These notes refer to the Finance Act 2012 (c.14) which received Royal Assent on 17 July 2012

FINANCE ACT 2012

EXPLANATORY NOTES

INTRODUCTION

Section 22: Treatment of the Receipt of Manufactured Overseas Dividends

Summary

1. Section 22 clarifies the legislation on manufactured overseas dividends (MODs). That legislation provides that where a MOD is received under deduction of tax, some or all of that tax may be treated as overseas tax. The change makes it clear that where there is a difference between the tax deducted, and the tax treated as overseas tax, the difference is not treated as income tax. This section also makes a similar change for deemed manufactured payments under some stock lending arrangements. The amendments have effect in relation to overseas dividends paid on or after 15 September 2011.

Details of the Section

2. Subsection (1) introduces amendments to the provisions in Part 17 of the Corporation Tax Act 2010 (CTA 2010) which cover the treatment of companies receiving MODs.

3. Where a company receives a MOD, and tax has been deducted under section 922(2) of the Income Tax Act 2007 (ITA 2007), then sections 792 and 793 of CTA 2010 provide that some or all of the tax deducted may be treated as overseas tax.

4. Subsection (2) inserts a new subsection (8) into section 793 of CTA 2010. The new subsection provides that if the amount mentioned in section 792(3)(b) (that is, the amount treated as withheld on account of overseas tax) is not the amount deducted under section 922(2) of ITA 2007, then nothing in the Tax Acts has the effect that the difference between the amounts is to be regarded as an amount on account of income tax.

5. Section 812 of CTA 2010 provides that where there is a stock lending arrangement, dividend or interest income is received by someone other than the lender of the security, and the arrangement does not provide for the lender to receive payments representing the dividend or interest, then the borrower is deemed to have paid a manufactured payment to the lender on the date when the real dividend or interest was paid. Sub-sections 812 (4) and (5) have the effect that tax withheld from these deemed manufactured payments is not treated as overseas tax.

6. Subsection (3) inserts new subsection (5A) into section 812 which provides that any amount, that would otherwise have been treated as an amount withheld on account of overseas tax from the dividends arising in the circumstances covered by section 812, is not an amount on account of income tax.

7. Subsection (4) provides that the amendments made by this section have effect in relation to overseas dividends paid on or after 15 September 2011.

Background Note

8. Financial traders and other participants in the financial markets commonly transfer shares on a temporary basis from one party to another as a form of secured loan or to gain access to specific securities. Payments known as MODs are often made by the temporary holder of shares to the original owner as compensation for the dividends arising on the shares which are received by the temporary holder.

9. Where a MOD is paid, the payer must deduct a sum representing income tax equal to the relevant withholding tax on the MOD. A company receiving a MOD from which tax has been deducted is treated as if it had received an overseas dividend paid after withholding a certain amount of overseas tax. The amount of overseas tax treated as withheld can vary between nil and a maximum of the amount deducted.

10. Where the amount treated as overseas tax is less than the amount deducted, it has been suggested that the difference between the two amounts should be treated as income tax, available for set-off or repayment. HM Revenue and Customs does not agree that this is the effect of the legislation but subsection (2) of the amendment introduced by this section puts it beyond doubt that it is not treated as income tax.

11. Subsection (3) applies to certain deemed manufactured overseas dividends under stocklending arrangements, and has a similar effect to subsection (2), clarifying that withheld tax is not to be treated as income tax.