Budget 2011 – Consultation on changes to Life Assurance taxation

Alongside the normal budget announcements made in March, the Chancellor made some key statements on changes to the life assurance taxation regime to be made on the introduction of Solvency II. These were set out in a Technical Note, supplemented by a consultation document issued in April 2011 on which comments are requested by 28 June 2011.

Key aspects of the proposals are set out below, but there is a lot more detail than can be set out in this short article. There will be a comprehensive and up to date session presented by the Working Party at the Life Convention in November.

Shareholder profits:- Insurers will be taxed based on trading profits in the Companies Act accounts. Actuarial models will need to accommodate projections of IFRS profits to capture the appropriate timing of tax payments that will then affect the Solvency Capital Requirement ("SCR") under the Pillar II regime. This may be complex. Transitional arrangements are expected to deal with the step change in existing taxable surplus, and to protect surplus trapped through court scheme restrictions.

Tax categories:- Gross Roll-Up business (GRB) and PHI business are to be combined, leaving just two categories – Basic Life Assurance and General Annuity Business (BLAGAB) taxed on I-E and a new category that we will refer to as Trade Profits Business which covers all other business. This may allow future GRB losses in proprietary companies to obtain immediate relief and reduces one motivation for writing GRB business in a subsidiary.

"I-E" regime:- The regime will be maintained but life assurance protection business issued after 1 January 2013 will be excluded and taxed on a Trade Profits Business basis. Existing life assurance protection business will continue to fall within the I-E regime. This change is expected to result in a reduction in profits as a result of the loss of expense synergy, or an increase in premium rates for new life protection business.

Apportionments:- Rather than the current formulaic and inconsistent apportionment bases, income and gains could be allocated on an actual basis based on the insurers own internal hypothecation of assets – an approach put forward by the Tax Working Party. This would be a welcome development to reduce the risks of unexpected profit/losses or other distortions that might otherwise need to be overcome through restructuring.

Further details on the consultation paper can be found under a search for "Life Insurance Companies: A New Corporate Tax Regime" on www.hmrc.gov.uk. A series of open meetings is taking place between April and July, arrangements for which are set out in the paper. The Tax Working Party together with the profession will be responding to the consultation.

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