

# RESPONSES TO CONSULTATION EXERCISE ON REFORM OF THE ACCRUED INCOME SCHEME

## INTRODUCTION

The Accrued Income Scheme (AIS) is an anti-avoidance provision which prevents tax avoidance by individuals and trustees who buy and sell securities. The scheme is complicated and difficult to comply with easily, and there have been calls for it to be simplified. The Government decided to consult on possible ways to achieve simplification whilst maintaining defences against tax avoidance.

This report summarises the consultation replies received.

A copy of the consultation document can be found on the Inland Revenue web-site at:

<http://www.inlandrevenue.gov.uk/budget2004/ais-condoc.pdf>

## RESPONSES

1. A total of 9 substantive responses were received, although not all replied to every question asked in Paragraph 6 of the consultation document. A list of respondents is contained in **Appendix A**.

### Overview of responses

2. Respondents were all agreed that the AIS was too complex and needs reform. A number of respondents suggested that the AIS hits normal transactions not designed to avoid tax, and that it was widely ignored by both taxpayers, their advisers and within the Revenue.

3. Although varying in detail, most responses were generally strongly supportive of the suggested approach of taxing or relieving the difference between the clean and dirty price, allied to an activity based threshold for individuals.

4. A number of respondents suggested that since the AIS now only applies to individuals and trustees and with the current climate of low interest rates and lower income tax rates than at the time the AIS was introduced, the scope for tax avoidance was much reduced so that the AIS could reasonably be simply abolished.

### Detail of suggestions for reform

4. A simple **raising of the current £5,000 threshold** for individuals was not seen as a worthwhile exercise on its own, and this approach would do nothing to alleviate the complexities of the AIS. Suggestions for increasing the threshold varied from £20,000 through to £100,000.

5. There was strong support for the introduction of an **activity based threshold**, although again the calls were for the threshold to be set in the range £20,000 to £100,000. All respondents preferred on simplicity and familiarity grounds to stick with nominal value rather than transfer proceeds if such an threshold were introduced.

6. Several respondents suggested it should be made explicit that securities held in a tax-free wrapper such as an ISA should not count towards any threshold introduced.

7. Most respondents thought the approach of **taxing or relieving the difference between clean and dirty price** would be a welcome simplification and saw no major drawbacks. A minority thought this would be no simpler than the current scheme.

8. Taking charges or reliefs into Case III was seen as a welcome simplification, but some questioned why there should be a timing difference between taxing a charge at the date of the transfer but deferring relief until the next coupon date.

9. A couple of respondents suggested there should be a separate regime for trusts, including the introduction of a threshold for trustees and an equalisation of the rate at which AIS charges and reliefs are taxed.

### Other suggestions for reform

10. Alternative methods of reform suggested were:

- a) exempt securities held for a defined period – suggestions being from 18 months to two years, and
- b) bring all securities within the capital gains tax net.

## ***Revenue response***

*These suggestions were mentioned at paragraphs 5.23 (ii) and (iv) of the consultation document and rejected. The Revenue still considers that neither proposal would be appropriate.*

*An exemption for securities held for a certain period would do nothing to simplify the AIS, and would arguably add to complexity. In addition, it would enable the very wealthy individuals and large trusts to avoid income tax by recycling a proportion of their holdings at a frequency just exceeding the exemption period.*

*Bringing securities fully within the capital gains net would be a reversal of the aim of the AIS, which is to prevent conversion of income into more lightly taxed capital gains. It would also have potential ramifications for the tax system beyond the confines of a reform of the AIS.*

## **NEXT STEPS**

As announced today, the Government has decided to proceed with reform of the AIS and is to further consult with respondents on the fine detail of the reform, with a view to including legislation in the 2006 Finance Bill.

## Appendix A

### LIST OF RESPONDENTS

<b>Individuals</b>
Gregory Wheatley
Anthony Nixon
Toby Harris

<b>Representative and Accountancy Bodies</b>
City of Westminster and Holborn Law Society
The Chartered Institute of Taxation
The Institute of Chartered Accountants in England and Wales
The Association of Corporate Trustees
The London Society of Chartered Accountants
Deloitte & Touche LLP