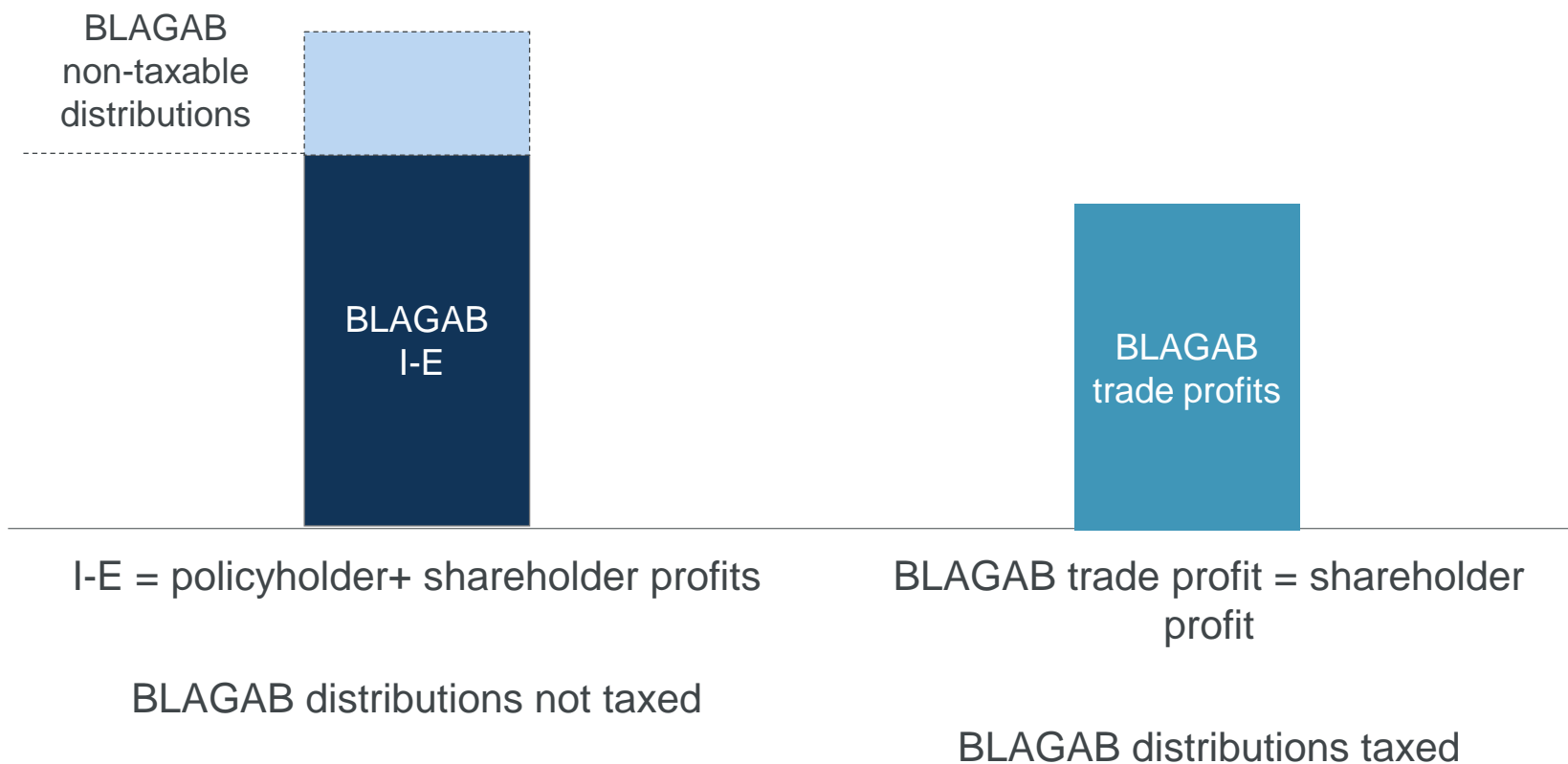
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BLAGAB trade profit – two purposes of comparison with I-E profits

- I-E profit split between
 - Shareholders share taxable at full CT rate (23%)
 - Policyholder share taxable at basic rate of income tax (20%)
- Determine the minimum taxable I-E profit (the shareholder profit).



BLAGAB trade profit – comparison with I-E profits, step 1



BLAGAB trade profit – comparison, policyholders' share of I-E profit

How much I-E profit should be allocated to policyholders and how much to shareholders ...

Deduction of non-taxable distributions from BLAGAB trade profits

- The policyholders' share of I-E profit is found by deducting the BLAGAB trade profits from the I-E profit
 - Non-taxable distributions are not included in I-E but are included in BLAGAB trade profits, therefore we need to remove the BLAGAB element from the BLAGAB trade profits before doing the above calculation
 - Only deduct the 'shareholders share', as BLAGAB trade profits is shareholder profit only

Shareholders share (*previously known as 'A/B'*)

$$\frac{\text{BTP}}{\text{BNTD} + \text{I}}$$

- The shareholders share is calculated by using the relevant proportion:
 - BTP = BLAGAB trade profits (i.e. shareholders profit)
 - BNTD = BLAGAB non-taxable distributions
 - I = BLAGAB income and chargeable gains (less losses) + miscellaneous receipts + minimum profits

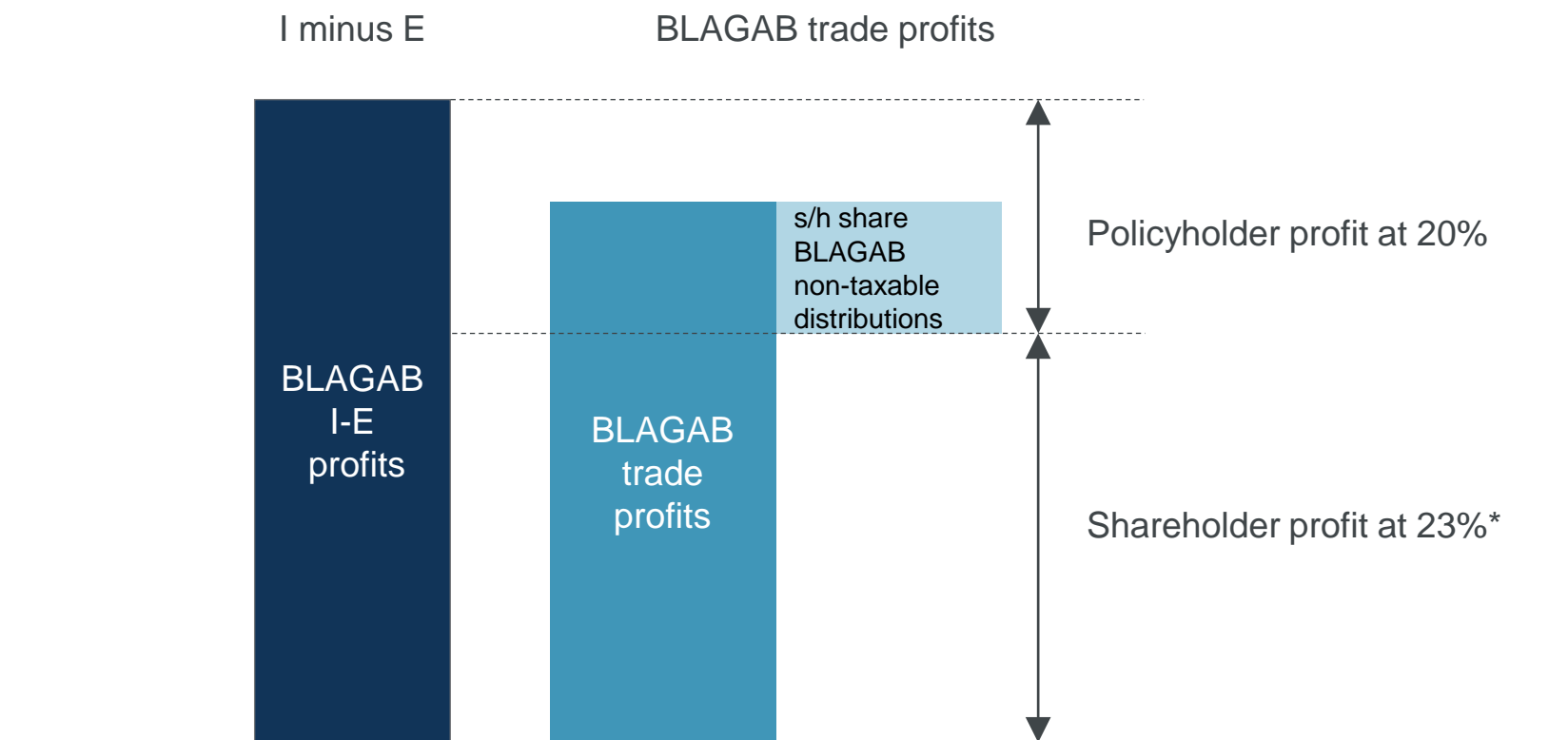
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$$\frac{\text{BTP}}{\text{BNTD} + \text{I}} \geq 1 \Rightarrow \text{All shareholder}$$



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BLAGAB trade profit – comparison with I-E profits, step 2



*Per 2013 Budget
23% from 1 April 2013
21% from 1 April 2014
20% from 1 April 2015



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BLAGAB trade profit – shareholder and policyholder profits

	£	£	£
Chargeable gains less allowable losses allocated to BLAGAB		6,000	
BLAGAB income		500	
BLAGAB income and gains		6,500	
Relief for non-trading loan relationship deficits		-	
Relief for BLAGAB management expenses		(60)	
BLAGAB I-E profits		6,440	
BLAGAB trade profits (after deducting policyholder tax)	3,884		
Less shareholder's share of BLAGAB dividends	(330)		
Shareholders profits taxed at 23%		(3,554)	x 23% = 817
Policy holders share of I-E profit (clause 103)		2,886	x 20% = 577
Total tax			1,394
Policyholder share			
<i>Calculation of I + BNTD</i>			
BLAGAB income and gains	6,500		
BLAGAB distributions	600		
I + BNTD	7,100		
Shareholders' fraction $BTP / (I + BNTD)$ $3,884 / 7,100 \times 100\%$	55%		
<i>Shareholders' share of non-taxable distributions</i>			
BLAGAB distributions	600		
Shareholders' share $55\% \times 600$	330		



BLAGAB trade profit – examples of different profiles – tax payable at s/h and p/h rates

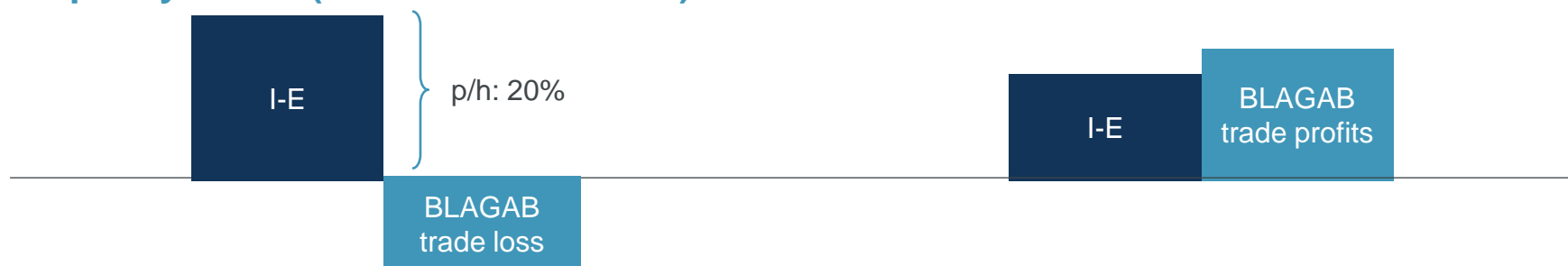
Part policyholder, part shareholder



All shareholder (BLAGAB trade profits > I-E)



All policyholder (BLAGAB trade loss)



Note 1

XSE profile – where I-E is less than BTP

XSI profile – where I-E greater than BTP

Note 2

The shareholder profiles above do not show the minimum profits adjustment, hence no tax rates are shown



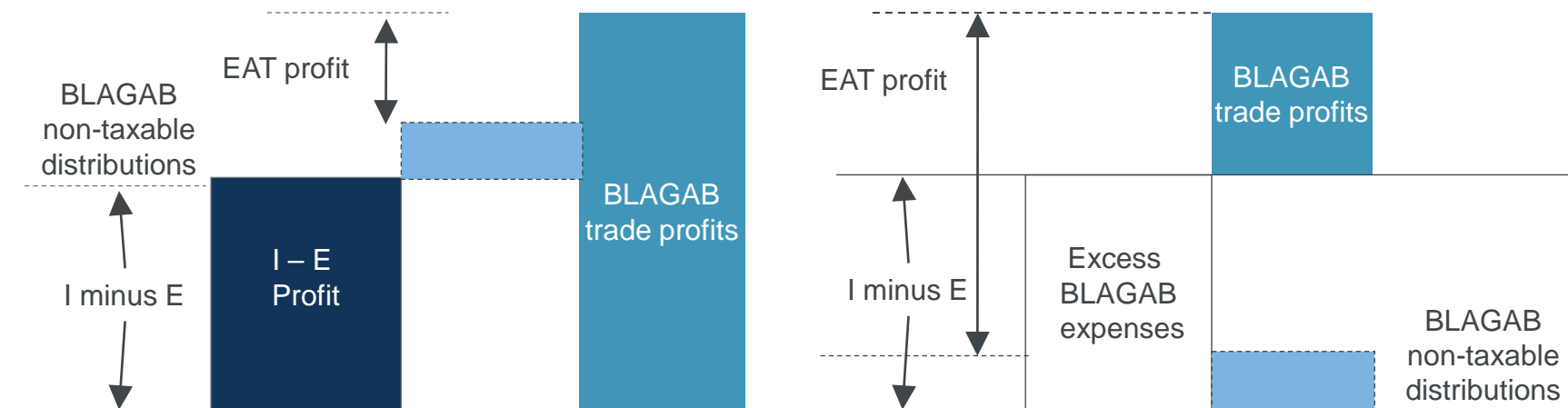
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BLAGAB trade profit – calculation of minimum BLAGAB profits

- Comparison of two profits:
 - I-E profit (assessed on I-E)
 - BLAGAB trade profit (notional calculation – unless a loss)
- If BLAGAB trade profit $>$ I-E \rightarrow I-E increased to level of minimum profits
 - Deemed Income receipt
 - Equal amount of E added to the E carried forward to next accounting period.



BLAGAB trade profit – excess adjusted trade profit



Excess adjusted BLAGAB trade profits (EAT profit)

- Used to calculate minimum profits to be brought into tax
- Add non-taxable BLAGAB distributions to I-E for comparison
- The excess is treated as an I-E receipt
- Management expenses equal to the excess are carried forward to following period.



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BLAGAB trade profit – excess adjusted profits example

	BTP > I-E		I-E > BTP	
	Adjustment		No adjustment	
	£	£	£	£
Adjusted BLAGAB trade profit				
BLAGAB trade profit		10,884		4,884
Adjusted in respect of losses		(1,000)		(1,000)
Adjusted BLAGAB trade profit (clause 93)		9,884		3,884
Calculation of the adjusted I-E profit				
<i>BLAGABI</i>				
BLAGAB income and gains	6,500		6,500	
BLAGAB non-taxable distributions	600		600	
	7,100		7,100	
<i>Less: BLAGAB E</i>				
Expenses deduction	(60)		(60)	
Adjusted I-E profit		7,040		7,040
Excess adjusted BLAGAB trade profit – clause 93		2,844		nil



BLAGAB trade losses – use

How can losses be used?

Clause 123

- Offset sideways
- Carry back 1 year

Clause 124

- Carry forward for proposes of
 - Minimum profits test, and
 - Policyholders tax rate

Clause 125

- Group relieve

Clause 127

- No relief against policyholder share of I-E

Losses available for group relief or s37 purposes Clause 126 restriction

BLAGAB trade loss for period	100
Less:	
Non trading deficits on BLAGAB loan relationships and derivatives	(20)
Loss available for surrender	80

Consequences of using a BLAGAB trade loss

- Deduct an amount equal to the loss used from BLAGAB management expenses



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