

**EXPLANATORY MEMORANDUM TO**  
**THE INDIVIDUAL SAVINGS ACCOUNT (AMENDMENT No. 3) REGULATIONS**  
**2016**

**2016 No. 977**

**1. Introduction**

- 1.1 This explanatory memorandum has been prepared by HM Revenue and Customs (HMRC) on behalf of HM Treasury and is laid before the House of Commons by Command of Her Majesty.

**2. Purpose of the instrument**

- 2.1 This instrument extends the range of investments that can be held in an Individual Savings Account (ISA) by making certain debentures (including those offered via a crowdfunding platform) eligible investments for the innovative finance ISA. Interest and gains from these investments will be tax-advantaged within this account.

**3. Matters of special interest to Parliament**

*Matters of special interest to the Select Committee on Statutory Instruments*

- 3.1 None.

*Other matters of interest to the House of Commons*

- 3.2 As this instrument is subject to negative resolution procedure and has not been prayed against, consideration as to whether there are other matters of interest to the House of Commons does not arise at this stage.

**4. Legislative Context**

- 4.1 ISA is a tax-advantaged savings product providing relief from tax to individuals. The ISA rules are set out in the Individual Savings Account Regulations 1998 (S.I. 1998/1870) (ISA Regulations).
- 4.2 ISA Regulations establish three types of ISA (cash ISA, stocks and shares ISA and innovative finance ISA) and specify the investments which can be held in each of these accounts. Investments that qualify to be held in an innovative finance ISA are specified at ISA Regulation 8A. The ISA Regulations also set out which financial institutions can offer ISAs and other account features and requirements.
- 4.3 The ISA Regulations were amended most recently by the Individual Savings Account (Amendment No. 2) Regulations 2016 (S.I. 2016/364) which, among other changes, established the innovative finance ISA.
- 4.4 Financial institutions are regulated by the Financial Conduct Authority (FCA) when they carry out activities in article 25 (arranging deals in investments) of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (S.I. 2001/544) (Regulated Activities Order). This Order also provides a definition of instruments creating or acknowledging indebtedness at article 77.

- 4.5 Where appropriate, this instrument applies definitions used elsewhere in tax and financial services legislation. These include the definition of charity in the Finance Act 2010, and the definition of persons interested in the capital of a company at section 170 of the Income Tax Act 2007.

## **5. Extent and Territorial Application**

- 5.1 The extent of this instrument is the United Kingdom.
- 5.2 The territorial application of this instrument is the United Kingdom.

## **6. European Convention on Human Rights**

- 6.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

## **7. Policy background**

### *What is being done and why*

- 7.1 The changes in this instrument are designed to increase choice for ISA investors. The instrument adds certain debentures (including debt securities and bonds) issued by companies (as defined in the ISA Regulation 2(1)(a)) or charities to the investments that can be held in an innovative finance ISA. When held within this account, income and gains from these investments will be tax-advantaged for the investor.
- 7.2 The instrument updates ISA Regulation 8A (qualifying investments for an innovative finance component) to provide that certain debentures can be held in an innovative finance ISA if they are transferable securities issued by a company or a charity. Where relevant, the instrument provides or updates definitions of relevant terms within ISA Regulation 2 (interpretation). Transferable security is defined with reference to section 102A(3) of the Finance Services and Markets Act 2000 (FSMA) and the definition of debenture is drawn from article 77 of the Regulated Activities Order, concerning instruments creating or acknowledging indebtedness. The instrument also defines charity for ISA purposes with reference to Schedule 6 to the Finance Act 2010.
- 7.3 ISA Regulation 8A is also updated to provide additional qualifying conditions for debentures, including concerning how these investments are facilitated (with reference to article 25 of the Regulated Activities Order), as well as requirements in relation to the role of the person facilitating the investments and the client relationship with the investor.
- 7.4 Anti-abuse conditions are also provided in relation to these debentures. For example, an investment will not qualify to be held in an innovative finance ISA if it is made available to an individual by reason of their employment status or similar, or if the investor is connected with the issuer of the debenture (defined with reference to section 170 of the Income Tax Act 2007). Further anti-abuse conditions are provided in relation to linked investments.
- 7.5 Investors wishing to subscribe to an innovative finance ISA can do so by paying cash to an ISA provider, subject to the annual ISA subscription limit (£15,240 in the 2016/17 tax year). This cash can be used to purchase qualifying debentures to be held within the investor's ISA.
- 7.6 This instrument also updates various ISA provisions to take account of the eligibility of these investments. This includes changes to the general conditions for accounts and

subscriptions to accounts at ISA Regulation 4; the rules at ISA Regulation 5DDA allowing spouses or civil partners of deceased ISA investors to make an additional permitted subscription to ISA; the definition of ‘outstanding principal balance’ at ISA Regulation 2; and the information that account providers must supply to HMRC about the accounts they manage at ISA Regulation 31. Minor and consequential amendments are also made to other ISA Regulations.

### ***Consolidation***

7.7 There are no plans to consolidate the ISA Regulations.

## **8. Consultation outcome**

8.1 HM Treasury consulted on whether to allow crowdfunded debt and equity securities to be eligible for inclusion within an ISA between 8 July and 30 September 2015, and published its summary of responses in November 2015<sup>1</sup>. 32 responses were received. Following this consultation, the government decided that crowdfunded debt securities would be eligible for the innovative finance ISA from autumn 2016, and committed to consider the position of equity securities further.

8.2 Draft regulations to include crowdfunded debt securities within ISA were published for a four week technical consultation in August 2016. There were 46 responses to this consultation, many of which sought clarity on how this change applied to securities issued by co-operative and community benefit societies. Other respondents suggested changes that would allow securities issued by a wider range of organisations to be eligible for ISA. As regards the technical detail of the draft SI, respondents generally agreed that it would achieve the intended policy objective, although one minor technical update was required to appropriately reflect the role played by crowdfunding platforms in relation to these investments.

## **9. Guidance**

9.1 HMRC's Guidance Notes for ISA providers will be updated to reflect the changes to the ISA rules. The Guidance Notes are available at <http://www.hmrc.gov.uk/isa/isa-guidance-notes.pdf>

## **10. Impact**

10.1 The impact on business, charities or voluntary bodies is mainly for financial institutions who choose to offer these investments within an innovative finance ISA. These businesses will face one-off and ongoing costs from complying with the ISA Regulations. However, it is anticipated the overall costs for businesses will be negligible.

10.2 The measure could also increase access to finance for some companies and charities by making the debentures they issue more attractive to investors.

10.3 The impact on the public sector is expected to be negligible.

10.4 A Tax Information and Impact Note covering this instrument was published on 9 August 2016 on the HMRC website at <https://www.gov.uk/government/publications/income-tax-crowdfunding-and->

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<sup>1</sup> <https://www.gov.uk/government/consultations/isa-qualifying-investments-consultation-on-whether-to-include-investment-based-crowdfunding>

individual-savings-accounts/income-tax-crowdfunding-and-individual-savings-accounts

**11. Regulating small business**

- 11.1 The legislation applies to activities that are undertaken by small businesses.
- 11.2 No specific action is proposed to minimise regulatory burdens on small businesses.
- 11.3 The basis for the final decision on what action to take to assist small business is that no business will be required to make any changes as result of this instrument. Whether or not a business chooses to issue or offer these investments within an innovative finance ISA will be a commercial decision.

**12. Monitoring & review**

- 12.1 HMRC will monitor the impact of these changes on an ongoing basis using the information provided annually by ISA providers and through regular contact with ISA managers.

**13. Contact**

- 13.1 Helen Williams at HM Revenue and Customs - Telephone: 03000 512336 or email: [savings.audit@hmrc.gsi.gov.uk](mailto:savings.audit@hmrc.gsi.gov.uk) can answer any queries regarding the instrument.