

**EXPLANATORY MEMORANDUM TO
THE INCOME TAX (MANUFACTURED OVERSEAS DIVIDENDS)
(AMENDMENT) REGULATIONS 2010**

2010 No. 925

1. This explanatory memorandum has been prepared by Her Majesty's Revenue and Customs (HMRC) and is laid before Parliament by Command of Her Majesty.

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

2. **Purpose of the instrument**

- 2.1 These regulations amend the Income Tax (Manufactured Overseas Dividends) Regulations 1993 ("the principal Regulations").

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

- 3.1 None.

4. **Legislative Context**

- 4.1 These regulations are being made because transactions have been disclosed to HMRC indicating that the principal Regulations leave open the possibility of avoidance of UK tax. In particular, that they could be used to sidestep certain restrictions that aim to prevent recipients of manufactured overseas dividends (MODs) from obtaining relief for overseas tax more than once.

5. **Territorial Extent and Application**

- 5.1 This instrument applies to all of the United Kingdom.

6. **European Convention on Human Rights**

As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

7. **Policy background**

- *What is being done and why*

- 7.1 MODs arise where under an arrangement for the transfer of overseas securities one party (the overseas dividend manufacturer) is required to pay to the other an amount representative of dividends or interest on the securities.

7.2 On payment of a MOD the overseas dividend manufacturer is sometimes required to deduct and account to HMRC for an amount that broadly corresponds to the overseas tax that would have been deducted from a real overseas dividend paid to a UK resident.

7.3 The Principal Regulations allow certain payers of MODs known as Authorised UK Intermediaries (AUKIs) to reduce the amount of tax that they would generally have to withhold on paying a MOD by offsetting overseas tax they have incurred on receipts of unrelated real or manufactured overseas dividends.

7.4 Where the overseas tax is used in this way, then the principal Regulations also ensure that it cannot be used again. That is, it cannot then be credited against the UK tax payable on the overseas dividend; or deducted from the amount of the overseas income brought into charge to tax.

7.5 The principle underlying this restriction is that the overseas tax should be used only once, so having been used for offsetting it should not be available to credit or reduce the taxable income.

7.6 Transactions have been disclosed where the overseas tax that is used for offsetting is not fully taken into account as an element in calculating trading profits of the overseas dividend manufacturer. In that case, the overseas dividend manufacturer may effectively obtain relief for the overseas tax twice, once under the offsetting rules and secondly by virtue of it not being included in the amount of taxable income received.

7.7 The main amendment to the principal Regulations in regulation 6 (entitlement to offsetting) therefore makes it a requirement for offsetting treatment that the gross amount of the real overseas dividend must be brought into account by the overseas dividend manufacturer in computing taxable income. Therefore, if an AUKI chooses to offset, HMRC should be able to ensure that the denial of any other form of relief for the overseas tax is fully effective.

7.8 Regulation 6 does not apply where the overseas dividend manufacturer matches under regulation 10 of the principal Regulations the MOD payment with the equivalent real overseas dividend or MOD receipt.

7.9 Regulation 6 also allows the AUKI to elect to bring into account dividends or MODs used for offsetting on a gross basis. If it does so then it will be permitted to continue to offset as under the principal Regulations before amendment.

7.10 The other amendments to the principal Regulations are also designed to ensure that the gross amount of the real overseas dividend or MOD must be brought into account for tax as a condition for obtaining any form of relief for the overseas tax referable to that real overseas dividend or MOD.

7.11 It is not intended that these Regulations should be consolidated.

8. Consultation outcome

8.1 There has been no formal consultation but discussion with the industry about the main changes indicate they are content with the need to close the avoidance opportunities.

9. Guidance

9.1 HMRC will amend the existing guidance on principal Regulations to reflect the changes made by these Regulations before returns for the periods to which the regulations apply are filed.

10. Impact

10.1 An Impact Assessment has not been prepared for this instrument as there is no impact on the public sector, or on charities or voluntary organisations.

11. Regulating small business

11.1 The legislation does not apply to small business.

12. Monitoring & review

12.1 The outcome will be subject to internal review to ensure that the projected revenue yield is achieved.

13. Contact

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