FINANCE ACT 2009

EXPLANATORY NOTES

INTRODUCTION

Section 58Schedule 29: Manufactured Overseas Dividends

Details of the Schedule

2. Paragraph 1 amends Schedule 23A of the Income and Corporation Taxes Act 1988 (ICTA), which contains provision for the corporation tax treatment of manufactured payments. The amendments ensure that the borrower under a debtor repo (sale and repurchase agreement) is not able to claim relief for overseas tax in excess of the amount of tax actually borne.

3. Paragraph 1(2) amends paragraph 4(4) of Schedule 23A, which treats a company that receives a MOD as receiving it after deduction of overseas tax.

4. Sub-paragraph (3) inserts new sub-paragraph 4A after paragraph 4 of Schedule 23A.

5. New paragraph 4A(1) introduces a new rule for determining the amount of overseas tax treated as suffered where a MOD is treated as paid under paragraph 13(1) of Schedule 13 to Finance Act (FA) 2007 (requirement to deduct tax from manufactured payments). Paragraph 13(1) of Schedule 13 applies where an overseas dividend is paid during the period of a creditor repo and requires the "lender" under that repo to account for income tax under section 922(2) of the Income Tax Act 2007 (ITA) as if it had paid a MOD to the original holder of the securities at the time the dividend is payable. The new rule provides that the recipient shall be treated as if the MOD were received after deduction of tax of amount A.

6. New paragraph 4A (2) provides that amount A may be one of three amounts:

   - where sub-paragraph (3) applies it is the amount of tax deducted under section 922(2) of the ITA. This is the same as the current rule in paragraph 4(4) of Schedule 23A;
   - where sub-paragraph (4) applies it is the amount deducted under section 922(2) less the excess of the actual amount of MOD payment over the amount deducted under section 922(2) of ITA; and
   - in any other case it is nil.

7. New paragraph 4A(3) applies where a MOD is actually paid to the recipient and it equals the relevant net amount. The relevant net amount is the gross amount of the real overseas dividend less any tax which must be deducted under section 922(2) of ITA. So if the gross amount of the dividend were 100 and the amount of tax deducted under section 922(2) were 15 then the relevant net amount would be 85.

8. But new paragraph 4A(3) does not apply where it is reasonable to assume that, in deciding the repurchase price of the securities, account was taken of the amount of the MOD actually paid. Thus, it will not apply if the repurchase price is lower than it would

be if the price reflected only the finance return implicit in the repo so that in substance a MOD greater than the relevant net amount is paid by the dividend manufacturer.

9. The language used here is similar to that formerly used in section 737A(2)(d) of ICTA 1988 (deemed manufactured payments under certain repo arrangements) before its repeal for corporation tax purposes in 2007.

10. New paragraph 4A(4) applies where a MOD is actually paid to the recipient and it exceeds the relevant net amount. In such a case the overseas tax is reduced by the excess. The effect is that if the gross amount of the dividend were 100, the amount deducted under section 922(2) of ITA were 15, but the actual MOD paid was 90 then the overseas tax would be treated as 10. This reflects the fact that in substance only 10 of overseas tax is economically borne by the recipient.

11. But new paragraph 4A(3) does not apply where it is reasonable to assume that, in deciding the repurchase price of the securities, account was taken of the amount of the MOD actually paid.

12. New paragraphs 4A(5) and (6) provide that the "repurchase price of the securities" means the price at which the payer of the MOD is entitled or obliged to sell the securities back to the recipient of the MOD, and that securities for this purpose means the securities in respect of which the MOD is paid.

13. New paragraph 4A(7) defines "relevant net amount" as the excess of the gross amount of the overseas dividend (as determined under paragraph 4(5) of Schedule 23A) less the amount of tax required to be deducted under section 922(2) of ITA.

14. Paragraph 2 provides that where a person receives a MOD by virtue of 736B of ICTA (deemed MODs in the case of certain stocklending arrangements) then the recipient is not treated as suffering overseas tax. This change to the rules for stocklending simply aligns those rules with the new position for repos.

15. Paragraph 3 gives the commencement rule. The legislation applies in relation to overseas dividends paid on or after 22 April 2009.