

FINANCE ACT 2012

EXPLANATORY NOTES

INTRODUCTION

Sections 55 to 179 Schedules 16 to 19: Solvency II and the Taxation of Life Insurance Companies

Details of the Sections

Part 2

Chapter 1

2. Chapter 1 contains sections 55 to 65 which explain the structure of this Part of the Act and define terms used in the legislation.
3. Section 56 defines “life assurance business”, and section 57 defines “basic life assurance and general annuity business” (BLAGAB), which excludes “protection business”, among other items. Sections 58 to 62 define terms used in section 57.

Chapter 2

4. Chapter 2 sets out the charge to tax on BLAGAB business, which is taxed on an I - E basis.
5. Section 66 explains that BLAGAB, non-BLAGAB long-term business and general insurance are to be treated as separate businesses.
6. Section 67 provides an exception to the separate trade treatment for BLAGAB when substantially all of the long-term business is not BLAGAB.
7. Section 68 imposes the charge to corporation tax on the I - E profit for BLAGAB; the “I - E profit” is explained in section 73.
8. Section 69 gives precedence to the I - E charge over the general charge to corporation tax on trade profits under section 35 of the Corporation Tax Act (CTA) 2009.
9. Section 70 explains what is meant by “the I - E rules”.
10. Section 71 applies the general corporation tax charge on trade profits to profits of non-BLAGAB long-term business, subject to Chapter 6 of the legislation and specific rules for transfers of non-BLAGAB long-term business.
11. Section 72 excludes companies carrying on only Permanent Health Insurance (PHI) business from Part 2 of the legislation and from provisions elsewhere in the Corporation Tax Acts which make special provision for long-term business carried on by insurance companies.

Chapter 3

12. Chapter 3 explains the I - E basis.

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13. Section 73 sets out the steps used to calculate the I – E profit (where the result is a positive amount) or the excess BLAGAB expenses (where the result is a negative amount). It points to other sections where specific terms are explained.
14. Section 74 lists items that come within the definition of income in step 1 of section 73.
15. Section 75 explains how to calculate the BLAGAB chargeable gains for the purposes of step 2 of section 73.
16. Section 76 explains how to calculate the BLAGAB management expenses for the purposes of step 5 of section 73.
17. Sections 77 and 78 define some of the terms used in the calculation of BLAGAB management expenses in section 76.
18. Section 79 sets out special rules for acquisition expenses (which are defined in section 80). These are expenses that are payable for the purpose of the acquisition of new business. They are spread over 7 years rather than deducted in full when incurred.
19. Section 81 details some specific amounts that are allowable as BLAGAB management expenses.
20. Section 82 applies certain restrictions, which apply to the management expenses of a company with investment business, to the calculation of BLAGAB management expenses.
21. Sections 83 and 85 bring into the new regime the existing provisions allowing relief, in computing I - E profits, for certain annuity payments.
22. Section 86 modifies, for I – E purposes, the rules in CTA 2009 regarding the taxation of profits from property businesses. It provides that a life insurance company may have more than one property business. There is a separate property business in respect of property held other than for the purposes of the long-term business. Separate businesses are established for property matched to BLAGAB liabilities; for property matched to other long-term liabilities; and for unmatched property held for the purposes of the long term business.
23. Section 87 sets out the treatment, for I – E purposes, of losses from property businesses. To the extent that they are referable to BLAGAB, such losses are to be treated as BLAGAB management expenses.
24. Section 88 ensures that for the purposes of the I – E profit calculation the rules on loan relationships, derivative contracts and intangible fixed assets apply as though the BLAGAB business were not a trade. The relevant rules in CTA 2009 apply accordingly.
25. Section 89 provides for certain BLAGAB miscellaneous income to be treated as I – E receipts in so far as it exceeds miscellaneous losses.
26. Sections 90 and 91 replicate existing provisions which impute investment return for I – E purposes when certain risks under BLAGAB contracts of insurance are reinsured.
27. Section 92 deems certain BLAGAB trading receipts, which would not otherwise fall within the charge to corporation tax, to be I – E receipts.
28. Section 93 requires a comparison between the BLAGAB trade profit and the I - E result and imputes an additional I - E receipt if the former is greater than the latter.
29. Section 94 requires that, in making the comparison in section 93, any exempt dividends referable to BLAGAB are to be included as I - E receipts. This is because all dividends are taken into account when computing the BLAGAB trade profit.

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30. Section 95 allows non-BLAGAB allowable losses to be deducted from the shareholders' share of BLAGAB chargeable gains, but not to the extent that they would create an I - E loss.
31. Section 96 restricts management expenses of an overseas life insurance company carrying on BLAGAB business in the UK where the income of the company allocated to BLAGAB includes FOTRA (free of tax to residents abroad) profits.

Chapter 4

32. Section 97 introduces Chapter 4, which contains rules for the allocation to BLAGAB of investment income and losses, expenses, and chargeable gains and allowable losses for the purposes of I – E.
33. Section 98 requires that investment income or losses, and expenses referable to BLAGAB are to be determined by an acceptable commercial method. It explains what is an acceptable commercial method. HM Treasury is given a power to make regulations prescribing what is, or is not, an acceptable commercial method.
34. Sections 99 to 101 explain how chargeable gains and allowable losses referable to BLAGAB are determined.
35. Section 100 provides that gains or losses on assets are attributable to BLAGAB to the extent that the assets are wholly or partly matched to BLAGAB liabilities. The concept of matching is explained in section 138.
36. Section 101 explains that the extent to which gains or losses on assets, which are not matched to BLAGAB liabilities, are referable to BLAGAB is determined using an acceptable commercial method. The section applies to the unmatched proportion of a gain or loss where the asset is partly matched. It explains what is an acceptable commercial method, and gives HM Treasury a power to make regulations prescribing what is, or is not, an acceptable commercial method.

Chapter 5

37. Chapter 5 sets out the rate of tax to be applied to the policyholders' share of the I–E profit and sets out how that share is to be determined.
38. Section 102 defines the rate of tax applicable to the policyholders' share of the I – E profit as the basic rate for income tax.
39. Section 103 sets out how the policyholders' share of the I – E profit is to be determined. For mutual insurance companies, the whole of the profit is attributable to policyholders.
40. Sections 104 and 105 explain terms used in sections 103 and 104.
41. Section 106 provides for a deduction in the calculation of the BLAGAB trade profits for tax of the accounting period charged at the policyholder rate.
42. Section 107 provides for an adjustment to BLAGAB trade profits in respect of deferred policyholder tax, and explains how it is to be calculated.
43. Section 108 defines terms used in section 107 and specifies the BLAGAB assets and liabilities in respect of which an adjustment may arise under that section. HM Treasury is given a power to amend by regulation the list of BLAGAB assets and liabilities.

Chapter 6

44. Section 109 applies the rules in Chapter 6 to the calculation of BLAGAB trade profit or loss and the non-BLAGAB long-term business profit.
45. Section 110 allows a deduction in calculating profits for sums allocated to policyholders except where certain sums of a capital nature are allocated to with-profits policyholders.

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46. Section 111 brings dividends and other company distributions into account as receipts in calculating the profits unless they are capital distributions. This section overrides the general rule that such dividends and distributions are not taxable.
47. Section 112 disapplies the provisions in CTA 2009 which exempt the indexation return on index-linked gilt-edged securities (gilts) from tax under the loan relationship rules in computing trade profits. But the section does not apply where the gilts are held to back index-linked PHI liabilities to policyholders.
48. Section 113 excludes profits, receipts and expenses arising from long-term business fixed capital assets from the computation of profits.

Chapter 7

49. Section 114 explains that Chapter 7 details how to allocate accounting profits, losses and various adjustments between BLAGAB and non-BLAGAB long-term business.
50. Section 115 requires that the allocation is to be in accordance with an acceptable commercial method. The method must be consistent with the method used for the purposes of section 41 (allocation of BLAGAB income, etc). The section also gives HM Treasury the power to prescribe cases in which a method is to be, or is not to be, regarded as an acceptable commercial method.

Chapter 8

51. Chapter 8 deals with changes in the allocation of assets and share pooling rules for life insurance business.
52. Section 116 deems a disposal and reacquisition at fair value when an asset moves between the categories set out in the section. This rule does not apply where none of the profits of a company are taxed on an I - E basis.
53. Section 117 modifies the rules in section 116 for overseas life insurance companies.
54. Section 118 sets out the rules where there is a transfer of business and as a consequence assets transferred move from one category to another.
55. Sections 119 and 120 adapt the capital gains share pooling rules for life insurance companies, including overseas life insurance companies.

Chapter 9

56. Chapter 9 explains how relief is provided for BLAGAB trade losses.
57. Section 123 applies the general trade loss rules in CTA 2009 to BLAGAB trade losses.
58. Section 124 describes how a BLAGAB trade loss may be carried forward to later accounting periods.
59. Section 125 explains the application of group relief rules to BLAGAB trade losses.
60. Section 126 says that losses relieved by way of section 123 or section 125 are to be reduced by the amount of any non-trading loan relationship deficit for the accounting period.
61. Section 127 prevents various reliefs (as identified in section 127(3)) from being set against the policyholders' share of the I – E profit.

Chapter 10

62. Chapter 10 contains the rules on transfers of long-term business.

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63. Where there is a transfer of BLAGAB business, Section 128 permits the transferee to receive relief for spread acquisition expenses (see section 79) which would have become available to the transferor in a period after the transfer if the transfer had not taken place.
64. Section 129 sets out the rules for the calculation of BLAGAB trade profits of the transferor and the transferee where there is a transfer of BLAGAB business within a group or from a mutual company to a non-mutual company.
65. Section 130 provides that, when there has been a transfer of business between unconnected parties on or after 1 January 2013, the transferee will get relief for the amortisation of an asset recognising the value of future profits arising from the business acquired when that amortisation is charged to the accounts .
66. Section 131 applies sections 129 and 130 where there is a transfer of non-BLAGAB long-term business.
67. Section 132 is an anti-avoidance provision, which applies where, on or after 1 January 2013, there is a transfer of long-term business (or part of a business) and the main purpose of a company entering into one or more of the arrangements is an unallowable purpose. Where it applies, the section requires necessary steps to be taken to negate the tax advantage arising.
68. Sections 133 and 134 set out the clearance procedure by which a company can seek confirmation from HMRC that section 132 does not apply.
69. Section 135 states that whether companies are members of the same group for the purposes of Chapter 10 is to be determined in accordance with section 170(2) to (11) of the Taxation of Chargeable Gains Act 1992.

Chapter 11

70. Chapter 11 contains definitions of terms and abbreviations used in this Part.
71. Section 138 explains the concept of matching of assets (or part assets) to liabilities, which is used in Chapter 4 and Chapter 8 of this Part.

Chapter 12

72. Section 142 gives HM Treasury powers to amend the legislation relating to life assurance business by way of secondary legislation in consequence of powers being exercised under the Financial Services and Markets Act 2000 (FSMA 2000).
73. Section 143 allows the meaning of the term “insurance business transfer scheme” to be amended by order following any change to section 105 FSMA 2000.
74. Section 144 provides a power to modify by regulations the legislation relating to overseas life insurance companies.
75. Sections 146 and 147 introduce Schedules 16 and 17, which contain minor and consequential amendments and transitional provisions respectively.
76. Section 148 states that the provisions of this Part are to have effect for accounting periods beginning on or after 1 January 2013.
77. Section 149 ensures that all life insurance companies will have an accounting period ending on 31 December 2012.