2003 No. 2573

INCOME TAX

The Insurance Companies (Taxation of Reinsurance Business) (Amendment No. 2) Regulations 2003

Made - - - - - - - -	*7th October 2003*
Laid before the House of Commons	*7th October 2003*
Coming into force - - - - -	*28th October 2003*

The Commissioners of Inland Revenue, in exercise of the powers conferred upon them by sections 431C(1) and 442A(2) to (6) of the Income and Corporation Taxes Act 1988(**a**) and paragraph 58 of Schedule 8 to the Finance Act 1995, make the following Regulations:

Citation, commencement and effect

1.—(1) These Regulations may be cited as the Insurance Companies (Taxation of Reinsurance Business) (Amendment No. 2) Regulations 2003 and shall come into force on 28th October 2003.

(2) Regulations 3(a) and (b), 9 to 11 and 12(3) have effect in relation to periods of account beginning on or after 1st November 2003.

(3) Regulations 3(c) and 4 to 8 have effect in relation to periods of account beginning on or after 1st January 2001.

(4) Regulation 12(2) has effect in relation to transfers of reinsurance arrangements taking place on or after 1st January 2003.

Amendments to the Insurance Companies (Taxation of Reinsurance Business) Regulations 1995

2. The Insurance Companies (Taxation of Reinsurance Business) Regulations 1995(**b**) are amended as follows.

Amendments to regulation 2

3. Amend regulation 2 (interpretation) as follows—

(a) after the definition of "EEA State" insert—

> ""expense risk" means the risk that the amount of expenses attributable to a policy or contract over its duration is greater than the amount expected by the cedant company when it entered into the policy or contract;",

(**a**) 1988 c. 1. Section 431C was inserted by paragraph 2, and section 442A by paragraph 34, of Schedule 8 to the Finance Act 1995 (c. 4). Section 442A was amended by paragraph 23 of Schedule 33, and Part 3(12) of Schedule 43, to the Finance Act 2003 (c. 14).

(**b**) S.I. 1995/1730, relevantly amended by S.I. 1996/1621 and S.I. 2003/1828.

(b) after the definition of “inspector” insert—

““insurance business transfer scheme” has the meaning given by section 431(2) of the Taxes Act(**a**);”, and

(c) after the definition of “policy” insert—

““the Prudential Sourcebook (Insurers)” has the meaning given by section 431(2) of the Taxes Act(**b**);”.

Amendments to regulation 4

4. Amend regulation 4 (calculation of investment return in first accounting period) as follows—

(a) in the definition of P after “otherwise” insert “(but excluding any such sums paid in repayment of a loan or otherwise diminishing a debt such as is mentioned in paragraph 12(4)(a)(ii) of Appendix 9.4 of the Prudential Sourcebook (Insurers))”,

(b) in the definition of C after “otherwise” insert “(but excluding any such sums paid by way of a loan or otherwise creating a debt such as is mentioned in paragraph 12(4)(a)(i) of Appendix 9.4 of the Prudential Sourcebook (Insurers))”, and

(c) for “the result is less than zero” substitute “C is greater than P”.

Amendments to regulation 5

5. Amend regulation 5(1) (calculation of investment return in second and subsequent accounting periods other than final accounting period)(**c**) as follows—

(a) in the definition of P_n after “otherwise” insert “(but excluding any such sums paid in repayment of a loan or otherwise diminishing a debt such as is mentioned in paragraph 12(4)(a)(ii) of Appendix 9.4 of the Prudential Sourcebook (Insurers))”,

(b) in the definition of C_n after “otherwise” insert “(but excluding any such sums paid by way of a loan or otherwise creating a debt such as is mentioned in paragraph 12(4)(a)(i) of Appendix 9.4 of the Prudential Sourcebook (Insurers))”, and

(c) for “the result” substitute “$((P_n - C_n) + I_{n-1})$”.

Amendments to regulation 6

6.—(1) Amend regulation 6 (calculation of investment return in final accounting period) as follows.

(2) In paragraph (1) after “investment returns” insert “treated as accruing”.

(3) After paragraph (3) add—

“(4) For the purposes of paragraph (1) above, the aggregate of the amounts of the investment returns treated as accruing in earlier accounting periods are the amounts treated as accruing in those accounting periods but—

(a) prior to any setting off permitted by regulation 7A(2)(c), calculated in accordance with regulations 4 and 5 as if in regulation 7(7) the formula were—

$$\frac{(X \times 100)}{Y} \text{ ; and}$$

(b) in any case falling within paragraph (10)(b)(iii) of regulation 7, adjusted by such an amount as the inspector determines to be just and reasonable in the circumstances after taking into account the factor specified in paragraph (12)(d) of that regulation.”.

(**a**) The reference is to section 431(2) of the Income and Corporation Taxes Act 1988 which was relevantly amended by article 26(3) and (8) of S.I. 2001/3629.

(**b**) The Prudential Sourcebook (Insurers) is defined by section 431(2) as the Interim Prudential Sourcebook for Insurers made by the Financial Services Authority (“the FSA”) under the Financial Services and Markets Act 2000 (c. 8). This sourcebook is part of the FSA Handbook. The FSA Handbook may be purchased on paper from the Publications Department (Sales), Financial Services Authority, 25 The North Colonnade, Canary Wharf, London E14 5HS and is available on line at www.fsa.gov.uk.

(**c**) Regulation 5(1) was amended by regulation 4(a) of S.I. 1996/1621.

Amendments to regulation 7

7.—(1) Amend regulation 7 (prescribed percentage rates of return for the purposes of regulations 4 and 5) as follows.

(2) In paragraphs (2) and (4) omit "but where the result is less than zero, taking the rate to be zero".

(3) In paragraph (7)—

(a) for the formula substitute—

$$\text{“}\frac{(X \times 100)}{Y} \times \textit{the Relevant Fraction}\text{”} \text{, and}$$

(b) omit "but where the result is less than zero, taking the rate to be zero".

(4) After paragraph (7) insert—

"(7A) For the purposes of paragraph (7) above, *the Relevant Fraction* is—

(a) in a case where, in finding X, the amount of investment income is increased by the amount of an increase in the value of the assets mentioned in sub-paragraphs (a) and (b) of that paragraph—

$$\frac{X - X1}{X} \;;$$

(b) in a case where, in finding X, the amount of investment income is decreased by the amount of a reduction in the value of those assets and, after being so decreased, is not less than zero—

$$\frac{(X2 - X1)}{X2} \;\text{; or}$$

(c) in a case where X is an amount that is less than zero—

$$0.5 + \frac{X1}{X2} \;;$$

where—

X is the same as for the purposes of that paragraph;

X1 is the amount included in the amount of investment income used in finding X which represents dividends and other distributions that are not chargeable to corporation tax by virtue of section 208 of the Taxes Act (which provides that dividends and other distributions of a company resident in the United Kingdom are not generally so chargeable); and

$X2$ is the amount of investment income before it is decreased by the amount of any reduction in the value of the assets mentioned in sub-paragraphs (a) and (b) of that paragraph.".

(5) For paragraph (10)(a) substitute—

"(a) the rate found by expressing the amount of the expected income from non-linked assets for the accounting period concerned as a percentage of the value of the total non-linked assets (other than assets not providing income) as identified in the relevant part of the periodical return of the cedant company specified in paragraph (11) below; or".

(6) After paragraph (12)(c) add ";

(d) the extent to which the reinsurer is in receipt of dividends and other distributions which—

(i) arise from assets held by the reinsurer which may reasonably be regarded as related to the reinsurance arrangement in question; and

(ii) are not chargeable to corporation tax by virtue of section 208 of the Taxes Act.".

(7) In paragraph (13) after "under" insert "regulation 6(4)(b) or".

New regulation 7A

8.—(1) After regulation 7 insert—

"**Treatment of amounts of investment return which are less than zero**

7A.—(1) This regulation applies where the amount of investment return on a policy or contract, as calculated in accordance with regulation 3, 4 or 5, is less than zero ("the negative amount").

(2) The negative amount may be set off in the following order against the following amounts—

(a) first, the amount of any income (other than any investment return which is treated under these Regulations as accruing) which—

(i) accrues in the same accounting period as that in which the negative amount is treated as accruing; and

(ii) is referable to basic life assurance and general annuity business and is charged to tax under Case VI of Schedule D;

(b) secondly, the amount of any investment return which—

(i) is treated under these Regulations as accruing in the same accounting period as that in which the negative amount is treated as accruing; and

(ii) is more than zero; and

(c) thirdly, the amount of any investment return which is treated under these Regulations as accruing—

(i) in an accounting period subsequent to that in which the negative amount is treated as accruing; and

(ii) in respect of the same policy or contract as that in respect of which the negative amount is treated as accruing;

and is more than zero.

(3) Any setting off under paragraph (2)(c) above shall, so far as possible, reduce amounts accruing in an earlier accounting period before reducing amounts accruing in a later one.

(4) Except as is provided for by paragraph (2) above, the negative amount shall be treated for the purposes of section 396 of the Taxes Act(**a**) as if it were zero.".

Amendments to regulation 9

9.—(1) Amend regulation 9 (exclusion of certain reinsurance arrangements from section 442A) as follows.

(2) In paragraph (1) for "(4)" substitute "(4A)".

(3) For paragraph (4)(a)(i) substitute—

"(i) the mortality risk or the morbidity risk (but no other risk other than the expense risk) is being reinsured, or both the mortality risk and the morbidity risk (but no other risk other than the expense risk) are being reinsured, and".

(4) After paragraph (4) insert—

"(4A) The description prescribed by this paragraph is of any reinsurance arrangement which is not prescribed by paragraph (4) above and consists of a contract which—

(a) has the effect of increasing the amount of assets that falls to be included at line 34 of Form 9 in the periodical return of the cedant company (representing assets available to meet its required minimum margin for long-term insurance business); and

(b) includes—

(i) terms for the transfer of liabilities to policyholders from the insurer; and

(ii) a provision for the recapture of such liabilities in specified circumstances.".

(**a**) The reference is to section 396 of the Income and Corporation Taxes Act 1988 which was amended by section 99(3) of, and Part 5 of Schedule 19 to, the Finance Act 1990 (c. 29).

Amendments to regulation 11

10. In regulation 11 (exclusion of certain business from section 431C)(**a**)—

(a) omit paragraph (b), and

(b) for paragraph (d) substitute—

"(d) the business is business in relation to which an election under regulation 11A has been made.".

New regulation 11A

11. After regulation 11 insert—

"**Election for certain business to be excluded from section 431C**

11A.—(1) A company may make an election under this regulation in relation to—

(a) any period of account beginning on or after 1st November 2003; and

(b) any of its reinsurance business which is business of the kind specified in paragraph (2), (3) or (4) below.

(2) The business specified in this paragraph is business—

(a) which is of any of the descriptions specified in section 431D(1)(b) of the Taxes Act(**b**), being business for which the policy or contract concerned was made on or after 1st November 1994; and

(b) the contract for which was made before the beginning of the company's first period of account to begin on or after 1st November 2003.

(3) The business specified by this paragraph is business the contract for which—

(a) was effected by a company resident in the United Kingdom at or through a branch or agency outside the United Kingdom where none, or no significant part, of the reinsurance business carried on relates to life assurance business with policy holders or annuitants residing in the United Kingdom; and

(b) was made before 1st November 1994.

(4) The business specified by this paragraph is business the contract for which was made after the beginning of the company's first period of account to begin on or after 1st November 2003 and replaces—

(a) a contract made before the beginning of the company's first period of account to begin on or after 1st November 2003 such as is mentioned in paragraph (2) above;

(b) a contract made before 1st November 1994 such as is mentioned in paragraph (3) above; or

(c) a contract that replaced a contract such as is mentioned in sub-paragraph (a) or (b).

(5) For the purposes of paragraph (4) above, a contract replaces a contract if it results in—

(a) no significant difference in the type of business being reinsured; and

(b) no significant variation in the terms on which that business is reinsured.

(6) For the purposes of paragraph (5) above, where more than one contract replaces a contract—

(a) there is no significant difference in the type of business being reinsured if the replacement contracts, when taken together, do not result in such a difference; and

(b) there is no significant variation in the terms on which business is reinsured if the replacement contracts, when taken together, do not result in such a variation.

(7) Where there is a relevant transfer from one person ("the transferor") to another ("the transferee") and the transferor makes an election under this regulation in relation to that business, the transferee is to be treated for the purposes of these Regulations as making the election.

(**a**) Regulation 11 was amended by regulation 5 of S.I. 1996/1621 and regulation 4 of S.I. 2003/1828.

(**b**) The reference is to section 431D of the Income and Corporation Taxes Act 1988 which was inserted by paragraph 2 of Schedule 8 to the Finance Act 1995 and amended by section 108 of the Finance Act 2000 (c. 17).

(8) In paragraph (7) above, “a relevant transfer” means a transfer of reinsurance business that is effected by—

(a) novation; or

(b) an insurance business transfer scheme.

(9) A company may revoke an election under this regulation with effect for any period of account in relation to which it would have effect.

(10) A revocation under paragraph (9) above must be in respect of all elections under this regulation which a company has made or is treated as having made.”.

Amendment to regulation 13

12.—(1) Amend regulation 13 (transfers of reinsurance arrangements effected by novation or insurance business transfer schemes) as follows(**a**).

(2) After paragraph (6) insert—

“(6A) For the purposes of regulation 7A, any negative amount that is available before the transfer to be set off by the transferor in accordance with paragraph (2)(c) of that regulation shall be treated as if it had accrued in an earlier accounting period of the transferee.”.

(3) Omit paragraph (8).

Ann Chant
Helen Ghosh
7th October 2003 Two of the Commissioners of Inland Revenue

(**a**) Regulation 13 was added by regulation 5 of S.I. 2003/1828.

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations amend the Insurance Companies (Taxation of Reinsurance Business) Regulations 1995 (S.I. 1995/1730) ("the principal Regulations"). The principal Regulations make provision for the purposes of section 442A of the Income and Corporation Taxes Act 1988 (c. 1) ("the Taxes Act") in relation to the calculation of the investment return on an insurance policy or annuity contract which is the subject of a reinsurance arrangement.

Regulation 1 provides for citation, commencement and effect. Authority for the retrospective effect of certain of the amendments is given by paragraph 58 of Schedule 8 to the Finance Act 1995 (c. 4).

Regulation 2 introduces the amendments to the principal Regulations.

Regulation 3 amends regulation 2 (interpretation).

Regulations 4 and 5 amend regulations 4 (calculation of investment return in first accounting period) and 5 (calculation of investment return in second and subsequent accounting periods other than final accounting period) respectively, in particular so as to allow the investment return to be less than zero in certain circumstances.

Regulation 6 amends regulation 6 (calculation of investment return in final accounting period) so as to modify the way in which the investment return in earlier accounting periods is calculated for the purposes of calculating the investment return in the final accounting period.

Regulation 7 amends regulation 7 (prescribed percentage rates of return for the purposes of regulations 4 and 5). The amendments allow the investment return to be less than zero. They also change the method of calculation so as to take account of the fact that the investment return may consist wholly or partly of dividends and other distributions of companies resident in the United Kingdom (which, if received directly by the cedant company, would be exempt from corporation tax).

Regulation 8 inserts a new regulation 7A (treatment of amounts of investment return which are less than zero).

Regulation 9 amends regulation 9 (exclusion of certain reinsurance arrangements from section 442A) so as to extend the types of reinsurance arrangement that are excluded from the operation of section 442A of the Taxes Act.

Regulation 10 amends regulation 11 (exclusion of certain business from section 431C) so that reinsurance business which is overseas life assurance business is no longer excluded from section 431C of the Taxes Act save where there is an election under new regulation 11A (election for certain business to be excluded from section 431C) in relation to it.

Regulation 11 inserts new regulation 11A.

Regulation 12 makes consequential amendments to regulation 13 (transfers of reinsurance arrangements effected by novation or insurance business transfer schemes).

STATUTORY INSTRUMENTS

2003 No. 2573

INCOME TAX

The Insurance Companies (Taxation of Reinsurance Business) (Amendment No. 2) Regulations 2003

£2.00

Printed and published in the UK by The Stationery Office Limited
under the authority and superintendence of Carol Tullo, Controller of
Her Majesty's Stationery Office and Queen's Printer of Acts of Parliament.
E1420 10/2003 131420 19585

ISBN 0-11-047961-0