These notes refer to the Finance Act 2014 (c.26) which received Royal Assent on 17 July 2014

FINANCE ACT 2014

EXPLANATORY NOTES

INTRODUCTION

Section 30: Avoidance Schemes Involving the Transfer of Corporate Profits

Summary

1. This section of the Corporation Tax Act 2009 (CTA2009) stops tax avoidance arrangements where arrangements are entered into to transfer profits between companies in the same group for tax avoidance reasons. It does not apply to any arrangement falling within the new section 695A of CTA2009 (introduced in Finance Act 2014 and proposed to come into effect from 5 December 2013) which relates specifically to arrangements involving derivative contracts, but it does apply to arrangements that have been put in place to circumvent that provision.

Details of the Section

2. Subsection (1) introduces a new section 1305A into Chapter 1 of Part 20 of the Corporation Tax Act 2009.

3. New Subsection 1305A(1) sets out the circumstances in which section 1305A applies. These circumstances are where the conditions set out in subsections (1)(a) to (1)(d) are met. However, new subsection 1305A(5) provides that section 1305A will not apply to arrangements which are caught by section 695A CTA 2009.

4. New Subsection 1305A(1)(a) sets out the first condition, which is that two companies “A” and “B” are party to arrangements whether or not at the same time. Arrangements are defined in subsection 1305A (6) as including any scheme, arrangement or understanding, whether or not legally enforceable.

5. New Subsection 1305A(1)(b) sets out the second condition, which is that company A and company B are members of the same group. New Subsection 1305A(4) sets out when companies are in the same group for the purposes of section 1305A.

6. New Subsection 1305A(1)(c) sets out the third condition which is that the arrangement results in what is in substance a payment from A to B of all, or a significant part of, the profits of the business of A or of a company which is a member of the same group as A or B or both. This is called the “profit transfer” and can be either direct or indirect.

7. New Subsection 1305A(1)(d) sets out the fourth condition, which is that a main purpose of the arrangement must be to secure a tax advantage. ‘Tax advantage’ here takes its meaning from section 1139 of the Corporation Tax Act 2010.

8. New Subsection 1305A(2) provides that for the purposes of corporation tax the profits of company A are to be calculated as though no profit transfer had occurred.

9. New Subsection 1305A(3)(a) denies any deduction in respect of the profit transfer and section 1305A(3)(b) applies to all or part of the profit transfer not covered by subsection (3)(a) and states that the profits of A must be increased by the amount of the profit transfer.

10. Subsection (2) of the section is a commencement provision and provides that the legislation has effect in relation to payments made on or after 19 March 2014.

Background Note

11. Section 1305A applies a tax avoidance test to any arrangements entered into for what is in substance a transfer of profit between companies in the same group.

12. The measure follows the announcement of section 695A CTA 2009 on 5 December 2013, to be introduced in Finance Act 2014 with effect from the date of announcement.

13. This measure does not apply to transactions that fall within section 695A CTA2009, which closes down an avoidance scheme. In the scheme, a company enters into a derivative contract known as a total return swap, with a parent company or another group company, generally located in a tax haven. Under the contract, all of the profits of the company are paid away in return for much smaller payments back. A deduction is claimed for the payment under the contract, leaving little or no profit chargeable to tax.

14. Section 1305A in contrast applies irrespective of the mechanism by which profits are transferred and is therefore not limited to payments under a total return swap. It can apply to a wider range of arrangements than section 695A but unlike that section is subject to a test which requires the arrangements to have a tax avoidance purpose.