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 28: Deemed Receipts under s.26(4): Double Taxation Relief

Summary

1. Section 28 provides rules for the amount to be brought into account in the calculation of double taxation relief where a receipt arises to it under the rules applying in respect of the abolition of relief for equalisation reserves.

Details of the Section

2. Subsection (1) sets out three conditions for this section to apply. Firstly, a receipt must arise to a company as a result of section 26(4) and, secondly, that the company must carry on business through a permanent establishment (PE) outside the United Kingdom for which double taxation relief is due in respect of any income or gain. A third condition relates to the PE concerned and provides that the PE must be one to which double taxation relief regulations applied in respect of apportionment of transfers into an equalisation reserve.

3. Subsection (2) provides that only the appropriate proportion (if any) of the receipt is to be taken into account in calculating the profits or losses on which double taxation relief is calculated.

4. Subsection (3) defines the appropriate proportion of the receipt as being equal to the mean of each proportion found for the relevant period or any other proportion determined on a just and reasonable basis.

5. Subsection (4) defines, other than in cases where a just and reasonable basis has been determined by the company, a proportion for a relevant period as the proportion of the company's premium income constituted by the PE's premium income for the same period.

6. Subsection (5) provides definitions of "the company's premium income", "the PE's premium income" and a "relevant period".

7. Subsection (6) defines "net premiums written" and provides that references to section 444BA of the Income and Corporation Taxes Act of 1988 include that section as modified by regulations made under that Act.

Background Note

8. There is currently a regulatory requirement for general insurance companies (but not members of Lloyd's) to maintain equalisation reserves in respect of certain lines of business. From 1996, amounts transferred into equalisation reserves were made tax deductible and transfers out were treated as taxable receipts of the company's business.

9. The relief currently available is dependent on the regulatory requirement for general insurance companies to maintain equalisation reserves. As a result of the European Union Solvency II Directive that requirement will be withdrawn.

10. An informal consultation took place between April and August 2011 with an industry working group. Both the Association of British Insurers and Lloyd's, representing general insurance companies and corporate and partnership members at Lloyd's, have been included in the consultation process.

11. Taking into account these discussions, the Government has decided to repeal the legislation that allows tax relief for equalisation reserves. The Government has also decided to introduce a transitional period for the release of built-up reserves that involves spreading that release in equal instalments over a six year period commencing from the date that the Solvency II capital requirements come into force. Insurers may also elect to have the full remaining balance of the built-up reserve released to tax in any calendar year during the transitional period.