

# Budget 2009



**HM Revenue  
& Customs**

**BN05**

**22 April 2009**

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## **TAXATION OF FOREIGN PROFITS**

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### **Who is likely to be affected?**

1. UK companies that are members of groups. The four elements of the foreign profits package will have the following impact:
  - changes to the rules governing the tax treatment of distributions received apply to all companies receiving foreign or UK dividends and other company distributions;
  - groups other than those consisting entirely of companies that are small or medium sized may be affected by the restriction of interest and other finance expense;
  - consequential changes to the Controlled Foreign Company (CFC) rules apply to companies that are subject to the existing CFC legislation; and
  - the repeal of the Treasury Consents rules applies generally and their replacement with a post-transaction information-reporting requirement applies to companies that undertake transactions of £100 million or more involving foreign investments.
2. UK companies that are not members of groups and receive dividends or other distributions, in relation to the changes to the rules governing the tax treatment of distributions.

### **General description of the measure**

3. The foreign profits package will be introduced in Finance Bill 2009 after a long period of consultation and consists of four elements:
  - dividends and other distributions received from foreign companies will largely be exempt from corporation tax (CT) and UK distributions will be exempt to the same extent;
  - finance expense payable by UK members of a group of companies will be subject to a cap equal to the consolidated gross finance expense of that group;
  - the CFC (superior and non-local) holding company exemptions and Acceptable Distribution Policy (ADP) exemption will be removed; and
  - the Treasury Consents rules (that requires approval from HM Treasury before certain transactions are undertaken) will be repealed and replaced by a post-transaction information-reporting requirement.

## **Operative date**

4. The changes to the taxation of distributions will apply to dividends and other distributions received on or after 1 July 2009.
5. The changes to the CFC regime have effect for accounting periods starting on or after 1 July 2009 with provision made for accounting periods that straddle this date. However, the exemption for non-local and superior holding companies may be available for qualifying companies in a transitional form until 1 July 2011.
6. The new reporting requirement applies to transactions undertaken on or after 1 July 2009.
7. The debt cap applies to finance expense payable in accounting periods beginning on or after 1 January 2010.

## **Current law and proposed revisions**

### Dividends

8. Foreign dividends and other distributions received are currently chargeable to CT, with credit given for any foreign tax withheld from a dividend and (for shareholdings of 10 per cent or more) for foreign tax charged on the profits out of which the dividend is paid (underlying tax). Currently UK distributions received are generally exempt from CT.
9. The new legislation will treat foreign and UK distributions in the same way. Distributions will generally be exempt if they fall into an exempt class and anti-avoidance provisions do not apply. The vast majority of distributions are expected to be exempt from CT. In addition to the changes announced in the 2008 Pre-Budget Report, exemption for dividends or other distributions arising from holdings of ten per cent or more will be extended to all companies.

### Debt cap

10. Interest is generally deductible in computing taxable profits, with various pieces of anti-avoidance legislation restricting relief in some circumstances.

11. The new legislation caps the tax deduction for finance expense payable by UK members of a group of companies to the consolidated gross finance expense of that group. Draft legislation was published on 9 December 2008. Following consultation a number of changes are proposed. These include:

- the way in which the net finance expense is calculated;
- the calculation of the consolidated gross finance expense; and
- introducing or amending a number of exclusions to deal with, for example, financial services, finance expense in respect of short term debt, group treasury companies and relatively small amounts of net finance expense

#### Controlled Foreign Companies (CFC)

12. The CFC regime currently provides an exemption from apportionment (and therefore from the resulting UK tax charge) for profits of a foreign company that qualifies as a holding company under the exempt activities test. The regime also exempts from apportionment profits of a foreign company that pays a dividend of at least 90 per cent of those profits within 18 months of the end of the accounting period concerned (the ADP exemption).

13. The changes to the CFC regime will remove the exemption for superior and non-local holding companies (subject to a two year transitional period) and the ADP exemption. The exemption for local holding companies will be retained.

#### Treasury Consents

14. The existing legislation requires companies to obtain approval from HM Treasury before undertaking certain transactions involving subsidiary companies resident outside the UK. The legislation includes a criminal sanction for non-compliance. For movements of capital between residents of EU Member States, the existing legislation imposes a reporting requirement.

15. The changes announced today will repeal the existing legislation. In its place the Government intends to introduce a modernised post-transaction reporting requirement that applies to transactions with a value of £100 million or more subject to a number of exclusions. These include several based on the existing 'general consents' rules and an exclusion for trading transactions. Companies must make a report within six months of the transaction.

#### Loan Relationships and derivative contracts: anti-avoidance

16. The draft legislation published on 9 December 2008 included provision for loan relationships and derivative contracts forming part of arrangements that have a tax avoidance purpose. The case for further legislation in this area will be kept under review, but the measure will not form part of Finance Bill 2009.

## **Further advice**

17. If you have any questions about:

- distributions please contact Andrew Page on 020 7147 2673 (email: [andrew.page@hmrc.gsi.gov.uk](mailto:andrew.page@hmrc.gsi.gov.uk));
- debt cap please contact Neil Nagle on 020 7147 2459 (email: [neil.nagle@hmrc.gsi.gov.uk](mailto:neil.nagle@hmrc.gsi.gov.uk)); and
- CFCs and Treasury consents please contact David Hannigan on 020 7147 2736 (email: [david.hannigan@hmrc.gsi.gov.uk](mailto:david.hannigan@hmrc.gsi.gov.uk)).

Information about Budget measures is available on the HM Revenue & Customs website at [www.hmrc.gov.uk](http://www.hmrc.gov.uk)