

# International Wealth Account

The UK tax consequences of taking capital from an offshore non-qualifying single premium life plan

The method you use to take capital from your International Wealth Account (IWA) can have a significant impact on the amount of tax you pay at the time of the withdrawal.

Your IWA is classified by HM Revenue and Customs as an 'offshore single premium non-qualifying life insurance plan'. Your plan is made up of 100 identical policies or clusters. These clusters are designed to enable UK tax resident planholders to minimise the amount of income tax due where a plan withdrawal creates a chargeable gain for UK income tax purposes.

The following notes compare the UK tax treatment of taking capital as a withdrawal across all clusters, or by surrendering whole clusters within the plan.

There are two possible methods of withdrawing capital from IWA, and each method may have different consequences for a UK resident tax payer:

- 1 A withdrawal by cashing-in all, or a specific number of individual clusters – options A or D on the IWA Claim form (MSP8511).
- 2 A withdrawal across all clusters – options B or C on the IWA Claim form (MSP8511) are both variations of this type of withdrawal.

The table below shows a plan history for a UK resident planholder liable to higher rate income tax (40%) on any life plan gains. The planholder requires a sum of GBP80,000 from the plan in the fourth plan year and the two examples show each of the withdrawal methods in turn and their impact on UK income tax:

Plan year	Date	Contribution	Withdrawal	Plan value at withdrawal	
1	08/04/2002-07/04/2003	GBP100,000	-		
2	08/04/2003-07/04/2004	-	-		
3	08/04/2004-07/04/2005	-	-		
4	08/04/2005-07/04/2006	-	GBP80,000	Plan value	GBP130,000
				Cash-in charge	(GBP2,000)
				Cash-in value	GBP128,000

### Example one – withdrawal across all clusters

A UK tax resident planholder is entitled to withdraw up to 5% of plan contributions each year without an immediate charge to income tax. This is known as the 'tax deferred withdrawal allowance'. In this case, any income tax is deferred until a future date, which would normally be when the plan is finally surrendered (although other possible events could result in the tax being chargeable).

In the above example, no previous withdrawals have been made in four plan years; therefore the planholder has a tax deferred withdrawal allowance of:

$$\text{GBP}100,000 \times 5\% \times 4 \text{ years} = \text{GBP}20,000$$

Income tax is immediately charged on any excess over this tax deferred withdrawal allowance, as follows:

Withdrawal =	GBP80,000
less 5% allowance (4 x GBP5,000) =	(GBP20,000)
Chargeable excess =	GBP60,000

#### Income tax due

$$\text{GBP}60,000 \times 40\% = \quad \quad \quad \text{GBP}24,000$$

### Example two – individual cluster cash-in

In this case, a significant number of whole clusters are cashed in. Unlike example one, there is no tax deferred allowance where whole clusters are cashed-in.

The chargeable gain is calculated as follows:

$$\text{Withdrawal required} = \text{GBP}80,000$$

Each single policy is worth

$$\text{GBP}130,000/100 = \text{GBP}1,300$$

But this is reduced further by any early cash-in charge.

Charge is 2% of contribution in year 4 = GBP2,000 for the entire plan or GBP20 per single cluster.

Each single policy is worth

$$\text{GBP}130,000 \div 100 = \text{GBP}1,300 - \text{GBP}20 = \text{GBP}1,280$$

How many clusters are needed to realise GBP80,000?

$$\text{GBP}80,000 \div \text{GBP}1,280 = 62.5$$

Planholders can only cash-in whole clusters, so in this case the number of clusters cashed-in is rounded down to 62.

Calculate the chargeable gain for one cluster using the following chargeable gain formula:

$$\text{Chargeable gain} = (A+B) - (C+D)$$

Where:

A = Cash-in charge (**net of any early cash-in charge**)

B = Previous withdrawals

C = Contribution

D = Previous chargeable excesses

$$\text{Chargeable gain} = (\text{GBP}1280 + \text{GBP}0) - (\text{GBP}1000 + \text{GBP}0)$$

$$\text{Chargeable gain} = \quad \quad \quad \text{GBP}280 \text{ per policy}$$

$$\text{Multiply by } 62 = \quad \quad \quad \text{GBP}17,360$$

#### Income tax due

$$\text{GBP}17,360 \times 40\% = \quad \quad \quad \text{GBP}6,944$$

**This is an immediate saving in tax of GBP17,056 for the same planholder compared to a withdrawal across all clusters.**

In this case you would receive GBP1,280 x 62 = GBP79,360, but you wanted to receive GBP80,000. The remaining GBP640 would be taken as a partial withdrawal across the remaining 38 clusters.

Is this chargeable to income tax? No, as the remaining 38 clusters have unused 5% allowances as follows:

$$100,000 \times 38 \div 100 (\text{contribution}) \times 5\% \text{ p.a.} \times 4 \text{ years} = \text{GBP}7,600$$

of which the partial withdrawal = GBP640

c/fwd 5% allowance =

$$\text{GBP}7,600 - \text{GBP}640 = \text{GBP}6,960$$

## Summary

In general terms the use of the two methods of taking capital from life plans may not make much difference over the lifetime of the plan, as any gain resulting from an excess withdrawal will be brought into the tax calculation on a full cash-in. However, as can be seen above, the immediate liability to income tax at the time of the withdrawal of capital can vary enormously.

## Further information

**There are two forms of relief available to some individuals which may help to reduce any UK income tax liability from life plan gains still further:**

- 1 Time apportionment relief** – reduces the chargeable gain when an individual returns to the UK having already purchased a plan. If the plan is held in trust by trustees resident for tax purposes outside the UK, this relief is unavailable.

The gain is reduced using the fraction:  $\frac{A}{B}$

Where A is the number of days the planholder was not resident in the UK and B is the number of days in the period.

- 2 Top slicing relief** – available to an individual not already a higher rate tax payer and reduces any resulting liability to higher rate tax arising as a consequence of adding the chargeable gain to their income for that year.

Where the plan is offshore, the number of years since commencement is taken into account. Where the plan was issued by a UK resident insurer as an onshore plan, the number of years since any previous chargeable event or, if none, since commencement, is taken into account.

Where a planholder was not resident in the UK for a proportion of the time that a plan has been held and top slicing relief applies in respect of a gain, then the number of complete plan years available in calculating the relief is reduced by the number of complete plan years during which the planholder was not resident in the UK.

Where the plan is subject to the rate applicable to a trust, top slicing relief is not available to trustees as they are subject to a flat rate of tax of 50%.

**If both time apportionment relief and top slicing relief apply to a particular individual, time apportionment relief is applied, then top slicing relief.**

Please note, however, that plans classified as personalised portfolio bonds are treated differently for tax purposes in the UK. If you are in any doubt how your plan is treated for tax purposes, we strongly recommend that you seek specialist tax advice.

Tax planning, and international tax planning in particular, is a complex area and we recommend that you seek professional financial advice.

**This guidance note is for information only, does not constitute advice and is not to be relied on as part of any recommendation. It is based on our understanding of UK taxation legislation as at July 2010. Tax is not the only determining factor when deciding how to take capital from an IWA, and Zurich International Life strongly recommends that planholders seek advice from their relevant financial professional before taking any action.**

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