

FINANCE ACT 2012

EXPLANATORY NOTES

INTRODUCTION

Section 180 Schedule 20: Controlled Foreign Companies and Foreign Permanent Establishments

Details of the Schedule

Part 3

Other Amendments

- 535. Paragraphs 10 to 13 update the statutory references in TMA 1970 to reflect the statutory references in the new CFC rules for the CFC charge.
- 536. Paragraph 14 repeals Chapter 4 of Part 17 ICTA (i.e. the current CFC rules).
- 537. Paragraphs 15 to 17 amend FA 1998. The amendments provide for two changes. The first change amends section 32 so that unrelieved surplus advance corporation tax can be set against the CFC charge under its new statutory reference as if it were an amount of corporation tax for the accounting period. The second change amends Schedule 18 (which deals with company tax returns) to reflect the new statutory reference for the CFC charge.
- 538. Paragraphs 18 to 20 amend paragraphs 54 and 57 of Schedule 22 to FA 2000 (tonnage tax) to ensure that they continue to apply to a CFC which is a member of a tonnage tax group and is a tonnage tax company by virtue of the group's tonnage tax election in the same way as under the current CFC rules.
- 539. Paragraph 21 repeals section 90 of FA 2002 as a consequence of the repeal of section 747(1B) of ICTA. The latter section disregarded the treaty (i.e. double taxation arrangements) non-resident provisions in relation to the CFC rules and treated a treaty non-resident company as a UK resident company in certain circumstances.
- 540. Paragraph 22 amends section 725 of ITA 2007 (transfer of assets abroad: reduction in amount charged where controlled foreign company involved) to ensure that they continue to reduce any charge on an individual under section 721 in respect of income which would be, or would include, a sum charged under the new CFC rules.
- 541. Paragraph 23 amends paragraph 3 of Schedule 11 to FA 2007 (technical provision made by insurers) to reflect new statutory references to a CFC and ensure they are covered by the paragraph.
- 542. Paragraphs 24 to 31 make various amendments to CTA 2009 as follows.
- 543. Paragraph 25 amends the overview section in CTA 2009 to update the relevant statutory reference so as to reflect the replacement of the current CFC rules by the new CFC rules.
- 544. Paragraph 26 amends the disguised interest rules at section 486D by omitting the specific references to CFCs in that section. This is because any arrangement to which

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the “disguised interest” rules will apply in the new CFC rules in computing a CFC’s assumed taxable total profits will fall within section 371SP if there is an arrangement, the purpose, or one of the main purposes, of which is to obtain a tax advantage for any person under section 1139(2)(da) of CTA 2010.

545. Paragraph 27 amends section 486E to ensure that the disguised interest rules continue to be disapplied in relation to CFCs that are held in certain circumstances under a UK holding company.
546. Paragraph 28 amends section 521E (relating to shares accounted for as liabilities) by omitting specific references to CFCs at subsections (5) and (6) of section 521E. This is because any arrangement to which the rules for “shares accounted for as liabilities” will apply in the new CFC rules in computing a CFC’s assumed taxable total profits will fall within section 371SQ if there is an arrangement, the purpose, or one of the main purposes, of which is to obtain a tax advantage for any person under section 1139(2) (da) of CTA 2010.
547. Paragraph 29 omits section 870 which adjusts the intangible fixed assets provisions in relation to assumptions that should be made when applying these provisions in computing a CFC’s chargeable profits. This is because the same assumptions are now contained in section 371SK and apply when computing a CFC’s assumed taxable total profits for the purposes of the new CFC rules.
548. Paragraph 30 inserts new section 931CA into Chapter 2 of Part 9A CTA 2009 (exemption of distributions received by small companies).
549. New section 931CA provides that where a CFC charge is charged in relation to a CFC’s accounting period and a dividend or other distribution of the CFC is received in an accounting period of a recipient in which the recipient is a small company, the whole or part of the distribution will be treated as exempt as long as certain conditions are met. These conditions are that:
- the whole or part of the distribution is paid in respect of the chargeable profits of the CFC (defined as the chargeable profits that are apportioned to chargeable companies at step 3 in section 371BC(1) of TIOPA);
 - the distribution is not of a kind mentioned in paragraph E or F in section 1000(1) of CTA 2010 (certain non-dividend distributions);
 - no deduction is allowed to a resident of any territory outside the United Kingdom in respect of the distribution; and
 - the distribution is not made as part of a tax advantage scheme.
550. Paragraph 31 updates Condition B in section 931E. The condition is applicable in determining whether a distribution falls into an exempt class for the purpose of Part 9A of CTA 2009. The amendments outlined in the paragraph mean that the statutory definition of “control” in the new CFC rules in the case where control is established by reference to the legal and economic control exercised by a UK resident (with at least 40 per cent of holdings, rights or powers) and a non-UK resident (with at 40 per cent but no more than 55 per cent of holdings, rights or powers) will apply to the same extent that it did in the current CFC rules.
551. Paragraphs 32 to 36 make amendments to Part 2 of Schedule 16 to FA 2009. The amendments extend the exempt activities test exemption in the current rules for qualifying holding companies for an accounting period that begins on or after 1 July 2009 but before 1 January 2013. Paragraph 34 applies these changes with effect from 30 June 2012 which means there is now no requirement to split an accounting period of a qualifying holding company where the accounting period straddles 1 July 2012.
552. Paragraphs 37 to 39 make various amendments to CTA 2010 as follows.

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553. Paragraph 38 amends section 398D. This section restricts the use of losses against profits arising from leasing plant and machinery in certain defined circumstances and extends the restriction to setting losses against apportioned profits of a CFC that relate to the same activity. The amendments ensure that the same restriction of loss relief against apportioned chargeable profits of a CFC continues in the new CFC rules.
554. Paragraph 39 amends section 938M of CTA 2010 (group mismatch schemes: controlled foreign companies) to reflect the new statutory references in Part 9A and to ensure that the provision continues to apply in the same way as it did previously.
555. Paragraph 40 amends the definition of tax advantage at section 1139 to include at section 1139(2)(da) the avoidance or reduction of a CFC charge under Part 9A of TIOPA.
556. Paragraphs 41 to 45 amend TIOPA as follows.
557. Paragraph 42 amends section 179. That section applies the “compensating adjustment” rules at sections 174 to 178 where the transfer pricing rule at section 147 requires a CFC’s profits or losses to be calculated as if the arm’s length provision had been made or imposed instead of the actual provision. Where the CFC is the “advantaged person” (i.e. the person whose UK tax has been reduced or whose tax loss has been increased by the actual provision), the “disadvantaged person” can make a claim for a “compensating adjustment” as long as certain conditions in section 179 are met.
558. Paragraph 42(2) substitutes a new subsection (1). This provides that subsection (2) applies if:
- the actual provision is provision made or imposed in relation to a CFC,
 - for the purposes of determining the CFC’s assumed taxable total profits for an accounting period, the transfer pricing rules will apply to that provision,
 - in relation to the accounting period, sums are charged on chargeable companies at step 5 in section 371BC(1), and
 - in consequence of the application of the transfer pricing rules, the total of those sums is more than it would otherwise be.
559. Section 179(2) is amended by the substitution of “CFC” for “controlled foreign company”.
560. In section 179(3)(a), “chargeable companies on which a sum is charged” is substituted for “companies mentioned in subsection (1)(c)” and in subsection (3)(b), “the CFC charge” is substituted for “tax chargeable under section 747(4) of ICTA”.
561. Subsection (4) is replaced by new subsections (4) and (5). New subsection (4) defines terms used in section 179 by reference to Part 9A and new subsection (5) states that in determining whether sums are charged on chargeable companies for the purposes of step 5 in section 371BC(1), including whether the application of the transfer pricing rules results in those sums being more than they would otherwise be, any claims under Chapter 9 of Part 9A for the accounting period are disregarded.
562. Paragraph 43 introduces new section 298A which allows HMRC Commissioners to make regulations to reduce a CFC charge that is a financing income amount to the same extent as the corporation tax charge is reduced for other financing income amounts. In this way the regulations will eliminate a double charge while retaining the restrictive effect of the debt cap on interest deductions. The regulations may also make consequential changes to both the debt cap and the CFC regime, as appropriate.
563. Paragraph 44 amends section 314 of TIOPA by including amounts arising from the application of section 314A as finance income amounts.

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564. [Paragraph 45](#) inserts new section 314A which provides that, to the extent that credits would have been included in financing income amounts by virtue of section 314, they will be taken to be included as finance income amounts by virtue of section 314A if certain conditions are met. The conditions are as follows:
- a sum is charged on a company at step 5 in section 371BC(1) of Part 9A of TIOPA,
 - the CFC's relevant corporation tax accounting period (as defined in section 371BC(3)) is a relevant accounting period of the company in relation to a period of account of the worldwide group,
 - the CFC's accounting period in relation to which the sum is charged ends in the period of account of the worldwide group, and
 - the CFC's chargeable profits include amounts ("the relevant finance profits") which fall only within Chapter 5 or 6 of Part 9A or which are qualifying loan relationship profits within the meaning of Chapter 9 of Part 9A.
565. New section 314A(2) and (3) provide that the percentage of the chargeable profits of the CFC that relate to "the relevant finance profits" is to be taken as a financing income amount of the company for the period of account of the worldwide group.
566. New subsection (4) provides that the reference to "the relevant finance profits" which fall within Chapter 5 or 6 of Part 9A is limited to the following qualifying amounts:
- trading loan relationships as defined by section 297 CTA 2009, or
 - non-trading loan relationships as defined by section 299 CTA 2009.

Profits from derivative contracts that are brought into account under Part 5 of CTA 2009 by section 574 of that Act and profits that fall within subsection 314(3) of TIOPA are specifically excluded from being finance income profits under this subsection.

567. [Paragraphs 46 to 48](#) substitute "CFC" for "controlled foreign company" in regulations 8A and 8B of the [Insurance Companies \(Reserve\) \(Tax\) Regulations 1996 \(S.I. 1996/2991\)](#).