EXPLANATORY MEMORANDUM TO

THE CORPORATION TAX ACT 2010 (PART 8C) (AMENDMENT) REGULATIONS 2017

2017 No. 364

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.

1.2 This memorandum contains information for the Select Committee on Statutory Instruments.

2. Purpose of the instrument

2.1 This instrument amends Part 8C of the Corporation Tax Act 2010 ("CTA 2010") so that charitable companies and amounts representing income of policyholders of with-profits funds are placed outside the scope of the special rate of corporation tax at 45% which is applied to restitution interest paid by HMRC.

2.2 It also strengthens an anti-avoidance provision to close a gap where the charge could have been avoided by a company being wound up or dissolved or where a company is a beneficiary of a claim for restitution which has been made on its behalf by a third party. Some minor changes are also made.

3. Matters of special interest to Parliament

Matters of special interest to the Select Committee on Statutory Instruments

3.1 This is the first use of the power provided by section 357YW of CTA 2010 to amend the provisions of Part 8C of CTA 2010.

3.2 Part 2 of this instrument has retrospective effect. The authority to make provisions with retrospective effect is contained in section 357YW(3) of CTA 2010.

Other matters of interest to the House of Commons

3.3 Disregarding minor or consequential changes, the territorial application of this instrument includes Scotland and Northern Ireland.

4. Legislative Context

4.1 There are changes being made to exclude charitable companies and amounts representing income of policyholders of with-profits funds to ensure they fall outside the scope of Part 8C.

4.2 The changes to the anti-avoidance provision are designed to close potential gaps in the legislation. The remaining changes are minor amendments for clarification purposes.

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 The Financial Secretary to the Treasury, Jane Ellison has made the following statement regarding Human Rights:

"In my view the provisions of the Corporation Tax Act 2010 (Part 8C) (Amendment) Regulations 2017 are compatible with the Convention rights."

7. Policy background

What is being done and why

7.1 The rules at Part 8C of CTA 2010 apply a special rate of corporation tax at 45% to payments of restitution interest made by HMRC with effect from 21 October 2015.

7.2 The restitution arises from claims made against HMRC for the (alleged) payment of tax to HMRC under a mistake of law or the (alleged) unlawful collection of tax by HMRC.

7.3 The policy rationale for setting a special rate of corporation tax at 45% was to tax the potential windfall which would arise to a claimant in receipt of an award of restitution. That windfall arises because many claims are for a significant number of years and, without Part 8C, the final award would be taxed at the prevailing low rate of corporation tax in comparison to the high rates of corporation tax which were in force over the period in which the restitution accrues.

Charitable companies (regulations 5 and 6)

Policyholders in with-profits funds (regulations 8 and 9)

7.4 In the case of both charitable companies and UK insurance companies in which policyholders invest in with-profits funds, the application of existing statutory exemptions under the Tax Acts meant that over the period of the claims, these claimants would either not have been liable to any tax at all (or would be liable to tax at a rate significantly below the current prevailing corporation tax rate) and without any reliance on available statutory reliefs, deductions or allowances. Consequently, the changes ensure that charitable companies are taken out of scope and UK insurance companies are taken out of scope to the extent that any restitution is attributed to its policyholders of with-profits funds.

Anti-avoidance provisions (regulations 7, 10 and 11)

7.5 At present if a claimant makes a claim on behalf of another person and passes any award to that person without the payment being recognised in its own financial statements it is arguable that the 45% charge cannot be applied to the claimant or the ultimate beneficiary. The proposed amendments at regulation 7 rectify this so that the rules will now apply the charge to the beneficiary in "pass through" situations.

7.6 Under the existing anti-avoidance provision at section 357YM of CTA 2010, if a company has assigned its rights to claim restitution to a person who is outside the scope of corporation tax and one of the main purposes for the transfer is to secure a tax advantage, the charge to the 45% corporation tax remains with the transferor company.

7.7 At present no provision has been made where the claimant is a non-resident company but is carrying on a trade in the United Kingdom through a permanent establishment in the United Kingdom and, separately, any transferor company (and by default the group of which it is a member) could avoid the retained charge by entering into liquidation or by being dissolved.

7.8 To address this, the amendments to the legislation proposed by regulation 10 now apply section 357YM to a non-resident company which carries on a trade in the United Kingdom through a permanent establishment in the United Kingdom. Regulation 11 introduces new legislation which will transfer the latent charge of the transferor company to a related group member if the transferor company enters into a winding up or is dissolved within a period of 12 months prior to when the tax on the restitution is withheld or becomes payable by an assessment (whichever is the later).

Miscellaneous amendments (regulations 12 to 18)

7.9 Regulation 12 clarifies that the tax withheld by HMRC when the award of restitution is paid will go towards discharging the claimant's liability under Part 8C of CTA 2010 as part of its self-assessment return.

7.10 Regulations 13 to 18 make minor amendments to the wording in certain sections of Part 8C of CTA 2010 which do not alter the effect or meaning of these sections.

8. Consultation outcome

8.1 There has been no public consultation on these changes since the major changes are anti-avoidance provisions. HMRC has consulted informally with the charitable sector in relation to the changes relevant to them.

9. Guidance

9.1 Guidance on the primary legislation has yet to be finalised but will take account of the proposed changes.

10. Impact

10.1 The impact on charities is that they will be placed outside the scope of the primary legislation as will amounts representing income of policyholders investing in with-profits funds. The impact on businesses will remain the same as before. There is no impact on voluntary bodies.

10.2 There will be no significant operational impact on HMRC.

10.3 A Tax Information and Impact Note covering this instrument will be published on the HMRC website at https://www.gov.uk/government/collections/tax-information-and-impact-notes-tiins.

11. Regulating small business

11.1 The amendments to the legislation are unlikely to have any impact on small businesses.

12. Monitoring & review

12.1 The legislation will be monitored through information collected from the relevant claims.

13. Contact

13.1 Susan Gardner at HMRC Telephone: 03000 563815 or email: susan.m.gardner@hmrc.gsi.gov.uk can answer any queries regarding the instrument.