

## BUDGET 2006

### Tax avoidance – the net closes

In recent years, we have become accustomed to Budget speeches being light on surprises, with changes being widely trailed in advance. Certainly, as far as issues in the employee benefits arena are concerned, the 2006 Budget continues this practice and indeed continues to pursue a theme that has been central to Treasury policy for several years now – anti-avoidance.

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#### Pension issues

There are three measures related to the A-day pension changes that get a mention – all effectively anti-avoidance measures.

The only real news concerns measures to limit the attractiveness of alternatively secured pensions. This is the mechanism by which members of a defined contribution arrangement will be allowed to avoid purchasing an annuity once they reach age 75. They are being introduced for the benefit of individuals who objected on religious grounds to annuities, but will be available to anyone. On death, if there are no dependants to whom a dependant's income could be provided, any unused funds could be transferred to other family members in the same scheme. Many advisers have been suggesting that such arrangements would be an effective way of passing money down the generations, using a self invested personal pension (SIPP) or

small self-administered scheme (SSAS). As suggested in a consultation document last July, HMRC have now confirmed that, where unused funds are transferred on in this way, they would be subject to inheritance tax as if they were part of the member's estate.

The second measure that gets mentioned also affects SIPPs and SSASs. This is the proposal, announced in the pre-Budget report in December, to go back on the previously declared intention to allow virtually unfettered investment freedom to members of such schemes. This had led many to talk of widespread use of such schemes as tax-effective vehicles for buying second homes, as well as fine wine, works of art and the like. Today's statement simply reiterates that measures will be included in the Finance Bill to remove the tax advantages for such investments.

The third measure was also flagged in the pre-Budget report, but this potentially affects all schemes and many more members. This is the controversial proposal to penalise a member (and potentially the scheme) if a tax-free cash sum is taken with the intention of re-investing it (or “re-cycling” it) in the same or a further pension arrangement. Draft legislation and guidance were originally published at the beginning of February and justifiably met with considerable criticism. The problem is that the “crime” is that the member has to have “envisaged” at the time the sum is taken that future pension contributions would be greater as a result of taking the cash sum. If HMRC believe this to be the case, the member would have to prove otherwise to avoid the whole cash sum being subject to an unauthorised payment charge of 40%. Furthermore, the scheme making the cash sum payment would have to demonstrate that it should not be

subject to a scheme sanction charge of at least 15% of the amount paid. We had hoped that the unreasonable nature of this measure and the likely difficulties arising trying to police it would become apparent to HMRC but unfortunately revised drafts published today do little to ease our concern.

The only slight improvement is that their guidance now says that a scheme would be able to justify not having the scheme sanction charge imposed, provided it has asked the member whether they intend to “re-cycle” the cash sum and the member has replied in the negative. As things stand, this measure could affect people taking cash sums of as little as £15,000 and it really does seem to us to be a totally unwarranted complication.

Hopefully, common sense will prevail once the matter is debated as part of the Finance Bill.

## Wider employment-related anti-avoidance issues

In a wider context, the government has reiterated the commitment made in the pre-Budget statement in December 2004 to clamp down on schemes designed to avoid the payment of tax and/or national insurance. Despite that statement, various

schemes have apparently been put in place using options over shares and securities. In accordance with the 2004 statement, these will now be retrospectively closed with effect from the date of the statement, 2 December 2004.

## Conclusion

At the end of our Budget response last year, we said that we would have liked more definitive detail and guidance on the tax reform measures due to come into force in a year's time. Sadly, the year is now almost up and the goal-posts are still being moved, with full guidance still neither complete nor accurate. In the light of the anti-avoidance theme running through the topics we have mentioned, we guess the truth is that we are unlikely to ever be able to say definitively that the rules for pension provision are set, straightforward and unambiguous. That doesn't augur well for the encouragement of the widespread long-term pension planning that the government purports to support.

And finally, while talking about the future, there are clear statements within the Budget report supporting the view that the Treasury is opposed to a key element of the Pension Commission's recommendations that was supported by the Department for Work and Pensions – the provision of a larger State basic pension as the foundation upon which private provision can be built.

The outcome of this inter-departmental tussle may emerge in the White Paper, promised for the Spring.