Written evidence submitted by the Chartered Institute of Taxation (FB11)

Representation to Finance Bill 2020 Public Bill Committee

Clause 36
Top Slicing Relief

Executive Summary

A welcome legislative clarification following a tribunal decision in favour of the taxpayer in relation to life insurance policy 'gains' – but how are gains before 11 March 2020 to be treated?

1 Overview

1.1 Top Slicing Relief (TSR) is a relief for policyholders of certain life assurance products (typically a single premium investment bond) who become subject to income tax when the policyholder receives an amount in excess of the premiums paid on the maturity, assignment (transfer of ownership) or on the surrender/ part surrender (cashing in the bond or part of it before the term has ended) of the policy. The 'gain' realised is chargeable to income tax, save that income tax at the basic rate is treated as having been paid already in the case of UK policies. A one-off gain that has built up over the life of the policy often results in the policyholder's income being pushed into the higher or additional rate band. TSR operates broadly by dividing the 'gain' on the policy by the number of years the policy has been held. That amount is treated as the top slice of income to determine the income tax rate that is then applied to the full 'gain'.

1.2 Clause 36 follows a First-tier Tribunal decision (*Silver v HMRC*[1]). The question at issue was whether the taxpayer was entitled to the personal allowance in the hypothetical calculation for TSR even though the level of her actual income meant that she was not actually entitled to the personal allowance. The clause provides for the personal allowance to be reinstated within the calculation for TSR in accordance with the decision in favour of the taxpayer in that case. The amendments are estimated to affect about 2,000 taxpayers annually.

1.3 The clause is helpful in providing clarification on the way TSR is intended to operate. However, given that the amendments are in accordance with the original policy intent, it is not clear why i) the amendments are not extended to years prior to 2019/20 (see section 2 below) and ii) why the benefit of the amendment is disapplied by an exception in the draft legislation even for 2019/20 or 2020/21 in certain circumstances (see section 3 below) but an HMRC concession may operate to override the draft legislation.

1.4 The amendments also clarify the order of the treatment of 'reliefs and allowances' within the TSR calculation. It is important that the 'personal savings allowance' is treated correctly, that is as a rate band not as an allowance. The term 'allowance' is a misnomer (See paragraph 4).

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[1] *Silver v HMRC [*2019] UKFTT 0263 (TC)

2 Application to earlier years

2.1 The amendments made by clause 36 have effect, with some restrictions (see paragraph 3 below) from the tax year 2019/20. It is not clear why the amendments, which are clarificatory in nature and in accordance with the original policy intent, should not be extended to years prior to 2019/20 to provide the same clarity for taxpayers in respect of earlier gains. Until these amendments, both HMRC self-assessment tax return software and commercial tax return software used HMRC's previous application of the rules for top-slicing relief. For most taxpayers it is likely to be beneficial to apply the same approach as clause 36 instead of the basis on which they submitted their tax returns for earlier years using the software at the time.

2.2 However, as clause 36 is not retrospective, an individual who is liable to tax in respect of gains from chargeable events before 2019/20 and who wishes to reinstate the personal allowance within the calculation for TSR will instead need to rely on the basis agreed in *Silver v HMRC*. Decisions of the First-tier Tribunal do not create a legally binding precedent. It is therefore not clear whether or not HMRC will accept claims for repayment from taxpayers with gains in years prior to 2019/20.

2.3 The fact that the amendments apply the changes only from 2019/20 is in contrast to the approach taken by Finance Bill clauses 100 (HMRC: exercise of officer functions) and 101 (Returns relating to LLP not carrying on business etc with view to profit). These clauses also put beyond doubt that the relevant rules work as designed and intended but apply both prospectively and retrospectively. (It may be relevant that the changes made by those clauses benefit the tax authority rather than the taxpayer.) As clause 36 is similarly clarificatory in nature, it seems that, by the same principle, clause 36 should apply also to pre-2019/20 gains.

2.4 It is recognised there may be a small number of cases where applying clause 36 retrospectively would give rise to an increased tax liability for taxpayers. A transitional rule could permit taxpayers in this position to elect out of the new rules.

3 Application of the amendments to the tax year 2019/20

3.1 The policy paper[2] accompanying this measure says 'The measure will have effect for all relevant gains occurring **on or after announcement at Budget 2020 [11 March 2020].**' However, clause 36 does apply to some pre-11 March 2020 gains and in doing so appears to create an anomaly. If an individual realises gains from chargeable events that occur both before 11 March 2020 *and* later in 2019/20, the measure will strictly apply to all those gains for 2019/20 including the pre-11 March gain falling within 2019/20. For example, suppose Fred has just one policy gain in 2019/20, in January 2020. His brother Tom has two policy gains in 2019/20: one in January 2020 and one on 23 March 2020. Seemingly, based on the draft legislation, Fred would not benefit from the amendments, but Tom would.

3.2 We understand that HMRC will in practice apply the changes to all gains arising in 2019/20 onwards. While this approach removes the Fred/Tom anomaly above, it is contrary to the draft legislation and raises the question of whether this concessionary approach is within HMRC's care and management powers. It seems unusual to introduce an extra statutory

[2] https://www.gov.uk/government/publications/changes-to-top-slicing-relief-on-life-insurance-policy-gains-from-11-march-2020/changes-to-top-slicing-relief-on-life-insurance-policy-gains-from-11-march-2020

concession to relieve a strict legislative position where the legislation has not yet been passed into law.

4 Reliefs and allowances

4.1 Clause 36 specifies how 'reliefs and allowances' are set against life assurance policy gains. The personal savings allowance does not operate as a typical allowance. It is a nil rate band of tax that does not extend the basic or higher rate bands. The draft legislation should specify that the personal savings allowance is not an allowance for this or any other purpose. The term 'allowance' is an unhelpful misnomer.

5 The Chartered Institute of Taxation

5.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT's comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

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The Chartered Institute of Taxation
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