



Finance (No. 2) Act 2005

2005 CHAPTER 22

PART 2

INCOME TAX, CORPORATION TAX AND CAPITAL GAINS TAX

CHAPTER 4

AVOIDANCE INVOLVING TAX ARBITRAGE

24 Deduction cases

- (1) If the Commissioners for Her Majesty's Revenue and Customs consider, on reasonable grounds, that conditions A to D are or may be satisfied in relation to a transaction to which a company falling within subsection (2) is party, they may give the company a notice under this section.
- (2) A company falls within this subsection if—
 - (a) it is resident in the United Kingdom, or
 - (b) it is resident outside the United Kingdom but is within the charge to corporation tax.
- (3) Condition A is that the transaction to which the company is party forms part of a scheme that is a qualifying scheme.
- (4) Condition B is that the scheme is such that for the purposes of corporation tax the company is in a position to claim or has claimed an amount by way of deduction in respect of the transaction or is in a position to set off or has set off against profits in an accounting period an amount relating to the transaction.
- (5) Condition C is that the main purpose, or one of the main purposes, of the scheme is to achieve a UK tax advantage for the company.
- (6) Condition D is that the amount of the UK tax advantage in question is more than a minimal amount.

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- (7) A notice under this section is a notice—
 - (a) specifying the transaction in relation to which the Commissioners consider that conditions A to D are or may be satisfied,
 - (b) specifying the accounting period in relation to which the Commissioners consider that condition B is or may be satisfied as regards the transaction, and
 - (c) informing the company that as a consequence section 25 (rules relating to deductions) has effect in relation to the transaction.
- (8) Nothing in this section prevents the Commissioners from giving a company falling within subsection (2) a notice under this section as regards two or more transactions.
- (9) Schedule 3 makes provision about what constitutes a qualifying scheme.

25 Rules relating to deductions

- (1) The following provisions of this section apply in relation to a transaction if—
 - (a) a notice specifying the transaction is given to a company under section 24, and
 - (b) when the notice is given, conditions A to D of section 24 are satisfied in relation to the transaction.
- (2) The company must compute (or recompute) for the purposes of corporation tax its income or chargeable gains, or its liability to corporation tax—
 - (a) for the accounting period specified in the notice under section 24, and
 - (b) for any subsequent accounting period,
 in accordance with rules A and B.
- (3) Rule A is that, in respect of the specified transaction, no amount is allowable as a deduction for the purposes of the Corporation Tax Acts to the extent that, in relation to the expense in question, an amount may be otherwise deducted or allowed in computing the income, profits or losses of any person for the purposes of any tax (including any foreign tax) other than—
 - (a) petroleum revenue tax, or
 - (b) the tax chargeable under section 501A(1) of ICTA (supplementary charge in respect of ring fence trades).
- (4) The reference in subsection (3) to an amount otherwise deducted or allowed in computing the income, profits or losses of any person for the purposes there mentioned includes a reference to an amount that would be so deducted or allowed but for any rule that has the same effect as rule A.
- (5) For the purposes of subsection (4) “rule” means—
 - (a) a provision of the Tax Acts, or
 - (b) a rule having effect under the tax law of any territory outside the United Kingdom.
- (6) Rule B applies if—
 - (a) a transaction, or a series of transactions, forming part of the scheme by reference to which conditions A to D are satisfied makes or imposes provision as a result of which one person (“the payer”) makes a payment and another person (“the payee”) receives, or becomes entitled to receive, a payment or payments,

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- (b) in respect of the payment by the payer, an amount may be deducted or otherwise allowed to the payer, or to another person who is party to, or concerned in, the scheme, in computing any profits or losses for tax purposes, and
 - (c) in respect of the payment or payments that the payee receives or is entitled to receive as a result of the transaction or series of transactions, or part of such payment or payments, the payee is not liable to tax or, if liable, his liability to tax is reduced as a result of provision made or imposed by the scheme.
- (7) Without prejudice to the generality of subsection (6)(c), the payee's liability to tax in respect of the payment or payments that he receives or is entitled to receive as a result of the transaction or series of transactions shall be treated for the purposes of subsection (6)(c) as reduced as a result of provision made or imposed by the scheme if—
 - (a) an amount arising from the transaction or series of transactions forming part of the scheme, or from another transaction or series of transactions forming part of the scheme, falls to be deducted or otherwise allowed to the payee in computing for tax purposes any profits or losses arising from the payment or payments or the entitlement to receive the payment or payments, or
 - (b) an amount of relief arising from the transaction or series of transactions forming part of the scheme, or from another transaction or series of transactions forming part of the scheme, may be deducted from the amount of income or gains arising from the payment or payments or the entitlement to receive the payment or payments.
- (8) The requirement in subsection (6)(c) is not satisfied if the payee is not liable to tax because he is not liable to tax on any income or gains received by him or for his benefit under the tax law of any territory.
- (9) The requirement in subsection (6)(c) is not satisfied if, or to the extent that, the payee is not subject to tax because his liability to tax is subject to an exemption falling within subsection (10).
- (10) An exemption falls within this subsection if—
 - (a) it exempts a person from being liable to tax in respect of income or gains, without providing for that income or those gains to be treated as the income or gains of one or more other persons, and
 - (b) it is conferred by a provision contained in or having the force of an Act or by a provision of the tax law of any territory outside the United Kingdom.
- (11) Rule B is that the aggregate of the amounts allowable as a deduction for the purposes of the Corporation Tax Acts in computing any profits to the company arising from—
 - (a) the specified transaction, and
 - (b) any other transaction that forms part of the scheme and to which the company is party,is to be reduced in accordance with subsections (12) and (13).
- (12) If, in respect of the payment or payments that the payee receives or is entitled to receive, the payee is not liable to tax for the purposes of the requirement in subsection (6)(c), the aggregate is to be reduced to nil.
- (13) If, in respect of the payment or payments, the payee is liable to tax as regards part or his liability to tax is reduced as described in subsection (6)(c), the aggregate is to be reduced to such proportion of the aggregate as is equal to the proportion of the payment

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or payments on which the payee is liable to tax; and for this purpose the amount by which the payee's liability is reduced is to be treated as an amount on which the payee is not liable to tax.

- (14) The company may choose to incorporate in its company tax return for the specified accounting period such relevant adjustments as are necessary for counteracting those effects of the scheme that are referable to the purpose referred to in condition C.
- (15) If, as a consequence of incorporating relevant adjustments in that company tax return, the company counteracts those effects of the scheme that are referable to the purpose referred to in condition C, the company is to be treated, so far as regards the scheme, as having complied with subsection (2).
- (16) The following are relevant adjustments—
 - (a) treating all or part of a deduction allowable for corporation tax purposes as not being allowable;
 - (b) treating all or part of an amount that for corporation tax purposes may be set off against profits in an accounting period as not falling to be set off.
- (17) In this section, references to tax purposes include a reference to the purposes of any foreign tax; and foreign tax has the meaning given by section 403D of ICTA.
- (18) In this section, “company tax return” means the return required to be delivered pursuant to a notice under paragraph 3 of Schedule 18 to FA 1998, as read with paragraph 4 of that Schedule.

26 Receipts cases

- (1) If the Commissioners for Her Majesty's Revenue and Customs consider, on reasonable grounds, that conditions A to E are or may be satisfied in relation to a company resident in the United Kingdom, they may give the company a notice under this section.
- (2) Condition A is that a scheme makes or imposes provision (“the actual provision”) as between the company and another person (“the paying party”) by means of a transaction or series of transactions.
- (3) Condition B is that the actual provision includes the making by the paying party, by means of a transaction or series of transactions, of a payment that is a qualifying payment in relation to the company.
- (4) Condition C is that, as regards the qualifying payment made by the paying party, there is an amount that—
 - (a) is available as a deduction for the purposes of the Tax Acts, or
 - (b) may be deducted or otherwise allowed in respect of the payment under the tax law of any territory outside the United Kingdom,
 and does not fall to be disregarded as described in subsection (5).
- (5) An amount is to be disregarded if or to the extent that it is, for tax purposes, set against any income arising to the paying party from the transaction or transactions forming part of the scheme.
- (6) Condition C is not to be treated as satisfied if—
 - (a) the paying party is a dealer,
 - (b) in the ordinary course of his business, he incurs losses in respect of the transaction or transactions forming part of the scheme to which he is party, and

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- (c) the amount by reference to which condition C would, but for this subsection, be satisfied is an amount in respect of those losses.
- (7) In subsection (6), “dealer” means a person who is a dealer in relation to a distribution within the meaning of section 95(2) of ICTA or who would, if he were resident in the United Kingdom, be such a dealer.
- (8) Condition D is that at least part of the qualifying payment is not an amount to which subsection (9) or (10) applies.
- (9) This subsection applies to an amount that is, for the purposes of the Corporation Tax Acts—
 - (a) income or gains arising to the company in the accounting period in which the qualifying payment was made in relation to the company, or
 - (b) income arising to any other company resident in the United Kingdom in a corresponding accounting period.
- (10) This subsection applies to an amount that is taken into account in determining the debits and credits to be brought into account by a company for the purposes of Chapter 2 of Part 4 of FA 1996 as respects a share in another company by virtue of section 91A or 91B of FA 1996 (shares treated as loan relationships).
- (11) Condition E is that the company and the paying party expected on entering into the scheme that a benefit would arise as a result of condition D being satisfied (whether by reference to all or part of the qualifying payment).
- (12) A notice under this section is a notice—
 - (a) informing the company of the Commissioners' view under subsection (1),
 - (b) specifying the qualifying payment by reference to which the Commissioners consider conditions B to E are or may be satisfied,
 - (c) specifying the accounting period of the company in which the payment is made, and
 - (d) informing the company that as a consequence section 27 has effect in relation to the payment.
- (13) For the purposes of this section a payment is a qualifying payment in relation to a company if it constitutes a contribution to the capital of the company.
- (14) For the purposes of this section the accounting period of a company (“company A”) corresponds to the accounting period of another company (“company B”) if at least one day of company A's accounting period falls within company B's accounting period.

27 Rule as to qualifying payment

- (1) The following provisions of this section apply in relation to a payment that is a qualifying payment in relation to a company if—
 - (a) a notice specifying that payment is given to the company under section 26, and
 - (b) when the notice is given, conditions A to E of section 26 are satisfied in relation to the company.
- (2) The company must compute (or recompute) for the purposes of corporation tax for the accounting period specified in the notice its income or chargeable gains, or its liability to corporation tax, as if the relevant part of the qualifying payment were an amount of income chargeable under Case VI of Schedule D arising to the company in that period.

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- (3) The relevant part of the qualifying payment is the part by reference to which conditions C and D are satisfied; and, where conditions C and D are satisfied in relation to the whole of the qualifying payment, the relevant part is the whole of the qualifying payment.
- (4) In this section “qualifying payment” has the same meaning as in section 26.

28 Notices under sections 24 and 26

- (1) Subsection (2) applies if the Commissioners for Her Majesty’s Revenue and Customs give a notice to a company under section 24 or 26 before the company has made its company tax return for the accounting period specified in the notice.
- (2) If the company makes its return for that period before the end of the period of 90 days beginning with the day on which the notice is given, it may—
 - (a) make a return that disregards the notice, and
 - (b) at any time after making the return and before the end of the period of 90 days, amend the return for the purpose of complying with the provision referred to in the notice.
- (3) If a company has made a company tax return for an accounting period, the Commissioners may only give the company a notice under section 24 or 26 in relation to that period if a notice of enquiry has been given to the company in respect of its return for that period.
- (4) After any enquiries into the return for that period have been completed, the Commissioners may only give the company a notice under section 24 or 26 if the requirements in subsections (5) and (7) are satisfied.
- (5) The first requirement is that at the time the enquiries into the return were completed, the Commissioners could not have been reasonably expected, on the basis of information made available to them or to an officer of Revenue and Customs before that time, to have been aware that the circumstances were such that a notice under section 24 or 26 could have been given to the company in relation to that period.
- (6) Paragraph 44(2) and (3) of Schedule 18 to FA 1998 (information made available) applies for the purposes of subsection (5) as it applies for the purposes of paragraph 44(1).
- (7) The second requirement is that—
 - (a) the company was requested to produce or provide information during an enquiry into the return for that period, and
 - (b) if the company had duly complied with the request, the Commissioners could reasonably have been expected to give the company a notice under section 24 or 26 in relation to that period.
- (8) If a company is given a notice under section 24 or 26 in relation to an accounting period after having made a company tax return for that period, the company may amend the return for the purpose of complying with the provision referred to in the notice at any time before the end of the period of 90 days beginning with the day on which the notice is given.

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- (9) If the notice under section 24 or 26 is given to the company after it has been given a notice of enquiry in respect of its return for the period, no closure notice may be given in relation to the company's tax return until—
- (a) the end of the period of 90 days beginning with the day on which the notice under section 24 or 26 is given, or
 - (b) the earlier amendment of the company tax return for the purpose of complying with the provision referred to in the notice.
- (10) If the notice under section 24 or 26 is given to the company after any enquiries into the return for the period are completed, no discovery assessment may be made as regards the income or chargeable gain to which the notice relates until—
- (a) the end of the period of 90 days beginning with the day on which the notice under section 24 or 26 is given, or
 - (b) the earlier amendment of the company tax return for the purpose of complying with the provision referred to in the notice.
- (11) Subsections (2)(b) and (8) do not prevent a company tax return for a period becoming incorrect if—
- (a) a notice under section 24 or 26 is given to the company in relation to that period,
 - (b) the return is not amended in accordance with subsection (2)(b) or (8) for the purpose of complying with the provision referred to in the notice, and
 - (c) the return ought to have been so amended.
- (12) In this section—
- “closure notice” means a notice under paragraph 32 of Schedule 18 to FA 1998;
 - “company tax return” means the return required to be delivered pursuant to a notice under paragraph 3 of Schedule 18 to FA 1998, as read with paragraph 4 of that Schedule;
 - “discovery assessment” means an assessment under paragraph 41 of Schedule 18 to FA 1998;
 - “notice of enquiry” means a notice under paragraph 24 of Schedule 18 to FA 1998.

29 Amendments relating to company tax returns

- (1) In Schedule 18 to FA 1998 (company tax returns, assessments, etc), in paragraph 25(1) (scope of enquiry) after “relief” insert “or a notice under section 24 or 26 of the Finance (No. 2) Act 2005 (avoidance involving tax arbitrage)”.
- (2) In paragraph 42 of that Schedule (restrictions on power to make discovery assessment etc), in sub-paragraph (2A), after “1988” insert “or section 24 or 26 of the Finance (No. 2) Act 2005”.

30 Interpretation

- (1) For the purposes of this Chapter—
- (a) references to a scheme are references to any scheme, arrangements or understanding of any kind whatever, whether or not legally enforceable, involving a single transaction or two or more transactions;

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- (b) it shall be immaterial in determining whether any transactions have formed or will form part of a series of transactions or scheme that the parties to any of the transactions are different from the parties to another of the transactions; and
 - (c) the cases in which any two or more transactions are to be taken as forming part of a series of transactions or scheme shall include any case in which it would be reasonable to assume that one or more of them—
 - (i) would not have been entered into independently of the other or others, or
 - (ii) if entered into independently of the other or others, would not have taken the same form or been on the same terms.
- (2) For the purposes of this Chapter, a scheme achieves a UK tax advantage for a person if in consequence of the scheme the person is in a position to obtain, or has obtained—
- (a) a relief or increased relief from income tax or corporation tax,
 - (b) a repayment or increased repayment of income tax or corporation tax, or
 - (c) the avoidance or reduction of a charge to income tax or corporation tax.
- (3) In subsection (2)(a) the reference to relief includes a reference to a tax credit.
- (4) For the purposes of subsection (2)(c) avoidance or reduction may in particular be effected by—
- (a) receipts accruing in such a way that the recipient does not pay or bear tax on them, or
 - (b) a deduction in computing profits or gains.

31 Commencement

- (1) The deduction cases provisions have effect in relation to accounting periods of a company beginning on or after 16th March 2005.
- (2) Where an accounting period of a company begins before, and ends on or after 16th March 2005, it shall be assumed for the purposes of the deduction cases provisions (and subsection (1) of this section) that that accounting period (“the straddling period”) consists of two separate accounting periods—
- (a) the first beginning with the straddling period and ending with 15th March 2005, and
 - (b) the second beginning with 16th March 2005 and ending with the straddling period,
- and the company’s profits and losses shall be computed accordingly for tax purposes.
- (3) The deduction cases provisions do not have effect so far as regards a transaction to which a company is party on 16th March 2005 and which on that date forms part of a scheme, if—
- (a) the company is not on 16th March 2005 connected with a person who is on that date also party to, or concerned in, the scheme, and
 - (b) the scheme ceases to exist before 31st August 2005.

Section 839 of ICTA applies for the purposes of this subsection.

- (4) The receipts cases provisions have effect in relation to any contribution to the capital of a company resident in the United Kingdom that is made on or after 16th March 2005.
- (5) In this section—

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- “the deduction cases provisions” means—
- (a) sections 24 and 25 and Schedule 3, and
 - (b) sections 28 to 30 so far as relating to the provisions in paragraph (a);
- “the receipts cases provisions” means—
- (a) sections 26 and 27, and
 - (b) sections 28 to 30 so far as relating to the provisions in paragraph (a).