These notes refer to the Finance Act 2010 (c.13) which received Royal Assent on 8 April 2010

FINANCE ACT 2010

EXPLANATORY NOTES

INTRODUCTION

Section 47: Apportionment of Asset Value Increases

Summary

1. Section 47 amends the operation of the apportionment provisions of section 432C of the Income and Corporation Taxes Act 1988 (ICTA) in certain specific circumstances. Where the section applies, the apportionment of the increase in the value of non-linked assets brought into account to a particular category of life insurance business is modified.

Details of the Section

2. Subsection (1) inserts new section 432CA into Chapter 1 of Part 12 of ICTA.

3. New section 432CA(1) provides that the provisions apply when, for a period of account:

   a) a company is not a non-profit company or has elected to be treated as a non-profit company;

   b) an amount is brought into account in a revenue account as an increase in the value of non-linked assets;

   c) section 432C of ICTA applies to determine the extent to which the amount brought into account is referable to life assurance business or gross roll-up business; and

   d) the amount in line 51 of Form 14 of the company's periodical return is less than the amount shown for the previous period of account.

4. When the provisions of new section 432CA apply, the difference between the amount in line 51 of Form 14 for the current period and the amount at line 51 of Form 14 for the previous period of account is identified. The lesser of that amount and the "relevant brought into account amount" for the current period of account is, for the purposes of applying section 432C of ICTA only, not treated as brought into account in the current period of account but is instead treated as if it had been brought into account in an earlier period of account or periods of account. This amount is the "affected amount".

5. New section 432CA(2) sets out that the "relevant brought into account amount" is the total of the amount brought into account as an increase in value of non-linked assets, amounts deemed to be brought into account as an increase in the value of non-linked assets by virtue of section 83(2B) of the Finance Act (FA) 1989 and amounts taken into account under section 83(2) of FA 1989 by virtue of section 444AB of ICTA.

6. The rules which determine the period(s) of account for which the "affected" amount is treated as being brought into account, for the purposes of applying section 432C of ICTA only, are in new section 432CA(4) to (10).

7. New section 432CA(5) identifies the periods of account in which the affected amount may be treated as being brought into account ("the appropriate periods of account") as

those in which there has been an increase in line 51 of Form 14 for the period when compared with the same figure for the previous period of account. The amount of that increase is the "relevant increase".

8. The "affected amount" is first allocated to the most recent appropriate period of account. Any excess of the "affected amount" over the relevant increase for that most recent period of account is then allocated to the next most recent appropriate period of account and so on.

9. Subsection (2) of the section provides for new section 432CA to have effect for accounting periods beginning on or after 9 December 2009.

10. Subsection (3) restricts the identification of appropriate periods of account to those which began on or after 9 December 2009.

11. If after allocation to the appropriate periods of account some or all of the "affected amount" has not been allocated to a period of account, subsection (4) specifies that the unallocated "affected amount" is treated as brought into account as an increase in value of the latest period of account beginning before 9 December 2009.

Background Note

12. The income and gains of a company's life insurance business are taxed as they are brought into account in the company's regulatory return to the Financial Services Authority (FSA). FSA rules allow companies to defer recognition of income and gains and this deferral is effective for tax purposes.

13. When income and gains are recognised they are apportioned between categories of business on the basis of the mix of business liabilities at the time when the profits are recognised not when they accrued. In a recent case, a company recognised a substantial amount of deferred income and gains, accrued in a period where the business was substantially life insurance business, in a period of account where there were no net life insurance business liabilities. This manipulation could have the effect of eliminating the tax due on these profits, particularly where non-profit funds were concerned.

14. On 15 July 2009 Written Ministerial Statements were laid before Parliament announcing an intention, following industry consultation, to legislate to prevent the manipulation of the liabilities in a non-profit fund in order to avoid tax when previously unrecognised profits are recognised.

15. Following the Written Ministerial Statements, HM Revenue & Customs consulted widely with industry representative bodies and all those insurance companies that would be affected by a change of legislation. That consultation continued after draft clauses were published at the 2009 Pre-Budget Report and the legislation is the fruit of that consultation.