

## **Community investment tax relief**

### ***Overview***

1. This Part provides for community investment tax relief, that is corporation tax reductions for companies which invest in community development finance institutions (CDFIs). It is based on Schedule 16 to FA 2002.

2. Schedule 16 to FA 2002 as enacted also provided for community investment tax relief for individuals who invest in CDFIs by way of reduction of income tax. Relief for individuals has been rewritten in Part 7 of ITA. This Part of this Bill largely mirrors Part 7 of ITA.

3. Schedule 1 to ITA has inserted sections 151BA, 151BB and 151BC in TCGA, replacing paragraphs 40 and 41 of Schedule 16 to FA 2002 and, so far as they apply for the purposes of capital gains tax or corporation tax on chargeable gains, paragraphs 47 and 48(2) of that Schedule. Those sections of TCGA accordingly apply in relation to community investment tax relief for both individuals and companies.

4. The commentary uses a number of abbreviations. They are listed below.

FA 2000      Finance Act 2000 (and similarly for other Finance Acts)

HMRC        Her Majesty's Revenue and Customs

ICTA         the Income and Corporation Taxes Act 1988

ITA          the Income Tax Act 2007

TCGA        the Taxation of Chargeable Gains Act 1992.

## **Chapter 1: Introduction**

### ***Overview***

5. This Chapter quantifies the tax reduction potentially available to a company, labels certain concepts and provides signposts to material contained elsewhere.

### **Clause 1: Meaning of "CITR"**

6. This clause sets out a general description of the nature of the relief, an entitlement to tax reductions, and defines it as "CITR". It is new.

### **Clause 2: Eligibility for CITR**

7. This clause summarises the general conditions which need to be met for a company ("the investor") to be eligible for CITR. It is based on paragraph 1 of Schedule 16 to FA 2002.

8. *Subsection (1)(a)* requires that, for an investment in a CDFI to qualify for CITR, the CDFI must be accredited under Chapter 2 of Part 7 of ITA.

9. Chapter 2 of Part 7 of ITA provides that accreditation is to be made by the Secretary of State, sets out the criteria for accreditation, contains powers to determine the manner of making applications and the terms and conditions of accreditation, and authorises delegation of the Secretary of State's functions. These functions have been assigned to the Secretary of State for Business, Enterprise and Regulatory Reform.

10. Section 340(2)(b) in Chapter 2 of Part 7 of ITA contains power for the Treasury to make regulations. Under the predecessor of that power in paragraphs 4 and 5 of Schedule 16 to FA 2002, the Treasury have made the Community Investment Tax Relief (Accreditation of Community Development Finance Institutions) Regulations 2003 (SI 2003/96).

11. Regulations may make different provision for bodies whose principal objective in providing finance is to invest in enterprises whose business does not consist of financing other enterprises or does so only to the extent permitted by the regulations. If such a body is accredited, it is designated as a retail community development finance institution (a "retail CDFI"). See the commentary on section 340 of ITA in the Explanatory Notes to that Act.

12. The distinction between a retail CDFI and an accredited CDFI which is not a retail CDFI (a "wholesale CDFI") is relevant to the limits on the total value of investments which a CDFI can make for an accreditation period and which are set out in section 348(4) of ITA and clause 12(4) of this Bill. SI 2003/96 provides different limits on the value of investments which a retail CDFI and a wholesale CDFI may make in any enterprise.

13. Paragraph 4 of Schedule 16 to FA 2002, as substituted by ITA, provides that Chapter 2 of Part 7 of ITA applies for the purposes of Schedule 16 to FA 2002, contains signposts to the provisions of that Chapter and defines "accreditation period". Accreditation period is now defined in clause 12(10) and, as a consequence of the direct references to Chapter 2 of Part 7 of ITA in subsection (1)(a) and elsewhere in this Part, it is unnecessary to rewrite the remainder of paragraph 4. The result, however, remains the same, that there is only one set of provisions relating to accreditation for both income tax and corporation tax purposes.

### **Clause 3: Form and amount of CITR**

14. This clause specifies the amount of the corporation tax reduction available and the accounting periods for which it may be claimed. It is based on paragraph 20 of Schedule 16 to FA 2002.

15. The provision in paragraph 20(2)(b) of Schedule 16 to FA 2002 (limiting the tax reduction to the amount which reduces the investor's tax liability to zero) has not been included in this clause. *Subsection (2)* is expressed simply in terms that the investor is entitled to a tax reduction for the relevant accounting period of 5% of the amount invested. The provision limiting the tax reduction is expected to be included in the Chapter of this Bill dealing with the calculation of corporation tax liability.

**Clause 4: Meaning of “making an investment”**

16. This clause provides that an investment in a CDFI may take the form of a loan or an issue of securities or shares. It is based on paragraph 2 of Schedule 16 to FA 2002.

**Clause 5: Determination of “the invested amount”**

17. This clause sets out rules for determining the amount invested for the purposes of clause 3. It is based on paragraph 21 of Schedule 16 to FA 2002. In particular, it deals with the complications which arise where a loan may be drawn down in tranches, by requiring the average capital balance of the loan in relation to the accounting period to be calculated.

**Clause 6: Meaning of “the 5 year period” and “the investment date”**

18. This clause provides the definitions of two significant terms. It is based on paragraph 3 of Schedule 16 to FA 2002. “The 5 year period”, which begins with “the investment date”, is the period during which conditions as to the repayment or redemption of the investment are imposed.

**Clause 7: Overview of other Chapters of Part**

19. This clause indicates the subject matter of the Chapters of this Part not previously mentioned in Chapter 1. It is new.

**Chapter 2: Qualifying investments**

*Overview*

20. This Chapter sets out the conditions which must be met if an investment is to be a qualifying investment.

**Clause 8: Qualifying investments: introduction**

21. This clause introduces:

- the respective conditions which apply to loans (clause 9), to securities (clause 10) and to shares (clause 11); and
- the provisions which apply to all kinds of investment (clauses 12 and 13).

It is based on paragraph 8 of Schedule 16 to FA 2002.

**Clause 9: Conditions to be met in relation to loans**

22. This clause sets out the three conditions applicable to loans. It is based on paragraph 9 of Schedule 16 to FA 2002.

**Clause 10: Conditions to be met in relation to securities**

23. This clause sets out the two conditions applicable to securities. It is based on paragraph 10 of Schedule 16 to FA 2002.

24. Condition A (*subsection (1)*) requires that securities must be subscribed for wholly in cash and fully paid for on the investment date. It is in similar terms to clause 11(1) which sets out identical requirements in relation to shares.

25. Clause 11(3) (based on paragraph 11(1) of Schedule 16 to FA 2002) provides that shares are not fully paid up for the purposes of clause 11(1) if there is any undertaking to pay cash to the CDFI at a future date in connection with the acquisition of the shares. The effect of this is to distinguish the meaning of “paid up” for that purpose from the meaning of those words for the purposes of the Companies Acts. Section 738(2) of the Companies Act 1985, and section 583 of the Companies Act 2006 which will supersede it, both provided that a share is deemed paid up in cash, or allotted for cash, if the consideration for the allotment or payment up is an undertaking to pay cash to the company at a future date.

26. There is no similar provision in the Companies Acts applicable to the issue of securities, but the position in relation to securities has been made explicit by the inclusion of *subsection (3)*, equivalent to clause 11(3). This clarification is not a change in either law or practice.

27. Respondents to consultation on the rewriting of paragraph 10 of Schedule 16 to FA 2002 for income tax purposes in ITA agreed with the inclusion of section 346(3) of that Act in similar terms. We have, however, slightly recast the provision in subsection (3) to make clear that the reference is to “fully paid for” rather than as in section 346(3) to “fully paid”. We propose to amend section 346(3) of ITA to conform (see Schedule 1).

**Q1. We welcome comments on the proposal to include clause 10(3) in relation to securities in similar terms to clause 11(3) in relation to shares.**

**Clause 11: Conditions to be met in relation to shares**

28. This clause sets out the two conditions applicable to shares. It is based on paragraph 11 of Schedule 16 to FA 2002.

**Clause 12: Tax relief certificates**

29. This clause sets limits on the value of investments in respect of which a CDFI may issue tax relief certificates in an accreditation period. It is based on paragraph 12 of Schedule 16 to FA 2002. Without a tax relief certificate, an investor may not claim CITR (see clause 3(5)(b)).

30. *Subsections (2) and (3)* provide that the limit applies to the total value of investments in the CDFI made in the accreditation period by companies under this Part and by individuals under Part 7 of ITA.

31. *Subsection (4)* provides different amounts for the limits for retail and wholesale CDFIs. See the commentary on clause 2.

32. *Subsections (6) and (7)* provide for the substitution of different amounts by Treasury order for the amounts in subsection (4). Subsection (7) is based on paragraph 12(5) of Schedule 16 to FA 2002 which provides that:

Any such substitution shall have effect in relation to such accreditation periods as may be specified in the order; and those periods may, if the substitution increases the amount for the time being specified in sub-paragraph (2), include periods beginning before the order takes effect.

33. Subsection (7) corrects two infelicities in the source legislation. For “the amount” it substitutes “an amount” to avoid any doubt that the power to apply an increase retrospectively can be exercised if one only of the amounts in subsection (4) is increased. For “the order takes effect” it substitutes “the order comes into force”. The wording in the source legislation could be misconstrued as referring to the time when the order is itself made. The substituted wording clarifies that the intended meaning is the time when the provisions of the order come into force. The opportunity is being taken to make the same clarifications in section 348(7) of ITA (see Schedule 1).

34. In *subsection (8)*, the words “wholly or partly”, which appear before “in contravention” in paragraph 12(6) of Schedule 16 to FA 2002, have been omitted as being unnecessary. Respondents to consultation on the rewriting of paragraph 12 of Schedule 16 to FA 2002 for income tax purposes in ITA agreed with the omission of these words in section 335(8) of that Act.

**Q2. We welcome comments on the proposal to omit the words “wholly or partly” from clause 12(8).**

**Clause 13: No pre-arranged protection against risks**

35. This clause is an anti-avoidance provision concerned with ensuring that the investor is subject to all usual investment risks and is not protected from their effect by insurance, indemnity, guarantee or other means. It is based on paragraph 13 of Schedule 16 to FA 2002.

36. In *subsection (3)* “transactions or series of transactions” has been added to the illustrative list of matters which are included within the term “arrangements”. The change from the source legislation is one of presentation rather than of substance.

37. It is intended that, in clauses such as this, the definition of “arrangements” will adopt this same form of words. We will in due course consider whether this definition of “arrangements” could be located at the end of this Bill so that it applies for the purposes of this Bill as a whole. If we adopt this course, then the specific definition of “arrangements” in this clause will be removed.

### **Chapter 3: General conditions**

#### **Overview**

38. This Chapter contains various general conditions to be met by the investor. It is based on Part 4 of Schedule 16 to FA 2002.

#### **Clause 14: No control of CDFI by investor**

39. This clause provides that the investor will not qualify for CITR in relation to an investment if the investor or a person connected with the investor controls the CDFI at any time in the 5 year period. It is based on paragraph 14 of Schedule 16 to FA 2002.

40. The legal structure of a CDFI may take a number of forms. It may be a company or some other form of body corporate or it may be a partnership or some other form of unincorporated association. The different meanings of control needed to deal with the possible different forms of a CDFI's constitution are set out in *subsections (3) to (6)*.

#### **Clause 15: Investor must have beneficial ownership**

41. This clause provides that the investor must be the sole beneficial owner of the investment. It is based on paragraph 15 of Schedule 16 to FA 2002. Trustees and joint investors are thus precluded from obtaining CITR. But see clause 41 which enables investments to be made by a nominee or a bare trustee for a company.

#### **Clause 16: Investor must not be accredited**

42. This clause prevents a CDFI claiming CITR in respect of an investment in another CDFI. It is based on paragraph 16 of Schedule 16 to FA 2002.

#### **Clause 17: No acquisition of share in partnership**

43. This clause provides that an investor cannot obtain CITR for capital contributed to a CDFI which is a partnership, including loan capital accounted for as partners' capital. It is based on paragraph 17 of Schedule 16 to FA 2002.

#### **Clause 18: No tax avoidance purpose**

44. This clause denies CITR if the investment is part of a scheme or arrangement the main purpose or one of the main purposes of which is the avoidance of tax. It is based on paragraph 18 of Schedule 16 to FA 2002.

### **Chapter 4: Limitations on claims and attribution**

#### **Overview**

45. This Chapter is based on Part 5 of Schedule 16 to FA 2002 other than paragraphs 20 and 21. Clauses 3 and 5 in Chapter 1 are based on those two paragraphs.

**Clause 19: Loans: no claim after disposal or excessive repayments or receipts of value**

46. This clause prevents a claim being made for any accounting period in respect of an investment by way of loan in certain circumstances. It is based on paragraph 22 of Schedule 16 to FA 2002. This clause links to the provisions in clauses 26, 28 and 29 which provide for a tax reduction already given to be recaptured in similar circumstances.

**Clause 20: Securities or shares: no claim after disposal or excessive receipts of value**

47. This clause sets out two conditions to be met before a claim can be made for any accounting period in respect of a subscription for securities or shares. It is based on paragraph 23 of Schedule 16 to FA 2002.

48. The first condition (*subsection (1)*) is that the investor has not disposed of the securities or shares before the first anniversary of the investment date which occurs after the end of the accounting period.

49. The second condition (*subsection(2)*) is that the investor has not received or is not treated as having received value from the CDFI in excess of the limits allowed under clause 30.

**Clause 21: No claim after loss of accreditation by the CDFI**

50. This clause provides that no claim may be made if the CDFI ceases to be accredited. It is based on paragraph 24 of Schedule 16 to FA 2002.

51. Depending on the investment date and the date upon which the CDFI ceased to be accredited, this clause may prevent a claim being made for the accounting period before that in which the CDFI ceased to be accredited (see *subsections (2) to (4)*).

52. Subsections (2) to (4) unpack paragraph 24(2) of Schedule 16 to FA 2002 in order to make its various elements clearer. We propose to take the opportunity also to make section 356(2) of ITA clearer by unpacking it in the same way (see Schedule 1).

**Q3. We welcome comments on the proposal to unpack paragraph 24(2) of Schedule 16 to FA 2002 and section 356(2) of ITA.**

**Clause 22: Accreditation of investor**

53. This clause provides that no claim may be made if the investor becomes accredited as a CDFI. It is based on paragraph 25 of Schedule 16 to FA 2002. This clause has no equivalent in Part 7 of ITA as an individual cannot be a CDFI.

54. Depending on the investment date and the date upon which the investor becomes accredited, this clause may prevent a claim being made for the accounting period before that in which it became accredited (see *subsections (2) to (4)*).

55. Subsections (2) to (4) unpack paragraph 25(2) of Schedule 16 to FA 2002 in the same way that clause 21(2) to (4) unpack paragraph 24(2) of that Schedule.

**Q4. We welcome comments on the proposal to unpack paragraph 25(2) of Schedule 16 to FA 2002.**

**Clause 23: Attribution: general**

56. This clause sets out the general rules dealing with the attribution to the loan, securities or shares included in the investment of the reduction in the investor's corporation tax liability for any accounting period made as a result of the investor's entitlement to CITR. It is based on paragraph 26(1) to (4), (7) and (8) of Schedule 16 to FA 2002.

57. Attribution is required for the purpose of determining the amount of the tax reduction which must be withdrawn or reduced in accordance with Chapter 5 of this Part.

**Clause 24: Attribution: bonus shares**

58. This clause sets out additional rules relating to attribution, to deal with the consequences of an issue of "corresponding bonus shares" (see *subsection (4)*) to the investor in respect of the original shares included in the investment. It is based on paragraph 26(5) and (6) of Schedule 16 to FA 2002.

**Chapter 5: Withdrawal or reduction of CITR**

***Overview***

59. This Chapter sets out the circumstances in which CITR attributable to an investment for any accounting period must be reduced to nil (withdrawn) or reduced proportionately. It is based on Part 6 of Schedule 16 to FA 2002.

**Clause 25: Overview of Chapter**

60. This clause provides an overview of the Chapter and contains signposts to its principal provisions. It is new.

61. *Subsection (3)* defines the term, "the 6 year period". This new term replaces the term "the period of restriction" defined in the same way in paragraph 33 of Schedule 16 to FA 2002. The 6 year period is relevant to clauses 29 and 30 which deal with receipts of value. As an anti-avoidance measure, receipts of value in the year before the investment date are taken into account, as well as those in the 5 year period, which begins with the investment date. See the commentary on clause 6 for the meaning of "the 5 year period" and "the investment date".

**Clause 26: Disposal of loan during 5 year period**

62. This clause provides that the CITR attributable to a loan must be withdrawn if, within the 5 year period, the investor disposes (otherwise than by receiving repayment) of part of the loan or, unless it is by way of a permitted disposal, of the whole of the loan. It is based on paragraph 28 of Schedule 16 to FA 2002.

63. A permitted disposal is defined in *subsection (2)*. If the disposal is a permitted disposal, any tax reduction already obtained is not withdrawn, but no further tax reduction may be claimed (see clauses 3(6) and 19).

**Clause 27: Disposal of securities or shares during 5 year period**

64. This clause provides for the withdrawal or reduction of CITR attributable to securities or shares, if the investor disposes of the whole or part of the investment in the securities or shares (except upon repayment, redemption or repurchase by the CDFI) within the 5 year period and the CDFI is accredited at the time of the disposal. It is based on paragraph 29 of Schedule 16 to FA 2002.

65. *Subsections (2) and (3)* provide for different consequences depending upon whether the disposal is a qualifying disposal.

66. *Subsection (4)* defines what is a qualifying disposal. It is based on paragraph 29(4) of Schedule 16 to FA 2002 with the omission of the words “for full consideration” in paragraph (a). See *Change 625* in Annex 1. Respondents to consultation on the rewriting of paragraph 29 of Schedule 16 to FA 2002 for income tax purposes in ITA agreed with the omission of these words in section 361(4)(a) of that Act.

<p><b>Q5. We welcome comments on the proposal to omit the words “for full consideration” in clause 27(4)(a).</b></p>
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67. There is inconsistency of language between paragraph 29(3) and (5) of Schedule 16 to FA 2002 which refer to CITR being attributable **for** an or any accounting period and paragraph 26(1)(b) of that Schedule (rewritten in clause 23(1)) which defines references in that Schedule to “CITR attributable ... **in respect of** an accounting period”. We propose to correct this by substituting “in respect of” in *subsections (3) and (5)*. We also propose to amend section 361(3) and (5) of ITA to correct the similar inconsistency (see Schedule 1).

68. *Subsection (5)* provides for circumstances where 5% of the invested amount is greater than the corporation tax liability of the investor for the accounting period.

**Clause 28: Repayment of loan capital during 5 year period**

69. This clause provides for the circumstances in which the CITR attributable to a loan must be withdrawn as a consequence of a repayment other than a “non-standard” repayment (see *subsections (3) to (5)*). It is based on paragraph 30 of Schedule 16 to FA 2002.

**Clause 29: Value received by investor during 6 year period: loans**

70. This clause applies if the investment consists of a loan and the investor or a person connected with the investor receives any value, other than an amount of insignificant value (as defined in *subsection (5)*), from the CDFI or a person

connected with the CDFI in the 6 year period. It is based on paragraph 31 of Schedule 16 to FA 2002.

71. *Subsection (2)* provides that, if value is so received, the invested amount (see clause 5) is adjusted by the amount treated as repaid and the investor is treated as having received a repayment other than a non-standard repayment for the purposes of clause 28 (see *subsection (4)*).

72. In subsection (5) we have added the words “of value” after “means an amount”. This conforms the language of this subsection with that of clauses 30(4), 31(4) and 35(4). We also propose to make the same addition in section 363(5) of ITA (see Schedule 1).

**Clause 30: Value received by investor during 6 year period: securities or shares**

73. This clause applies if the investment consists of securities or shares and the investor or a person connected with the investor receives any value, other than an amount of insignificant value (as defined in *subsection (4)*), from the CDFI or a person connected with the CDFI in the 6 year period. It is based on paragraph 32 of Schedule 16 to FA 2002.

74. *Subsection (2)* provides that, if value is so received and its amount wholly or partly exceeds the permitted level (see *subsection (3)*) by more than an amount of insignificant value, the CITR attributable to the investment must be withdrawn.

**Clause 31: Receipts of insignificant value to be added together**

75. This clause applies at a time when the investor receives value, if the investor has also received value earlier in the 6 year period and the total amount of the value received earlier was of insignificant value. It is based on paragraph 34 of Schedule 16 to FA 2002.

76. The amount of the receipt in question is to be added to the amounts of value previously received. If the total value of the amounts received is not an amount of insignificant value, the total value is treated as received at that time for the purposes of this Part, including in particular clauses 28, 29 and 30.

77. *Subsection (8)* is new. It provides that this clause is subject to clause 34 which modifies the effect of this clause and of clauses 29, 30 and 35.

78. Clauses 29(7) and 30(5) already provide that those clauses are subject to clause 34. Subsection (8) of this clause and new subsection (5) of clause 35 (see the commentary on that clause) have been added to ensure consistency. Schedule 1 provides for identical provisions in relation to section 368 of ITA to be added to sections 365 and 369 of that Act to ensure the same consistency in Part 7 of ITA.

<p><b>Q6. We welcome comments on the addition of subsections (8) of clause 31 of this Bill and of section 365 of ITA</b></p>
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**Clause 32: When value is received**

79. This clause explains when value is received. It is based on paragraph 35 of Schedule 16 to FA 2002.

80. In *subsection (1)(d)(i)*, as in section 366(1)(d) of ITA, the singular “associate” is used in place of the plural “associates” in paragraph 35(1)(d)(i) of Schedule 16 to FA 2002. Similarly in *subsection (1)(d)(ii)* the singular “a director or employee” is used instead of the plural “directors or employees” in paragraph 35(1)(d)(ii) of that Schedule.

**Clause 33: The amount of value received**

81. This clause determines the respective values received in relation to the respective transactions listed in paragraphs (a) to (g) of clause 32(1). It is based on paragraph 36 of Schedule 16 to FA 2002.

82. To give clarity, *subsection (1)* sets out the values against the paragraphs of clause 32(1) in tabular form.

83. In a case falling within clause 32(1)(d)(ii), the table permits the deduction of consideration which is given by a director or employee or an associate of a director or employee, in addition to consideration given by the investor or any associate of the investor. See *subsection (2)* and *Change 650* in Annex 1.

**Q7. We welcome comments on the proposal to permit, in a case falling within clause 32(1)(d)(ii), the deduction of consideration given by a director or employee or an associate of a director or employee for a benefit or facility provided by the CDFI.**

**Clause 34: Value received if there is more than one investment**

84. This clause provides that, if there is more than one investment, any value received is to be apportioned among the investments according to the respective amounts invested and sets out how those amounts are to be calculated. It is based on paragraph 37 of Schedule 16 to FA 2002.

85. A minor wording change has been made in *subsection (1)(c)* for the sake of clarity. For “falls” there is substituted “is received”. Schedule 1 makes the same clarificatory amendment in section 368 of ITA.

**Clause 35: Effect of receipt of value on future claims for CITR**

86. This clause applies if an investor holding securities or shares receives value (other than an amount of insignificant value) but, because that value is less than the permitted level, the CITR attributable to those securities or shares is not withdrawn under clause 30. It is based on paragraph 38 of Schedule 16 to FA 2002.

87. *Subsection (2)* reduces the amount invested (see clause 5) in respect of which CITR may be claimed for the accounting periods specified in *subsection (3)*.

88. *Subsection (5)* is new. It provides that this clause is subject to clause 34 which modifies the effect of this clause and of clauses 29, 30 and 31.

89. Clauses 29(7) and 30(5) already provide that those clauses are subject to clause 34. Subsection (5) of this clause and new subsection (8) of clause 31 (see the commentary on that clause) have been added to ensure consistency. Schedule 1 provides for identical provisions in relation to section 368 of ITA to be added to sections 365 and 369 of that Act to ensure the same consistency in Part 7 of ITA.

**Q8. We welcome comments on the addition of subsections (5) of clause 35 of this Bill and of section 369 of ITA**

**Clause 36: Receipts of value by or from connected persons**

90. This clause extends the meaning of “the investor” and “the CDFI” in clauses 29 to 35. It is based on paragraph 39 of Schedule 16 to FA 2002.

91. The words “if the context permits” have been added in this clause. These words, which do not appear in paragraph 39 of Schedule 16 to FA 2002, do not change the law. They make clauses 29 to 35 clearer, by stating explicitly what is implicit in the source legislation.

**Clause 37: CITR subsequently found not to have been due**

92. This clause provides the basis for making an assessment under clause 38 in cases where a claim for a tax reduction has been incorrectly allowed. It is based on paragraph 27 of Schedule 16 to FA 2002.

**Clause 38: Manner of withdrawal or reduction of CITR**

93. This clause authorises the making of assessments to recapture CITR attributable to an investment which has been withdrawn or reduced. It is based on paragraph 27 of Schedule 16 to FA 2002.

94. Paragraph 27(4) of Schedule 16 to FA 2002 is expected to be consequentially amended by Bill 5 to omit the words “under Case VI of Schedule D”.

**Chapter 6: Supplementary and general**

***Overview***

95. This Chapter contains miscellaneous provisions and definitions applicable to Part 7.

**Clause 39: Information to be provided by the investor**

96. This clause imposes obligations on the investor to notify an officer of Revenue and Customs of events giving rise to the withdrawal or reduction of any CITR attributable to a loan or any securities or shares. It is based on paragraph 42 of Schedule 16 to FA 2002.

97. There is inconsistency of language between paragraph 42(1)(b) of Schedule 16 to FA 2002 which refers to CITR being attributable **for** any accounting period and paragraph 26(1)(b) of that Schedule (rewritten in clause 23(1)) which defines references in that Schedule to “CITR attributable ... **in respect of** an accounting period”. We propose to correct this by substituting “in respect of” in *subsection (1)(b)*. We also propose to amend section 373(1)(b) of ITA to correct the similar inconsistency (see Schedule 1).

**Clause 40: Disclosure**

98. This clause authorises disclosure of information between HMRC and the Secretary of State for the purpose of discharging their respective functions under this Part. It is based on paragraph 43 of Schedule 16 to FA 2002.

**Clause 41: Nominees**

99. This clause allows for loans, securities or shares to be acquired, held and disposed of by nominees or bare trustees. It is based on paragraph 44 of Schedule 16 to FA 2002.

**Clause 42: Application for postponement of tax pending appeal**

100. This clause ensures that the investor cannot claim to postpone any payment of tax under section 55 of TMA on the grounds that the investor is eligible for CITR unless a claim has actually been made. It is based on paragraph 45 of Schedule 16 to FA 2002.

**Clause 43: Identification of securities or shares on a disposal**

101. This clause provides rules for the identification of the securities or shares disposed of for the purposes of this Part. It is based on paragraph 47 of Schedule 16 to FA 2002.

**Clause 44: Meaning of “issue of securities or shares”**

102. This clause provides definitions, in relation to a body, of an issue of securities or shares by that body and, in relation to a company, of an issue of securities or shares to that company. It is based on paragraph 46 of Schedule 16 to FA 2002.

**Clause 45: Meaning of “disposal”**

103. This clause defines “disposal”. It is based on paragraph 48 of Schedule 16 to FA 2002.

**Clause 46: Construction of references to being “held continuously”**

104. This clause explains what is meant by “held continuously”, for the purposes of those clauses of this Part which require the investment to have been “held continuously” by the investor during a specified period (see for example clauses 30 and 35). It is based on paragraph 49 of Schedule 16 to FA 2002.

**Clause 47: Meaning of “associate”**

105. This clause provides a definition of associate which is relevant to clauses 32 and 33. It is based on paragraph 50 of Schedule 16 to FA 2002.

**Clause 48: Minor definitions etc**

106. This clause explains various terms used in this Part. It is based on paragraph 51 of Schedule 16 to FA 2002.

107. With the exception of “body”, the terms defined in paragraph 51(1) of Schedule 16 to FA 2002 have been omitted, as they are either no longer required or are defined generally for the purposes of this Bill.

108. A definition of “bonus shares” has been added in *subsection (1)*. This definition was added in section 382(1) of ITA to ensure consistency between Parts 5 and 7 of ITA. The addition in clause 48(1) of the defined term (which is used in clause 24) ensures consistency with Part 7 of ITA.

109. In *subsection (2)*, which determines when shares are to be treated as being of the same class, for the words “if dealt with on the Stock Exchange” in paragraph 51(2) of Schedule 16 to FA 2002 there are substituted the words:

if they were —

- (a) included in the official UK list and
- (b) admitted to trading on the London Stock Exchange.

See section 1005 of ITA as applied for corporation tax purposes by section 841 of ICTA for the meaning of “included in the official UK list”.

110. The words used in paragraph 51(2) of Schedule 16 to FA 2002 have been in wide use in tax legislation from a time when the London Stock Exchange only operated a single market. The reference to the Stock Exchange is accordingly to be taken as a reference to the requirements of the London Stock Exchange in relation to shares traded on the main market, rather than on AIM or any other platform. The substituted words are intended to preserve and clarify the meaning of the source legislation and do not change the law.

**Q9. We welcome comments on the proposed substitution in clause 48(2).**

111. Paragraph 51(3) of Schedule 16 to FA 2002, which applies section 839 of ICTA (connected persons) for the purposes of that Schedule, has been omitted. This Bill will include a clause defining connected persons for the purposes of the Corporation Tax Acts, based on section 839 of ICTA, and a further clause applying that definition generally for the purposes of this Bill.

## Schedule 1

### Part 1: Other enactments

#### Finance Act 2000

#### Schedule 15

112. Schedule 15 to FA 2000 (Corporate venturing scheme) makes provision (see paragraph 1) for:

- (a) relief against corporation tax (“investment relief”) on amounts subscribed by companies for shares (see this Part and Parts II to VI of this Schedule);
- (b) relief against income of companies for losses on disposals of shares to which investment relief is attributable (see Part VII of this Schedule); and
- (c) the postponement of certain chargeable gains of companies where the gains are reinvested in shares to which investment relief is attributable (see Part VIII of this Schedule).

113. Schedule 15 applies only in relation to shares issued on or after 1 April 2000 but before 1 April 2010 (see section 63(4) of FA 2000). For that reason, Schedule 15 is not being rewritten.

#### *Paragraphs 46(2) and 67(3)*

114. Part 6 of Schedule 15 provides for the withdrawal or reduction of investment relief on the disposal of “relevant shares” (as defined in paragraph 2). For the purposes of that Part, paragraph 46(2) lists four types of disposal including:

- (a) by way of a bargain made at arm’s length for full consideration.

115. One of the requirements for relief to be available under Part 7 of Schedule 15 on the disposal of shares to which investment relief is attributable is set out in paragraph 67(3):

- (3) The second requirement is that the disposal on which the loss is incurred must be a disposal of the kind described in paragraph (a), (b), (c) or (d) of paragraph 46(2).

116. *Change 625* proposes the omission of the words “for full consideration” from clause 27(2)(a) rewriting paragraph 29(4)(a) of Schedule 16 to FA 2002. It is also proposed, as referred to in *Change 625*, to omit those words when rewriting section 575(1)(a) of ICTA for the purposes of share loss relief in this Bill.

117. Paragraph 46(2)(a) of Schedule 15 to FA 2000 is the only other place in the Tax Acts where those words qualify the words “bargain made at arm’s length”. *Change 625*, therefore, also proposes their omission from paragraph 46(2)(a) for the purposes of both Part VI and Part VII of Schedule 15.

**Q10. We welcome comments on the proposal to omit the words “for full consideration” from paragraph 46(2)(a) of Schedule 15 to FA 2000.**

## **Income Tax Act 2007**

118. Schedule 1 makes two minor textual amendments to Part 7 of ITA, in addition to the amendments to sections 346, 348(7), 356, 361, 363, 365, 368, 369 and 373 to conform those provisions to the corresponding provisions of this Bill (see the commentary on clauses 10, 12, 21, 27, 29, 31, 34, 35 and 39).

## **Section 355**

119. The first textual amendment is to section 355(2) of ITA and corrects a typographical error in the description of section 364(1) of that Act.

## **Section 364**

120. The second textual amendment removes words from section 364(1)(d) of ITA which are unnecessary and have, accordingly, not been included in the corresponding clause 30(1)(d) of this Bill.

## **Annex 1**

### **Change 625: Share loss relief, community investment tax relief and the corporate venturing scheme: omit the words “for full consideration”: clauses [share loss relief] and 27 and Schedule 1 (paragraph 46(2)(a) of Schedule 15 to FA 2000)**

This change deletes the words “for full consideration” which qualify “by way of a bargain made at arm’s length”. It removes words which are not in practice applied to impose any additional requirement.

There are three places in the Tax Acts where the words “by way of a bargain made at arm’s length” are qualified by the words “for full consideration”. These are:

- section 575(1)(a) of ICTA (relief for losses on unquoted shares in trading companies);
- paragraph 29(4)(a) of Schedule 16 to FA 2002 (community investment tax relief); and
- paragraph 46(2)(a) of Schedule 15 to FA 2000 (the corporate venturing scheme).

Paragraph 46(2)(a) of Schedule 15 to FA 2000 is also applied for the purposes of paragraph 67 of that Schedule by paragraph 67(3).

All these provisions apply for corporation tax purposes only. Prior to ITA, section 575(1)(a) of ICTA and paragraph 29(4)(a) of Schedule 16 to FA 2002 also applied for income tax purposes.

Section 575(1)(a) of ICTA and paragraph 67 of Schedule 15 to FA 2000 are concerned with the circumstances in which an allowable loss incurred on a disposal of

shares may be claimed as a relief in calculating taxable income. The phrase “for full consideration” has not caused practical difficulty in relation to the application of either of those provisions.

Case law (Berry v Warnett (1982), 55 TC 92 HL<sup>1</sup> and Bullivant Holdings Limited v CIR (1998), 71 TC 22 ChD<sup>2</sup>) confirms that a bargain may be made at arm’s length if a full and fair price is paid. Whether the price is full and fair is to be determined by reference to the circumstances of the disposal and it is clear that the price paid may be full and fair notwithstanding that it is substantially below open market value.

If the words “for full consideration” mean no more than that a full and fair price is paid in the circumstances of the disposal, the words are otiose. If they have independent meaning, this may require that the price paid is not less than market value, if market value is greater than the amount which is a full and fair price in the circumstances of the disposal. But in practice no such requirement is imposed.

Accordingly the words “for full consideration” have been omitted from section 131(3)(a) of ITA rewriting section 575(1)(a) of ICTA for income tax purposes. See Change 20 in Annex 1 to the Explanatory Notes to ITA.

This Bill similarly omits those words from clause 1(2)(a) of this Bill rewriting section 575(1)(a) of ICTA for corporation tax purposes and amends Schedule 15 to FA 2000 so that the words do not apply for the purposes of paragraph 67 of that Schedule (see below).

Paragraph 29 of Schedule 16 to FA 2002 and paragraph 46 of Schedule 15 to FA 2000 are concerned with the withdrawal or reduction of tax relief previously obtained.

These paragraphs contrast with the only other provisions in the Tax Acts dealing with the withdrawal or reduction of investment reliefs, namely:

- section 299(1)(a) and (b) of ICTA and section 209(2) and (3) of ITA (withdrawal or reduction of EIS relief); and
- section 266(2) and (3) of ITA (withdrawal or reduction of VCT relief).

In those provisions, the words “by way of a bargain made at arm’s length” appear without any qualification.

In practice, the provisions for the withdrawal or reduction of CITR are operated on the same basis as the similar provisions relating to EIS relief and VCT relief - see

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<sup>1</sup> [1982] STC 396

<sup>2</sup> [1998] STC 905

paragraph 7020 of HMRC's Community Investment Tax Relief Manual (CITM 7020).

The words "for full consideration" have accordingly been omitted from section 361(4)(a) in Part 7 of ITA rewriting Schedule 16 to FA 2002 for income tax purposes. See Change 20 in Annex 1 to the Explanatory Notes to ITA.

This Bill similarly omits those words from:

- clause 27 rewriting paragraph 29(4)(a) of Schedule 16 to FA 2002 for corporation tax purposes and
- paragraph 46(2)(a) of Schedule 15 to FA 2000 (see Schedule 1).

*This change is in taxpayers' favour in principle. But it is expected to have no practical effect as it is in line with generally accepted practice.*

**Change 650: Community investment tax relief: permit deduction of expenses incurred by director, employee or associate: clause 33**

This change permits consideration given by a director or employee of an investor or by an associate of such a director or employee for a benefit or facility provided by the CDFI to be deducted in calculating value received.

Paragraph 35 of Schedule 16 to FA 2002, rewritten in clause 32, provides for the circumstances in which the investor receives value from the CDFI for the purposes of determining whether any CITR falls to be reduced or withdrawn.

One of those circumstances (paragraph 35(1)(d)) is the provision by the CDFI of a benefit or facility for:

- (i) the investor or any associates of the investor, or
- (ii) directors or employees of the investor or any of their associates.

Associate is defined in paragraph 50 of Schedule 16 to FA 2002, rewritten in clause 47.

Paragraph 36(d) of Schedule 16 to FA 2002 determines the amount of the value received in a case falling within paragraph 35(1)(d) as:

- (i) the cost to the CDFI of providing the benefit or facility, less
- (ii) any consideration given for it by the investor or any associate of the investor.

But paragraph 36 does not permit the deduction of any consideration:

- in a case where the benefit or facility is provided to a director or employee, given by the director or employee or by any associate of the director or employee, or
- in a case where the benefit or facility is provided to an associate of a director or employee, given by the associate or by the director or employee.

As the consideration is most likely to be given by the recipient of the benefit or facility, this may put the investor in a worse position if the benefit or facility is provided to a director or employee or an associate of a director or employee than if the benefit or facility is provided to the investor itself or an associate of the investor.

In rewriting paragraph 36(d) of Schedule 16 to FA 2002 in clause 33 this omission has been rectified.

***This change is in taxpayers' favour in principle and may benefit some in practice. But the numbers affected and the amounts involved are likely to be small.***