EXPLANATORY MEMORANDUM TO

THE TAX CREDITS (EXCLUDED COMPANIES) REGULATIONS

2009 No. 3333

1. This explanatory memorandum has been prepared by Her Majesty's Revenue and Customs and is laid before the House of Commons by Command of Her Majesty.

This memorandum contains information for the Select Committee on Statutory Instruments.

2. Purpose of the instrument

2.1 From 22 April 2009, an individual who owns a ten per cent or greater shareholding in a non-UK resident company and is in receipt of dividends will be entitled to a dividend tax credit if the dividend-paying company is a resident of a qualifying territory. Section 397BA of the Income Tax (Trading and Other Income) Act 2005 defines "qualifying territory" and also gives the Treasury power to designate a territory as non-qualifying even if it comes within the definition. These regulations designate certain descriptions of company resident in a qualifying territory as ineligible for the tax credit.

3. Matters of special interest to the Select Committee on Statutory Instruments

3.1 None

4. Legislative Context

4.1 Subsections 397BA (1) and (2) define "qualifying territory" as the United Kingdom and a territory with which the United Kingdom has a double taxation agreement with a non-discrimination provision.

4.2 The Regulations are made to exclude from the tax credit certain descriptions of company which are excluded from the benefits of such a double taxation agreement. This is the first use of the power to make regulations under section 397BA.

5. Territorial Extent and Application

5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

The Financial Secretary to the Treasury (The Rt. Hon Stephen Timms MP) has made the following statement regarding Human Rights:

In my view the provisions of the Tax Credits (Excluded Companies) Regulations 2009 are compatible with the Convention rights.

7. Policy background

7.1 Schedule 19 to the Finance Act 2009 implements the second part of a two-stage reform of UK personal dividend taxation.

7.2 Individuals in receipt of dividends from UK resident companies are entitled to a tax credit to compensate for the economic double taxation that arises from the same income being taxed twice – once as corporate profits in the hands of the payer company and then again as dividend income in the hands of the recipient. With effect from 6 April 2008, individuals in receipt of dividends from non-UK resident companies have also been entitled to a tax credit if they own less than 10 per cent of the shares in a non-UK resident company.

7.3 With effect from 22 April 2009, there is a further extension of the dividend tax credit to individuals in receipt of dividends from non-UK resident companies where the individual owns a 10 per cent or greater shareholding in the distributing non-UK resident company and the source country has a double taxation treaty with a non discrimination article. This has the effect of limiting the tax credit to dividends originating from territories which levy a tax on corporate profits similar to corporation tax.

7.4 However, some double taxation agreements exclude certain types of company from the benefits of the agreement. These typically are companies which are subject to minimal rates of taxation. The Regulations have the effect of excluding these companies from the tax credit.

8. Consultation outcome

8.1 There has been no formal consultation in relation to these Regulations. However, they have been available in draft on the HMRC website.

9. Guidance

9.1 Her Majesty's Revenue and Customs are publishing a Revenue and Customs brief "Changes to the Income Tax Credit for Foreign Dividends".

9.2 Full details of the changes and how they affect individual taxpayers will also be given in the Notes to the Foreign Pages of the 2009-2010 Self Assessment Return.

10. Impact

10.1 The impact on business, charities or voluntary bodies is negligible.

10.2 The impact on the public sector is negligible.

10.3 An Impact Assessment has not been prepared for this instrument because a negligible impact on the private or voluntary sector is foreseen.

11. Regulating small business

11.1 The legislation does not apply to small business.

12. Monitoring & review

12.1 The impact of the measure will be monitored through on-going surveillance and wider analysis of the savings market which will pick up any general trends in receipts of foreign dividend income.

13. Contact

Andrea Pierce at Her Majesty's Revenue and Customs Tel: 020 7147 2591 or email: andrea.pierce2@hmrc.gsi.gov.uk can answer any queries regarding the instrument.