

OFFSHORE FUNDS – CONSULTATION ON TAX REFORM

SUMMARY OF RESPONSES ISSUED BY THE INLAND REVENUE ON 27th NOVEMBER 2002

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The consultation document issued on 22 April 2002 can be found on the Inland Revenue website at

http://www.inlandrevenue.gov.uk/consult_new/offshore_funds.pdf

Paper copies can be obtained from

Sonia Tennant
Revenue Policy
Business Tax
Room 4W2
22 Kingsway
LONDON WC2B 6NR

Telephone 020 7438 6989

Introduction

The Government is grateful for the responses to the consultation document issued by the Inland Revenue at the last Budget on the future of the offshore funds tax regime.

In the light of those responses, the Government has asked the Inland Revenue to take forward work for the 2004 Finance Bill, with the aim of replacing the current offshore funds regime with new rules that will provide similar tax treatment of investment in offshore funds and equivalent UK products. The Government remains committed to continuing constructive dialogue with fund managers and other stakeholders on the implementation of a new regime.

This report summarises the views and comments of respondents, starting with a general overview and then outlining what was said about each of the options discussed in the original document – “no change”, “abolition”, “reform” and “replacement”.

There is also an appendix containing a brief description of the current regime, including some of its key technical terms.

1 Overview

1.1 The Government published a consultation document on possible reform of the offshore funds tax regime on 22 April 2002, inviting responses by 31 July. There were 53 responses, mainly from representative bodies, fund managers, solicitors and accountants.

1.2 Respondents were unanimous in wanting reform. Recurring complaints were that the rules in sections 757-764 and Schedules 27-28 ICTA 1988 (the offshore funds regime)

- had not kept pace with commercial, regulatory and tax changes since their introduction in 1984;
- put unnecessary obstacles in the way of fund managers wanting to sell their funds to UK investors; and
- were discriminatory under European (EC) law.

1.3 Many outlined the principles they believed should underpin any new arrangements. These included

- tax neutrality between the treatment of investment in offshore and equivalent UK funds;
- rules that were easy to operate and comply with;
- compliance with EC law;
- reliance on accountancy and commercial returns; and
- where necessary, specially targeted measures to counter tax avoidance.

1.4 Respondents also argued that reform should be approached with long-term considerations in mind, and that the Government should avoid making repeated changes to the rules.

1.5 There were, however, different views about how best to achieve reform. A few respondents argued that the offshore funds regime could be removed without the need for substantive arrangements to be put in its place. But the majority accepted that some form of replacement regime would be necessary to avoid damaging the competitiveness of UK funds and similar savings products. Some respondents went further by pressing for wider changes encompassing the taxation of investment in UK authorised unit trusts (AUTs), open-ended investment companies (OEICs) and, in a few cases, life insurance companies. Those insurers who responded stressed that any major change to the way investment in AUTs and OEICs was taxed would need to take account of the taxation of life policies.

1.6 Most respondents argued that at the very least there should be specific changes to the current regime, making it easier for funds to apply for and secure “distributor” status. For example,

- the investment restrictions test should either be abolished or significantly modified to bring it into line with regulatory developments both within the UK and overseas;
- rules for determining whether the level of distributions to investors were sufficient should rely more on commercial accounting than on UK tax principles; and
- sub-funds, or even share classes, should be allowed to be classified in their own right as distributing funds, providing fund managers the economies of scale denied to them by the current rules.

1.7 But some doubt was expressed whether modifying the existing regime would go far enough. There was clearer support for the idea of a replacement regime based on the closer alignment of the tax treatment of investment in offshore funds with that of equivalent UK products. However, there were diverging views on the design of such a regime. Some differed on

points of principle such as the treatment of income that had been accumulated but not distributed. Some did not agree on the practicalities involved.

1.8 To the extent that it may not prove possible to align fully the tax regimes for onshore and offshore funds, the majority of responses preferred to retain an income tax charge on realisation for those investing in offshore funds that did not meet the conditions of either a new or amended regime.

Respondents were critical of the suggestion that gains in funds that did not meet the necessary conditions should be taxed by reference to annual increases in value. Some argued that income from investments in particular types of UK fund should be allowed to roll up without an annual income tax charge, in the same way as offshore funds.

2 No Change

Should the current regime be retained? If so, why?

2.1 The unanimous view of respondents was that the current offshore funds regime could not be left as it is. Reasons given were that it

- no longer fulfills its original design brief, nor meets current objectives as set out in the consultation document;
- may be susceptible to challenge under EC Law;
- acts as a barrier between the UK and other European Union (EU) member states as funds designed for UK investors may not be attractive to continental European investors;
- is restrictive, onerous and over-complex, and forces decisions that are tax-driven, uncommercial and unnecessary;
- does not reflect the realities of modern investment management in a commercial world that has seen very significant change since the regime was introduced in 1984;
- is incompatible with self-assessment principles;
- distorts the market and inhibits fair competition between onshore and offshore collective investment schemes and similar savings products;
- does not tax investors in a simple, clear, certain and effective way.

2.2 While still advocating the need for change, a small minority of respondents did however make supportive comments about the current regime, saying that it

- is relatively simple to operate;
- does not cause fund managers undue compliance burden;
- is efficient and does not lead to significant tax loss;

- does not confuse investors, nor in practice cause them significant difficulties, even when distributor status is settled after the deadline for submitting self-assessment tax returns.

3 Abolition of the offshore funds regime without replacement

Should the current regime be abolished? If so, how can additional compliance burdens for investors be avoided?

3.1 There was strong support for the general proposition that the offshore funds regime should be abolished. Most responses observed that the tax advantages identified in 1984 are now considerably narrower due to the closer alignment of income tax and capital gains tax rates.

3.2 Six responses advocated abolition without any need for a replacement regime. The remainder still supported abolition but with two main reservations.

- First, a significant number urged that the regimes for onshore and offshore funds should be aligned. They argued that removal of the offshore funds regime, whilst desirable in itself, would place UK funds at a disadvantage. Most favoured abolishing the tax charge on UK fund income that is rolled up, whilst only one suggested the opposite - taxing offshore fund income as it rolls up. Some went further and advocated a full review of the taxation of savings products.
- Second, respondents believed that the Government would want to take action to continue to protect tax revenues. They argued that the current regime at least offers relative certainty and ease of calculation. They were concerned that any alternative measures to protect tax revenues might be more difficult to operate.

3.3 A smaller number argued that abolition was possible, with only targeted anti-avoidance measures being necessary to address the issue of tax avoidance.

How can the use of particular types of offshore fund to convert income into capital gains be avoided?

3.4 A significant number of responses suggested that the consultation document asked the wrong question because the potential conversion of income into capital gains is no longer a significant problem. The responses split almost evenly into two groups.

- The first group argued that commercial drivers are far more important for investors than tax advantages, which are now seen as fairly minimal.
- The second group advocated aligning the regimes for UK and offshore funds, with the preference being to remove the tax charge on rolled-up income in UK funds. As a result there would be less need to counter the conversion of income to capital in offshore funds, although some recognised the case for retaining the current tax rules for UK bond funds, and some form of regime for their offshore equivalents to prevent deposit providers being put at a disadvantage.

3.5 The next most substantial set of responses advocated specific, targeted anti-avoidance measures. Some suggested that existing rules could be used or adapted.

4 *Reform of the offshore funds regime*

4.1 Most respondents agreed that at least some reform of the current rules was necessary. Responses ranged from options for minimum reform to the regime, to more radical and fundamental change, but within the framework of the existing provisions. There was, however, some concern that continuing a regime which in effect required distribution of income might leave ongoing conflicts with EC Law.

4.2 Respondents were generally opposed to investment restrictions as part of the tax rules. They argued that regulatory issues are for regulators, not tax authorities. There was strong opposition to the United Kingdom Equivalent Profits (UKEP) tests and clear support for taxation based on fund accounts. Most respondents proposed that, where there were umbrella arrangements, taxation should be determined on the basis of sub-funds or share classes rather than at the fund level. There was no support for a mark to market basis as a replacement for the Offshore Income Gain.

How can the current regime be improved to give investors greater certainty without affording special treatment to returns of offshore income or gains?

4.3 A number of respondents did not believe that investors had any real practical difficulties in reporting their income from offshore funds for self-assessment purposes. They argued that it was only in exceptional circumstances that a fund intending to operate as a distributing fund might fail to obtain that status. Only one respondent said that the interaction with self-assessment was one of the major complaints against the current regime.

4.4 A common theme for improvement was the granting of an advance "clearance" to funds seeking distributor status, or to have a category of permanently qualifying ("approved") funds, whose status would remain

unchanged during their lifetime, provided they made an annual self-assessment that appropriate criteria had been met. Any loss of status would only impact upon periods after the loss, or lead to a time apportionment of gains or deemed disposal of the holding. A number of respondents thought that some kind of “information reporting” regime could also provide greater certainty for investors, particularly if that could be coupled with a one-off advance clearance as an information provider (see also part 5).

4.5 A majority of respondents envisaged that, whatever improvements were made, there should remain in some form a distinction between qualifying and non-qualifying funds. A few advocated placing the onus upon investors to check the status of their fund before making entries on self-assessment tax returns. And they suggested that funds should, in some way, be obliged to inform investors of any change in their status.

Would making the application process for approval a part of the self-assessment regime be a welcome change?

4.6 Almost twice as many respondents felt that inclusion of approval applications within the self-assessment framework would be a welcome change compared with those who thought it would make no difference, would not be welcome or would not lead to any greater certainty for investors. The idea of advance clearance was seen by a number as being the most effective means of providing greater certainty for investors and minimising compliance burdens for fund managers. Several respondents advocated self-certification of status by funds.

Should the rules (regarding investment restrictions) be changed? If so, what changes should be made and how best could the interests of UK investors be protected?

4.7 By far the majority of respondents said that the investment restrictions test should either be removed or significantly changed. A common theme was that investment limits and investor safeguards are matters for regulators of the funds and not tax authorities. For funds marketed throughout Europe and which hold a UCITS (“Undertaking for Collective Investment in Transferable Securities”) passport, that level of regulation will impose restrictions on investment, ensuring a spread of risk. The UCITS Directive was not in place when the offshore funds regime was first introduced in 1984 and fund regulation has changed significantly since that time. Some considered that the rules should be relaxed to match those applicable to UK regulated funds, or more closely aligned with the UCITS Directive.

What safeguards would ensure that offshore funds were not put in a better position than their UK-based equivalents?

4.8 A common theme again was that investor safeguards should be matters for the regulator rather than the tax authorities. Reliance should be placed upon those regulatory standards. A number of respondents referred to UCITS Directive standards as suitable for EU funds.

4.9 However, some respondents rejected reliance solely on the UCITS Directive as this would not give the product flexibility required by fund managers wishing to sell both regulated and unregulated funds.

How far, and in what way, should the rules differentiate between regulated funds and funds that are unregulated (or practically so) in their home state?

4.10 Most respondents thought that there should be no distinction between regulated and unregulated funds for tax purposes. A small number of respondents thought that it should be possible to distinguish them, but that regulated funds should not be subject to more restrictions than those imposed by their regulator.

4.11 Indeed one view expressed was that only regulated funds should be subject to restriction - that imposed by their regulator - but that unregulated funds should not be subject to any investment restrictions. They should only be available to "sophisticated investors" who should possess sufficient expertise to guide them on risk.

Which current UKEP provisions (if any) cause fund managers difficulty? Why are they difficult?

4.12 A number of respondents questioned whether it was appropriate to retain UKEP as a test at all. Instead they suggested that greater reliance should be placed on the accounts of the fund drawn up in accordance with appropriate standards, such as UK General Accepted Accounting Practice (UK GAAP) or International Accounting Standards (IAS).

4.13 Particular points of concern mentioned were

- the need in some circumstances to distribute more than a fund's accounts income to satisfy the distribution test due to different treatment for accounting and tax purposes;
- the distinction between trading and investment income;
- uncertainty as to whether expenses deducted from income in the accounts would be allowable;
- application of the Accrued Income Scheme (AIS);
- the way in which the de-minimis test is applied;
- the border between income and chargeable gains;
- foreign exchange movements, option premiums and discounted securities;
- in the case of fund of funds, difficulties in taking account of the interests in a qualifying fund of a primary fund when applying the distribution test.

4.14 However, a few said that the UKEP test did not present any greater difficulties than UK funds faced in making their corporation tax computations.

How could they (the UKEP provisions) be modified?

4.15 A number of respondents suggested that closer alignment of the test with one based on the fund's accounts should be made. Other specific areas for modification suggested were

- replacement of the AIS with rules similar to those applied to the "loan relationships" of UK-authorized funds in the 2002 Finance Act;
- application of the derivative contract and foreign exchange rules for UK-authorized funds, also introduced in 2002;
- greater clarity about what is to be regarded as distributable income;
- statutory definition of "trading" income: for example, a "turnover of investments" limit below which trading would be deemed not to have taken place (though some respondents thought it was not possible to arrive at a definitive set of parameters in this area and that each case would need to turn on its own facts).

What reliance should be placed on the financial accounts of a fund, instead of a UKEP calculation, so that it might be easier for fund managers to comply with the regime while continuing to safeguard the Exchequer?

4.16 Of the responses to this question only one did not think that reliance should be placed upon accounts, on the grounds that the current requirement to produce a UKEP calculation provided a standard methodology that avoided the variations that different accounting standards could produce.

4.17 While considering that a test by reference to the fund's accounting measure of income was highly desirable, many respondents added the

proviso that these should be accounts prepared in accordance with UK GAAP or IAS or such like.

Should the rules be changed so that the distribution conditions for qualifying status need only be met at the sub-fund level?

Should the rules be changed to allow particular classes of interest within a single fund to qualify and others to be non-qualifying?

4.18 Many respondents saw the issue of umbrella fund structures as one of the key elements within the present regime requiring change. Some went further and suggested it as the most important aspect of the review. Only one respondent who commented did not specifically advocate change.

4.19 A clear majority of respondents were in favour of change to allow differentiation between classes of interest because of the economies of scale this would allow. It would then be possible to offer, from a single fund or sub-fund, classes of interest that met the differing demands of investors. Some however considered that recognition should only be at fund or sub-fund level. One provider suggested that allowing particular classes of interest to qualify could prove difficult to administer with another suggesting that it might lead to additional costs.

Are fund managers able to give some idea of the preferred rank order of any changes to the current regime that they would like to see?

4.20 The three changes to the current regime ranked as most important by respondents were

- abolition or significant reform of the investment restrictions test;
- abolition or significant reform of the UKEP test, in particular the closer alignment with fund accounts;

- allowing sub-funds, or share classes, to stand alone.

4.21 The next two changes in respondents' order of importance were

- compatibility with self-assessment or some form of self-certification,
- abolition of the requirement to distribute income.

Given the current difficulties we perceive with deferral of tax liabilities, what scope is there for investments in non-qualifying funds to be taxed on some form of a mark to market basis?

4.22 This question attracted as much comment as any other in the consultation document.

4.23 Respondents did not favour a mark to market basis of taxation for individuals. Among the reasons for this were that

- it would involve taxation of unrealised gains, a novel and unfair departure for individuals, without any current equivalent in UK taxation;
- it could give investors cash flow problems and force them to sell their investment purely to fund the tax;
- investors are not gaining significant advantage from their current ability to defer;
- it would be discriminatory and prevent managers selling certain types of fund;
- in particular it would disadvantage managers selling "alternative" collective investment schemes or "hedge funds";
- it would put extra compliance burdens on individuals, making it harder for them to complete their self-assessment returns accurately;
- it does not apply to other equivalent roll-up investments for individuals such as discounted securities or managed insurance bonds.

Are there alternatives which would address these difficulties?

4.24 A number of respondents suggested that a better approach to deferral, if that were perceived to be a problem, would be by means of targeted anti-avoidance measures. But the nature of these was not specified.

4.25 A majority of respondents also considered that the current regime of taxation of gains as income on realisation generated a sufficient tax charge on rolled-up income, which probably deters the majority of UK investors from investing in funds subject to those rules. Indeed one fund management group observed that they had not seen a demand from UK individual investors for offshore roll-up funds which, in their view, supported this contention.

4.26 Some respondents, however, argued that the tax system should ensure that investors are charged to capital gains tax on capital returns, and income tax on income returns. The current system was seen as unfair to the extent that it taxed capital returns as income. But a mark to market approach to non-qualifying funds would not resolve that.

5 Replacement of the Offshore Funds Regime

What are the merits and practicalities of imitating the tax rules for UK-authorized funds by adopting a parallel approach to investment in offshore funds and inviting those funds to join a similar form of information-providing regime?

5.1 The vast majority supported in principle the idea of imitating the tax rules for UK-authorized funds by adopting a parallel approach to investment in offshore funds and inviting those funds to join a similar form of information-providing regime. But two responses were totally opposed to funds having a tax status dependent upon their level of information disclosure.

5.2 The main objections concerned the method and nature of reporting taxable income. There was strong opposition to having to report a "UK tax-adjusted" figure – funds would have to acquire the necessary knowledge and would have to incur costs to amend systems. Some therefore argued against the proposal, while others made it a reservation in giving overall support.

5.3 Most of those who expressed a more detailed view advocated reliance on accounts figures although some observed that accounting standards might be an issue in certain jurisdictions.

5.4 There was general agreement that this form of regime would be preferable to the current position, where the tax legislation effectively forces funds to distribute in order to obtain more favourable tax treatment for investors.

Are there problems in principle or in practice with the taxation of income from investments in offshore funds regardless of whether or not the income has actually been received?

5.5 This issue generated a wide range of comment and opinions.

5.6 A small number said they saw no problem in principle with adopting this approach as it is already well established for UK funds. A similar number, on the other hand, considered it totally inappropriate on principle to tax income that has not been received.

5.7 But the majority of the responses concentrated more on the practical difficulties involved, such as

- cash flow for paying the tax;
- deriving an appropriate measure of income – in particular the treatment of profits which might on current principles be construed as “trading” income, a key issue for hedge funds;
- computational issues, for example the impact of in-year sales and purchases, and the treatment of any accrued income in any final gain on disposal.

5.8 One response observed that the cash outlay of tax on income from UK funds is mitigated at present by tax credits, but that this would not be the case for offshore funds.

Can or should the current UKEP rules be adapted for the purpose of establishing annual income arising from the fund?

5.9 Broadly, there was no appetite for importing UKEP rules into a new regime. Comment on the UKEP provisions is covered in 4.12-4.15.

What reliance could be placed on the financial accounts of a fund, instead of a UKEP calculation, so that it might be easier for fund managers to comply with a new regime while continuing to safeguard the Exchequer?

5.10 Respondents were generally supportive. Detailed comment on the use of accounts is covered in 4.16-4.17.

Where the beneficial owner is represented by a nominee, what particular practicalities are involved that would need to be taken account of if we were to link elements of tax treatment to the information obligations of the fund?

5.11 The majority of respondents outlined problems in identifying the beneficial owners. This was not an issue just confined to funds, but one also for bonds and equities, and other financial assets.

5.12 Opinion was split more or less evenly. One group proposed that information should be published to enable the unit holder to compute his income, with the duty placed on the unit holder to retrieve and use the information.

5.13 The opposite view was that specific information should be provided to the named holder registered with the fund. Nominees should be made responsible for passing it on, and so on, until it reached the ultimate beneficial owner.

5.14 Issue of simple "income per unit" data was preferred to the issue of vouchers. The former would more easily permit intermediaries to disaggregate and pass on the relevant information.

If the Revenue were to be able to confirm a fund as an 'information-provider', what would the clearance process entail and what assurances could be given?

5.15 This produced a wide range of comments. The largest number suggested that the clearance should be a one-off process, subject to a duty to inform the Revenue if circumstances changed.

5.16 Other views put forward advocated

- approval of the manager, not each fund;
- a presumption towards approval;
- publication of clear and simple rules, on a self-assessment basis.

5.17 However, two noted that a one-off process would need to be balanced against the possible impact of a Revenue audit, which might affect several previous years.

Given the current difficulties we perceive with deferral of tax liabilities, what scope is there for investments in funds that are not information-providers to be taxed on some form of a mark to market basis?

5.18 Mark to market again found no favour. Reasons for opposing such an approach are covered in 4.23.

5.19 Some respondents considered what mark to market rules should look like were they adopted. Proposals included:

- making mark to market movements subject to tax as capital gains, with the benefit of annual exemptions and taper relief;
- allowing unrealised and realised losses on the same type of investment to be available for unrestricted loss relief (i.e. carry back or forward, or relief in the year against gains on similar investments);
- spreading either gains or tax liabilities over a number of years, if either exceeded a defined level of a taxpayer's taxable income or tax liability;
- limiting any requirement to mark to market, at the investor's option, to every five years.

Are there alternatives which likewise would address these difficulties?

5.20 The vast majority supported retention of the Offshore Income Gain, but one advocated charging a higher rate, and two advocated better-targeted anti-avoidance rules.

5.21 A few responses suggested other alternatives such as

- imputing a “deemed amount” annually;
- the introduction of an optional regime, which would allow investors to elect to be taxed under current rules even if the fund provided information, or to be taxed according to the new, information provision rules even if the fund itself had not been cleared as an information provider (in the latter case the investors would provide the information).

How might a new regime be ‘incentivised’ for investors?

5.22 The vast majority opposed incentives, mainly on the grounds of commercial and economic factors. One mentioned possible discrimination.

5.23 Two suggested a lower rate for income from funds that met certain conditions, and one proposed a form of tax credit.

Are there any general or specific points that can be made about the regulatory impacts of a replacement, information-providing regime?

5.24 A small number commented, the main points being:

- the approval process should be one-off;
- information should be limited to that required for other purposes;
- there should be certainty in the system.

Is it possible to make any estimate of the costs and benefits to fund managers of change to an information-providing regime?

5.25 Many did not comment. Those that did anticipated short-term costs of changing systems, which would be outweighed by the benefit of being able to rationalise their fund structures.

5.26 One respondent put its changeover costs at US\$50,000 and also added that there would be costs in rationalising and marketing any new fund structures.

What kind of transitional period would be necessary if a new regime were implemented?

5.27 There was a mix of views on timing, some proposing the next tax year following the one in which the legislation was passed, and some arguing for a further 12 months after that.

5.28 The consensus was that as clean a break as possible should be achieved to avoid the costs of different regimes running together. The favoured option was to compute a deemed disposal on the date of change, but defer it until the time of an actual disposal.

5.29 On transition generally, various representations referred to the importance of ensuring that transitional provisions operated fairly for all types of investors and funds.

6 *Summary of Responses raising other specific issues*

Representations also covered the following points:

- the need to review other areas where anomalies arise such as the treatment of unauthorised unit trusts, particularly property schemes;
- the interaction between the offshore funds regime in its present form and other corporation tax provisions (for example, the life insurance provisions in section 212 TCGA 1992 and the controlled foreign company rules);
- clarification of the scope of the charge in the case of foreign partnerships;
- more generally, a definition of offshore fund to be introduced independent of the FSMA 2000 definition.

Appendix

The Current Offshore Funds Tax Regime

i) The UK offshore funds regime was introduced in 1984 and since then only relatively minor changes have been made to it. It governs the taxation of all UK-resident investors in overseas collective investment schemes, or 'offshore funds' as the legislation describes them.

ii) Broadly, its purpose is to counter the use of particular types of fund to convert income flows into capital gains. Prior to its introduction, a UK-resident investor could accumulate income in a particular type of offshore fund and, when the investment was realised, be subject only to capital gains tax rather than having to pay income tax on the accumulating (or "rolled up") income. In 1984 the differences between capital gains tax and income tax were significant, and while there has been some convergence since then, the capital gains tax rules remain more generous to this day.

iii) The offshore funds regime introduced the concept of 'qualifying' and 'non-qualifying funds'. Corporate taxpayers apart, investors in a qualifying fund are subject to income tax on income arising from the fund; and to capital gains tax on any gain they realise when they dispose of their interests in the fund. This broadly matches the treatment of investments in an equivalent UK fund.

iv) However, investors in non-qualifying funds are subject to income tax when they make a disposal. This is the so-called "Offshore Income Gain". No distinction is made between the income and capital accumulated in the fund. The purpose of the regime is to set aside the legal form of the realisation (disposal of an asset) and treat any realised gain as income.

v) In order to secure approval as a qualifying fund, and capital gains treatment for UK-resident investors on the disposal of their investments, the fund must make an application to the Inland Revenue for 'distributor' status. To be successful the fund must show that it has satisfied a range of conditions relating to the accounting period for which approval is sought.

vi) Broadly, the key conditions are that the fund must be able to demonstrate that it has

- distributed 85% (or more) of its income for each period or, if a higher figure, 85% or more of its UK equivalent profits (UKEP);
- met particular investment restrictions (which broadly equate to the regulations in place for authorised unit trusts in 1984).

vi) UKEP are broadly the amounts which would have been chargeable to corporation tax were the fund a UK resident company, though there are a number of special rules including the exemption of chargeable gains.

vii) Approval is only given retrospectively and must be applied for and obtained for each and every period of account for which it is required. UK-resident investors will only be able to obtain capital gains tax treatment for their holdings if the fund in which they have invested has met all the conditions for approval throughout their period of investment.

viii) The same distinction between qualifying and non-qualifying funds may impact upon the taxation of companies. Though, by contrast, they pay corporation tax on their income and capital gains alike, capital treatment may still be advantageous to them and the legislation seeks to remove that advantage if their investment is in a non-qualifying fund. There are also rules for particular types of holding or companies which may lead to different treatment. For example, certain investments may fall within the separate set

of rules that govern the taxation of 'loan relationships'. There are also specific provisions for life insurance companies.

ix) Where a fund is constituted as an umbrella fund, the fund as a whole and each class of interest in it must satisfy the required conditions before the fund can be approved as qualifying.

x) Currently in excess of 600 funds each year are seeking and obtaining qualifying status compared to around 400 funds ten years ago. Many of them are established in well-known fund management centres such as Luxembourg, Dublin and the Channel Islands.