

Note of Meeting

Friendly Societies Consultation Group

18 July 2006

22 Kingsway

Attendees

HMRC

Jim Craig (JC)
Colin McHardy (CMH)

AFS

Graham Wilson (GW)
Graham Seymour (GS)
Paul Engers (PE)
Chris Russell (CR)
Sue Goodliffe (SG)
Graham Henderson (GH)

Apologies: Danny Berry – HMRC and Nick Morrell, Steve Jones - AFS

1. Minutes and Action Points from 22 June meeting

The minutes from the last meeting were agreed by all.

Actions completed but not covered in the points below:

GW had provided JC with Email contacts for the AFS members and communications via Email are now in place.

JC and CMH have fed back comments from the AFS committee, regarding the need for simplification on policyholder tax matters, to the appropriate policy areas.

Danny Berry is the leading contact on policyholder tax in HMRC. He will work together with Jon Prothero and Gary Coombes in HMT, who will want to consider potential changes in the context of overall savings policies.

2. AFS paper on Business Transfers

GW had circulated the AFS paper on Business Transfers and JC and CMH have got matters in hand.

JC advised that he has no real issues about the objectives.

He acknowledged the reason for smaller companies wishing to be able to transfer out blocks of business to meet solvency requirements etc. This is fine where the whole business is transferred. It is simply ring-fenced upon transfer.

In principle, there will be no major obstacles now to proposing that exempt business can be transferred to a life office, subject to agreement from HMT. The overriding objective is to allow one off tax neutral transfers for bona fide commercial reasons.

JC said that the only practical issue still to be resolved is the introduction of measures to prevent of blocks of exempt business being transferred on an ongoing basis. The AFS committee was happy with this in principle, although felt that there would be few instances of potential abuse in practice.

The next stage is to take the proposal forward and to agree the detail. The AFS committee undertook to outline the mechanics of the proposal eg tax treatment in the transferee company and appropriate measures to ensure that only one-off bona fide transfers are allowed.

CM noted that any proposal worked up by the group would need to be put to and agreed by ministers.

Action AFS committee

2. Inadvertent/Unavoidable Breach of Exempt Business Limits

This was covered in part B of Graham Wilson's paper, circulated by email on 7 July 2006.

JC said that we have a fair degree of agreement of the principles. Currently lawyers instruct or agree the assignment of policies with no knowledge of the knock on tax consequences.

JC liked the AFS's proposal of repealing Section 462(1), as a simple solution to the problem of relieving smaller societies of the burden of having to deal with loss of tax exemption. However, he has concerns that removing this Section will also remove the incentive for societies to enforce policyholder tax compliance.

SG said that she would have extended the proposal to keep policies both exempt and qualifying and that it seems very harsh that policyholders find that the policy has been rendered non-qualifying from no fault of their own. JC said that he would take this issue back to the HMRC policyholder tax area. His concern was how to find a way to protect this group of innocent policyholders without creating loopholes for others.

CR suggested that a practical solution to this would be to introduce a clause that a policyholder shall not breach the premium limits in respect of any policy issued to him together with any policies acquired by him for money or money's worth. GS felt that this would be consistent with existing legislation. JC may contact CR direct to obtain more detail. The matter will be discussed further at the next meeting.

Action JC

3. Simplified Regime for Smaller Societies

JC reported that he had done some research into some VAT "flat rate" schemes, including schemes for farmers, small businesses and cathedrals. Of particular interest is the scheme for churches and cathedrals who raise money. The main activity of these establishments is that of a place of worship, with no business motive. Money can be raised and business activity introduced through a tea room, souvenir shop, entry charges etc. The scheme had four separate bands depending on the level of "business" activities. A flat rate of VAT reclaim is then applied. In this example, the top and bottom bands worked well, but practical difficulties were faced with the middle two bands.

GW reported that a few more questionnaires had been received back from AFS members. The current results reflect that a considerable number of societies have just exempt and Holloway business. Some other societies additionally have a small amount of Case VI business.

A similar process, to the cathedral scheme, could be set up for friendly society business with a matrix of the different types of business carried on, premiums etc, giving rise to 3 to 4 types of classification (like a league of Premier plus divisions 1, 2 and 3). HMRC would have to decide where the bands were to lie. JC envisages still applying a two tier system. There were mixed feelings as to both the concept itself and how the system would work in practice.

Further consideration needs to be given to what issues present the greatest compliance burden. These may not be in line with what was expected by the authors of TCondoc or even the AFS tax committee. Some indication has been gleaned from the AFS questionnaires received back from members.

The main issues appear to be:

Loan relationship calculations:

Could these be exempt below a certain level?

CM noted that getting into areas like this would cause difficulties.

Deemed disposal calculations:

HMRC felt it may be easier to apply an exemption to this than to loan relationships as this area was more specific to the Life regime.

Case VI computations:

Do we need the floor and needs basis for friendly societies?

“Investment reserve” and “brought into account” are concepts that may be unfamiliar and misunderstood.

Are Case VI computations really necessary for smaller societies?

The impact of changes in legislation eg to the Form 58 basis can be horrendous. Could these be modified or exempted?

GS said that the societies suffering the most under the current regime are those who have a mix of both taxable and exempt business. He feels that we should aim to find a simplified method of filing for them, for example premiums plus income less claims, together with a simple profit and loss account. The result would be close enough to the FSA Return. It would be in line with trading companies and would remove the Life tax complications at very little cost to the Exchequer.

It was agreed that little progress had been made at the first meeting on this issue. JC felt that this was possibly due to having been side tracked by the phrasing in the TCondoc concentrates on the distinction between directive and non-directive societies. GW said that the AFS tax committee needs to work out the areas of difficulty before addressing how we could deal with those areas.

It was agreed that there is no certainty that we can arrive at workable solutions. The problem will be getting the mechanics to work. HMRC are not fundamentally opposed to the principle of some simplification. They need to think in terms of matching resources to revenue. A small amount of tax loss may be acceptable where there is a resource saving. However, if changes are made there will inevitably be winners and losers among the Societies.

GS felt that it is more important to have a simpler regime with which tax payers comply (yet no tax take) than to have a complex regime which is not understood or complied with (also with no tax take). Furthermore, it is important that we aim to get compliance with the spirit of the legislation in addition to the letter of the law.

Action AFS committee

AOB:

GW pointed out that friendly societies face a unique issue in the amalgamation of Case VI business. If the six into one option is pursued, we will wish to ensure that Holloway business exemption is preserved..

Agreed minutes (8/9/06)

CM noted that as well as Friendly Society specific issues, HMRC was also keen to get AFS input on the rest of the consultation. CM left it to AFS as to whether they preferred to do this through the Friendly Societies strand, via a separate meeting, through correspondence or indeed any other means which AFS preferred.

GS noted that some of the mainstream issues, like amalgamation of categories & apportionment would impact on Friendly societies, due to the presence of taxable & exempt life business, Holloway business etc.

AFS indicated that a written response to the TCondoc would likely be made by the AFS tax committee, highlighting Friendly Society issues such as the above.

4. Next Meeting

It was agreed to aim for a date towards the end of August, to be coordinated by JC and GW.

Action JC and GW

Note: meeting subsequently agreed to take place on Wednesday 6 September 2006 at 2.30pm at 100 Parliament Street.

Sue Goodliffe
31 July 2006