TIME APPORTIONMENT RELIEF AND TOP-SLICING RELIEF

FOR FINANCIAL ADVISERS ONLY

The aim of this document is to provide an overview of the changes to time apportionment relief (TAR) and top-slicing relief for offshore bonds, due to the implementation of the Finance Act 2013.

This explains how the new TAR rules can impact upon top-slicing relief and the effect that this can have on bonds already in force, prior to this legislation change.

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TIME APPORTIONMENT RELIEF

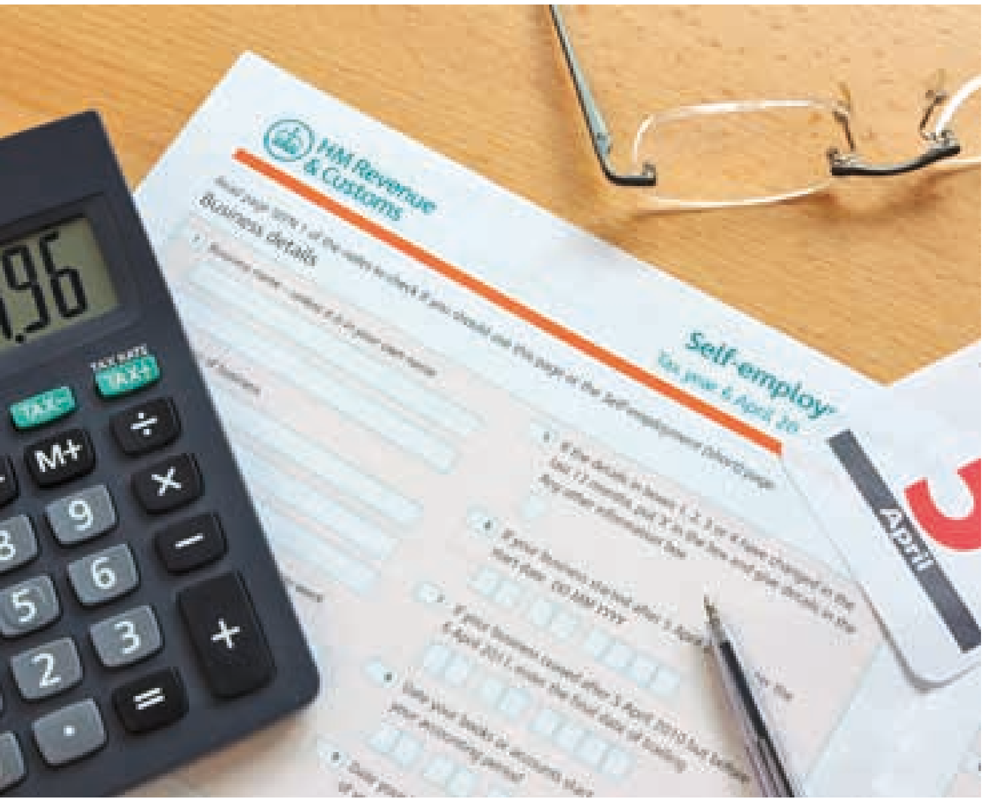
Background

Time apportionment relief is used to reduce a UK chargeable gain. It allows the chargeable gain to be proportionately reduced by the amount of time the policyholder has been resident outside the UK, during the term of the bond.

For policies issued on or after 6 April 2013

As a result of the Finance Act 2013, time apportionment relief (TAR) for bonds issued on or after 6 April 2013, is now defined as 'a reduction in the chargeable gain on an offshore bond, **if the person liable to UK income tax was not UK resident** throughout the life of the Bond.'

Therefore, where there have been previous bond owners (with the exception of gifts between spouses and civil partners who live together), only the residence history of the person liable to the tax can now be claimed.



For policies issued prior to 6 April 2013

The TAR rule which applies to bonds issued prior to 6 April 2013 that have not been topped up or been assigned since this date (including security assignments), is 'TAR is available for the bond holder, **for any period the bond has been held by a non-UK resident individual since the bond started**.'

So, if for example, a bond had been assigned prior to 6 April 2013, from a non-UK resident individual to a UK resident individual, the assignee could benefit from the original owners period of non-UK residence.

When TAR doesn't apply

TAR is only available to individuals and cannot be claimed if the policy has ever been owned by a non-UK resident trustee.

Also, this does not apply to offshore bonds issued as life assurance policies before 18 November 1983, or capital redemption policies issued prior to 23 February 1984, as a basic rate tax credit is available for these.

TAR Calculation

$$\text{Chargeable Gain} \times \frac{\text{Number of days held as a UK resident}}{\text{Number of days the policy has been in force since inception}}$$

To illustrate this, an example is as follows:

Mr & Mrs Smith invested £100,000 into an offshore bond on 3 May 2010, whilst non-UK resident.

They returned to the UK on 15 May 2017 and then surrendered the bond on 5 February 2018, for a value of £150,000. Therefore, creating a gain of £50,000 as no withdrawals were taken.

TAR will reduce the £50,000 gain as follows:

Gain of £50,000 x 266 days / 2835 days =
£4,691.35 net gain, i.e. a 90.62% reduction.

TOP-SLICING RELIEF

Background

Top-slicing relief allows individuals to potentially mitigate paying higher rate or additional rate income tax, on some or even possibly all of a chargeable gain.

Top-slicing relief is available for UK resident individuals who 'do not pay higher or additional rate income tax on other income (excluding the gain) however, when the gain is added to income, the individual becomes subject to higher or the additional rate.'

This is applied to the chargeable gain for any complete bond years the policyholder was a UK resident.

It needs to be noted that the thresholds where an individual will be subject to higher rate income tax are now different in Scotland than the rest of the UK.

However, the Finance Act 2013 brought the following changes for top-slicing **on excess events only**:

For policies issued on or after 6 April 2013
The number of top slicing years equals the number of years since the previous excess event.

However, for those UK residents who have not been UK resident throughout, TAR will apply.
This means that the number of years available for top-slicing remains the period back to the commencement, subject to the figure being reduced for periods of non-UK residence.

For policies issued prior to 6 April 2013, which not been varied since
The number of top-slicing years equals the number of years since the bond commencement.

To clarify, **an excess event is where a withdrawal/partial surrender has exceeded the 5% cumulative tax deferred withdrawal allowance** and an excess event occurs at the end of the policy year in which the monies were withdrawn.

Needless to say, if there has been no previous excess events, then irrespective of when the bond was issued, the period available for top-slicing for excess events will always be back to the commencement date of the bond.

For other chargeable events, such as surrenders, deaths and maturities, the top-slicing relief period has not changed and always goes back to the commencement date of the bond.

When top-slicing relief doesn't apply

- It's not available to assist taxpayers already liable to tax at the higher rate before the chargeable event gain is added to their income.
- It doesn't reduce income below £100,000 to preserve full entitlement to the personal allowance.
- Top-slicing is only available to individuals, therefore it cannot be claimed by trustees, executors/personal representatives, or corporate entities.
- This does not apply to annual gains that arise on 'personal portfolio bond events.'

Example 1

Mrs Williams, has a current total taxable income of £20,000 after allowances.

She invested £150,000 in an offshore bond on **5 March 2012**. On 3 April 2014, she left Wales to work in the UAE.

She then returned to Wales on the 25 November 2016 and surrenders the policy on the 10 January 2018 for £190,000, making a chargeable gain of £40,000 as no withdrawals were taken.

$$\text{Chargeable Gain of £40,000} \times \frac{1171 \text{ days}}{2138 \text{ days}}$$

= £21,908.33 net gain

Top-sliced gain

£21,908.33/2 = £10,954.16 added to the policyholder's income (the bond has been held for 2 full policy years when Mrs Williams was a UK resident).

The top-sliced gain added to her income after allowances is £30,954.16, which is within the basic rate threshold for England and Wales of £33,500 for the 2017-2018 tax year.

Therefore, the income tax payable is £21,908.33 x 20% **= £4,381.67.**

Let's also consider what would happen if Mrs Williams had a total taxable income after allowances of £30,000:

The income tax payable would be:

£3,500 (remainder of the threshold available) x 20% x 2 = £1,400

£10,954.16 - £3,500 = £7,454.16 x 40% x 2 = £5,963.33

Total Tax payable = **£7,363**

Example 2:

Mr Campbell, is a higher rate tax payer, who invested £300,000 in an offshore bond on **7 March 2011**, whilst non-UK resident.

On 30 October 2017, he returned to Northern Ireland and subsequently surrendered the bond on 10 November 2017, for £420,000.

Since the bond commenced, he had taken total withdrawals of £30,000, making a total gain of £150,000 (£420,000 + £30,000 - £300,000).

He is still a higher rate tax payer, so no top-slicing relief is available.

$$\text{Chargeable Gain of £150,000} \times \frac{\text{11 days}}{\text{2532 days}}$$

= £651.66 net gain x 40% tax = **£260.66 tax payable**.

Example 3:

Mrs Smith, who is permanently resident in England has a current total taxable income of £26,000 after allowances.

She invested £150,000 into an offshore bond on **10 April 2013**.

In the second bond year, a withdrawal of £20,000 was taken, which exceeded the 5% allowance and therefore creating an excess of £5,000 on 9 April 2015, which was declared for UK income tax purposes.

Mrs Smith then took another withdrawal of £30,000 in the fourth bond year, which created an excess of £15,000 on the 9 April 2017.

No TAR relief will apply, as there has been no period of non UK residence.

Top-sliced gain

£15,000/2 = £7,500 added to the policyholder's income (although the bond has been in force for 4 full policy years, the top-slicing relief period only goes back to the last excess event – i.e. 9 April 2015). **This reduces the period available for top-slicing from 4 years down to 2 years.**

The top-sliced gain added to her income after allowances is £33,500, which is just within the basic rate threshold for England and Wales of £33,500 for the 2017-2018 tax year.

Therefore, the income tax payable is £15,000 x 20% = **£3,000**

HMRC SELF ASSESSMENT

HMRC help sheet HS321 (Gains on foreign life insurance policies) provides further information and guidance for completing tax returns.

Gains on foreign policies are inserted into the 'Foreign' pages of the tax return referenced as the 'SA106'.

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