STATUTORY INSTRUMENTS

2009 No. 2034

INCOME TAX

CORPORATION TAX

The Investment Trusts (Dividends) (Optional Treatment as Interest Distributions) Regulations 2009

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The Treasury make the following Regulations in exercise of the powers conferred by section 45 of the Finance Act 2009(**a**).

PART 1
PRELIMINARY PROVISIONS

Citation, commencement and effect

1.—(1) These Regulations may be cited as the Investment Trusts (Dividends) (Optional Treatment as Interest Distributions) Regulations 2009 and shall come into force on 1st September 2009.

(2) These Regulations have effect in relation to amounts distributed on or after 1st September 2009.

Structure of these Regulations

2. The structure of these Regulations is as follows—

this Part contains preliminary provisions;

Part 2 deals with the optional treatment of dividends as interest distributions;

Part 3 deals with the duty to deduct tax from interest distributions; and

Part 4 deals with information and record keeping relating to distributions.

Interpretation

3.—(1) In these Regulations—

the "Commissioners" means the Commissioners for Her Majesty's Revenue and Customs;

"ICTA" means the Income and Corporation Taxes Act 1988(**b**);

"interest distribution" has the meaning given in regulation 5(2);

"period of account" has the meaning given in section 832(1) of ICTA(**c**); and

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(**a**) 2009 c. 10.
(**b**) 1988 c. 1.
(**c**) The definition of "period of account" was inserted by section 103(1) and (6) of the Finance Act 2002 (c. 23).

"qualifying interest income" means the amount determined in accordance with regulation 8.

(2) In these Regulations "recipient", in relation to an interest distribution of an investment trust or prospective investment trust, means the beneficial owner of the interest distribution, except where the distribution is held on trust (other than under a bare trust) or forms part of the estate of a deceased person; and, in such a case, the recipient means the trustees of the trust on which the interest distribution is held or, as the case may be, the deceased person's personal representatives.

PART 2

OPTIONAL TREATMENT OF DIVIDENDS AS INTEREST DISTRIBUTIONS

Circumstances in which dividends may be treated as interest distributions

4.—(1) Subject to paragraph (2), regulation 5 applies if—

(a) a company is an investment trust or a prospective investment trust as respects an accounting period;

(b) an amount is distributed by the company as a dividend in respect of a period of account which includes that accounting period; and

(c) the amount distributed in relation to the period of account is distributed on or before the first anniversary of the day on which that period of account ends.

(2) In a case where an amount is distributed by the company as a dividend in respect of a period of account which includes two or more accounting periods of the company, the company must be an investment trust or prospective investment trust as respects all of those accounting periods.

Treatment of dividends as interest distributions

5.—(1) If this regulation applies, the company may designate as an interest distribution all or part of the amount distributed as a dividend or dividends in respect of the period of account which includes the accounting period.

(2) A dividend, or part of a dividend, in respect of which a designation under this regulation has been made is referred to in these Regulations as an "interest distribution".

(3) A designation under paragraph (1) becomes irrevocable at the time the interest distribution is made.

(4) The aggregate of the amounts distributed as interest distributions in relation to an accounting period may not exceed the amount of the company's qualifying interest income for the accounting period.

Regulation 8 explains how a company's qualifying interest income for an accounting period is calculated.

(5) For the purposes of paragraph (4), where an interest distribution is made in respect of a period of account which includes more than one accounting period the amount distributed as the interest distributions in relation to each accounting period is—

$$\frac{A \times I}{T}$$

where—

"A" is the amount of qualifying interest income for the accounting period;

"I" is the total of the amounts distributed as interest distributions in respect of the period of account; and

"T" is the total amount of the qualifying interest income in respect of all the accounting periods in the period of account.

Notification of designation of dividends as interest distributions

6. If a company makes a designation under regulation 5, the application by the company for approval as an investment trust under section 842 of ICTA (investment trusts)(**a**) as respects the accounting period to which the designation relates must include details of the total amount distributed, or to be distributed, as interest distributions in respect of the accounting period.

Interest distributions not to be treated as distributions for purposes of the Tax Acts

7. An amount distributed as an interest distribution by an investment trust or prospective investment trust shall be treated for the purposes of the Tax Acts as if the amount distributed is not a distribution.

Qualifying interest income

8.—(1) The company's amount of qualifying interest income for an accounting period is the amount by which the aggregate of the company's relevant credits exceeds the aggregate of the company's relevant debits given for that period.

(2) Subject to paragraph (3) and regulation 9, the company's relevant credits and relevant debits are—

(a) credits and debits given for the accounting period for the purposes of Part 5 of the Corporation Tax Act 2009 (loan relationships)(**b**); and

(b) credits and debits given for the accounting period for the purposes of Part 7 of that Act (derivative contracts) in relation to—

(i) derivative contracts the underlying subject matter of which consists wholly of assets representing loan relationships or currency or both, and

(ii) contracts for differences the underlying subject matter of which consists wholly of any one or more of interest rates, creditworthiness and currency.

(3) The company's relevant debits for an accounting period do not include debits arising under regulation 10 in respect of interest distributions made in respect of the accounting period.

(4) If, in relation to an accounting period, the aggregate of the company's relevant debits exceeds the aggregate of the company's relevant credits the amount of the qualifying interest income for that period shall be treated as nil.

(5) In this regulation expressions used in Parts 5 and 7 of the Corporation Tax Act 2009 have the same meaning as they have in those Parts.

Qualifying interest income: further provisions

9.—(1) In the circumstances specified in paragraph (2), the underlying subject matter of a derivative contract is treated for the purposes of regulation 8 as consisting wholly of assets representing loan relationships or currency or both (as the case may be).

(2) The circumstances specified are where the underlying subject matter consists only of—

(a) assets representing loan relationships or currency or both, and

(b) other underlying subject matter which is—

(i) subordinate in relation to those assets, or

(ii) of small value in comparison with the value of the underlying subject matter.

(**a**) Section 842 was amended by section 117(1) of the Finance Act 1988 (c. 39), section 55 of the Finance Act 1990 (c. 29), paragraph 14(55) of Schedule 10 to the Taxation of Chargeable Gains Act 1992 (c. 12), paragraph 8 of Schedule 17 to the Finance Act 1994 (c. 9), paragraph 4(7) of Schedule 9, paragraph 56 of Schedule 25 and Part 3(2) of Schedule 40 to the Finance Act 2002 (c. 23), section 45(4) of the Finance Act 2004 (c. 12), paragraph 228 of Schedule 1 to the Income Tax Act 2007 (c. 3), and section 57(3) of, and paragraph 7(9) of Schedule 26 to, the Finance Act 2007 (c. 11).

(**b**) 2009 c. 4.

(3) In the circumstances specified in paragraph (4), the underlying subject matter of a contract for differences is treated for the purposes of regulation 8 as consisting wholly of one or more of interest rates, creditworthiness and currency (the "principal subject matter").

(4) The circumstances specified are where the underlying subject matter consists only of—

(a) the principal subject matter, and

(b) other underlying subject matter which is—

(i) subordinate in relation to the principal subject matter, or

(ii) of small value in comparison with the value of the underlying subject matter.

(5) For the purposes of paragraphs (2) and (4), whether part of the underlying subject matter of a contract of a company is subordinate or of small value is to be determined by reference to the time when the company enters into or acquires the contract.

Interest distributions: effect for investment trust or prospective investment trust

10.—(1) This regulation applies in respect of an accounting period if a company—

(a) is an investment trust or prospective investment trust in respect of the accounting period, and

(b) makes an interest distribution in relation to the accounting period.

(2) Subject to paragraph (3), the Corporation Tax Acts have effect in relation to the company as if the interest distribution made by the company in relation to the accounting period were interest under a debtor relationship of the company (and, accordingly is an amount recognised in determining the company's profit or loss for the period).

(3) Paragraph (2) does not apply to the extent that the aggregate of the amount distributed as interest distributions in relation to the accounting period exceeds the amount of the company's qualifying interest income for that period.

(4) In paragraph (2) "debtor relationship" has the same meaning as in section 302(6) of the Corporation Tax Act 2009 (loan relationships).

Interest distributions: effect for recipients

11.—(1) In relation to a recipient of an interest distribution within the charge to corporation tax, the Corporation Tax Acts have effect as if the interest distribution were interest under a creditor relationship of that person.

(2) In paragraph (1) "creditor relationship" has the same meaning as in section 302(5) of the Corporation Tax Act 2009 (loan relationships).

(3) In relation to a recipient of an interest distribution within the charge to income tax, the Income Tax Acts have effect as if the interest distribution were a payment of yearly interest on the date the interest distribution is made.

(4) If a recipient of an amount distributed by a company—

(a) is informed (whether directly by the company or by a person who receives the amount on behalf of the recipient) that the amount is distributed to the recipient as an interest distribution, and

(b) is so informed at, or as soon as reasonably possible after, the time the amount is distributed,

the recipient shall treat that amount as an interest distribution (whether or not the amount distributed is an interest distribution for the purposes of the Corporation Tax Acts in relation to the company).

Failure to obtain approval as an investment trust

12. No amount may be distributed as an interest distribution by a company in relation to an accounting period after the time the company is informed by the Commissioners that approval for the purposes of section 842 of ICTA is not given by them as respects that accounting period.

PART 3

DUTY TO DEDUCT TAX FROM INTEREST DISTRIBUTIONS

Duty to deduct tax interest distributions

Duty to deduct tax from interest distributions: general

13.—(1) Any obligation to deduct a sum under section 874(2) of the Income Tax Act 2007(**a**) is subject to the provisions of this regulation.

(2) In this Part the "deduction obligation" means the obligation specified in paragraph (1).

(3) The deduction obligation does not apply to the interest distribution if—

(a) the recipient is a company (whether or not the company is resident in the United Kingdom for tax purposes);

(b) the recipient consists of the trustees of a unit trust scheme;

(c) the reputable intermediary condition in regulation 14 is met with respect to the recipient on the date the interest distribution is made; or

(d) the residence condition in regulation 17 is met with respect to the recipient on the date the interest distribution is made.

(4) But if the recipient is a company acting in the capacity of a trustee of a trust, the deduction obligation is not excluded by virtue of paragraph (3)(a).

(5) In this regulation, "unit trust scheme" has the meaning given by section 237 of the Financial Services and Markets Act 2000(**b**).

The reputable intermediary condition

The reputable intermediary condition

14.—(1) The reputable intermediary condition is met with respect to a recipient on the date the interest distribution is made if conditions A to C are met.

(2) Condition A is that the interest distribution is made on behalf of the recipient to a company.

(3) Condition B is that the investment trust or prospective investment trust making the interest distribution has reasonable grounds for believing that the recipient is not ordinarily resident in the United Kingdom.

(4) Condition C is that the company mentioned in paragraph (2)—

(a) is subject to the EC Money Laundering Directive,

(b) is subject to equivalent non-EC provisions, or

(c) is a company which—

(i) is resident in a regulated country or territory, and

(ii) is an associated company of a company which is subject to sub-paragraph (a) or (b).

(**a**) 2007 c. 3; section 874(2) was amended by paragraph 26 of Schedule 1 to the Finance Act 2008 (c. 9).
(**b**) 2000 c. 8.

The reputable intermediary condition: further provisions

15.—(1) This regulation applies for the purposes of Condition C in regulation 14.

(2) A company is subject to the EC Money Laundering Directive if it is a credit institution or financial institution as defined by Article 1 of Directive 91/308/EEC(**a**), as amended by Directive 2001/97/EC(**b**).

(3) A company is subject to equivalent non-EC provisions if it is required by the law of any country or territory which is not a member State to comply with requirements similar to those which, under Article 3 of Directive 91/308/EEC (as so amended), member States must ensure are complied with by credit institutions and financial institutions.

(4) A country or territory is a regulated country or territory if it either is a member State or imposes requirements similar to those, which, under Article 3 of that Directive (as so amended), member States must ensure are complied with by credit institutions and financial institutions.

(5) A company is to be treated as another's associated company if it would be so treated for the purposes of Part 11 of ICTA (see section 416 of that Act).

The reputable intermediary condition: consequences of reasonable but incorrect belief

16.—(1) This regulation applies if conditions A to D are met.

(2) Condition A is that an interest distribution is made by an investment trust or prospective investment trust.

(3) Condition B is that the investment trust or prospective investment trust, in reliance on the reputable intermediary condition being met with respect to the recipient of the interest distribution, does not comply with the deduction obligation in relation to the interest distribution.

(4) Condition C is that the deduction obligation would apply but for the reputable intermediary condition being met.

(5) Condition D is that (contrary to the belief of the investment trust or prospective investment trust) the recipient is in fact ordinarily resident in the United Kingdom.

(6) The following provisions of the Income Tax Act 2007 have effect as if the deduction obligation applied—

(a) section 874 (duty to deduct from certain payments of yearly interest), and

(b) Chapter 15 of Part 15 (collection: deposit-takers, building societies and certain companies).

The residence condition

The residence condition

17.—(1) The residence condition is met with respect to a recipient on the date the interest distribution is made if any of conditions A to E is met.

(2) Condition A is that, in relation to an interest distribution which is not made to or received under a trust, there is a valid declaration, made by the recipient, that the recipient is not ordinarily resident in the United Kingdom.

(3) Condition B is—

(a) that the recipient receives the interest distribution as the personal representative of a deceased person, and

(b) that the deceased person had made a declaration, which was valid at the time of the deceased person's death, that the deceased person was not ordinarily resident in the United Kingdom.

(**a**) OJ L 166, 28.6.1991, p.77-83.
(**b**) OJ L 344, 28.12.2001, p.77-82.

(4) Condition C is—

(a) that the recipient receives the interest distribution as a personal representative of a deceased person, and

(b) that the personal representative has made a declaration that the deceased, immediately before the time at which the deceased died, was not ordinarily resident in the United Kingdom.

(5) Condition D is that, in the case of an interest distribution made to or received under a trust where the whole of the income is, or falls to be treated as, or under any provision of the Tax Acts is deemed to be, the income of a person other than the trustees of that trust, there is a valid declaration, made by the person in question that the person is either not ordinarily resident or, in the case of a company, not resident in the United Kingdom.

(6) Condition E is that, in circumstances in which condition D does not apply and with respect to a recipient in the case of an interest distribution made to or received under a trust, there is a valid declaration, made by the trustees of that trust, that—

(a) the trustees are not resident in the United Kingdom, and

(b) each beneficiary of the trust is either not ordinarily resident or, in the case of a beneficiary which is a company, not resident in the United Kingdom.

The residence condition: declarations

18.—(1) A declaration for the purposes of regulation 17 must—

(a) be in such form as may be required or authorised by the Commissioners;

(b) be made in writing to the investment trust or prospective investment trust making the interest distribution in question; and

(c) contain any details or undertakings required by paragraphs (2) to (4).

(2) A declaration made for the purposes of condition A or B in regulation 17 must contain—

(a) the name and principal residential address of the person making it; and

(b) an undertaking that the investment trust or prospective investment trust will be notified by that person if the person becomes ordinarily resident in the United Kingdom.

(3) A declaration made for the purposes of condition C in regulation 17 must contain the name of the deceased and the principal residential address of the deceased immediately before the time at which the deceased died.

(4) A declaration made for the purposes of condition D or E in regulation 17 must contain—

(a) the names and principal residential addresses of the trustees of the trust or, in the case of a trustee which is a company, the name of the company and the address of its registered or principal office;

(b) the names and principal residential addresses of the beneficiaries of the trust or, in the case of a beneficiary which is a company, the name of the company and the address of its registered or principal office; and

(c) an undertaking that the trustees of the trust will notify the investment trust or prospective investment trust if—

(i) they become resident in the United Kingdom,

(ii) any beneficiary of the trust named in the declaration becomes ordinarily resident or, in the case of a company, resident in the United Kingdom, or

(iii) any person who becomes a beneficiary of the trust after making the declaration either is at the time of becoming a beneficiary, or subsequently becomes, ordinarily resident or, in the case of a company, resident in the United Kingdom.

References to beneficiaries in regulations 17 and 18

19. In regulations 17 and 18 references to a beneficiary are references to any person who is known to the trustees of the trust to be either—

(a) a person who is, or will, or may become, entitled to any income of the trust, whether in the form of income or not, or

(b) a person to whom any such income may be paid, or for whose benefit any such income may be applied, whether in the form of income or not, in the exercise of a discretion by the trustees.

Interest distributions: declarations and position of investment trust or prospective investment trust

20.—(1) For the purposes of determining whether an interest distribution should be made with or without any deduction required by the deduction obligation, an investment trust or prospective investment trust is entitled to treat a declaration made for the purposes of regulation 17 as valid.

(2) But the investment trust or prospective investment trust may not treat the declaration as valid if condition A or B is met.

(3) Condition A is that the investment trust or prospective investment trust receives a notification in compliance with an undertaking under regulation 18 that a person to whom the undertaking relates has become resident or ordinarily resident in the United Kingdom.

(4) Condition B is that the investment trust or prospective investment trust comes into possession of information by some other means which indicates that such a person is or may be resident or ordinarily resident in the United Kingdom.

PART 4

INFORMATION AND RECORD KEEPING RELATING TO DISTRIBUTIONS

Information relating to distributions

21.—(1) If an amount is distributed as an interest distribution, section 234A of ICTA (information relating to distributions: further provisions)(**a**) shall apply to the company making the interest distribution as if the amount distributed were a payment of interest.

(2) In the case of an investment trust or prospective investment trust, an appropriate statement for the purposes of section 234A of ICTA includes a written statement—

(a) showing—

(i) the gross amount of the distribution made to the recipient,

(ii) the number and class of shares held by the recipient in respect of which the distribution is made,

(iii) the net amount of the distribution per share,

(iv) whether any tax has been deducted from the distribution,

(v) the date the distribution was made,

(vi) the percentage of the gross distribution attributable to the amount treated as an interest distribution and the percentage attributable to dividend;

(b) providing details to allow the recipient to access an electronic means of calculating the amounts that would be shown in a written statement that would apart, from this paragraph, be provided in accordance with subsection (6) or (7) of section 234A; and

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(**a**) Section 234A was inserted by section 32(4) of the Finance (No. 2) Act 1992 (c. 48) and amended by paragraphs 2 and 7 of Schedule 37 to the Finance Act 1996 (c. 8).

(c) providing the recipient with an alternative method of obtaining the details of those amounts without recourse to electronic means.

Notification of interest distributions made without deduction of tax

22.—(1) If, during a tax year, a company has made interest distributions without deduction of tax, the company must give notice of that fact to the Commissioners within 14 days of the end of that tax year.

(2) Notice given under paragraph (1)—

(a) must be given in writing, and

(b) has effect for the tax year in which the distribution was made and for subsequent tax years until the notice is withdrawn.

(3) A company that fails to comply with paragraph (1) is liable to a penalty not exceeding £3,000 determined in accordance with section 100 of the Taxes Management Act 1970(**a**).

(4) Sections 100A, 100B, 102, 103(4) and 118(2) of the Taxes Management Act 1970(**b**) apply to a penalty determined in accordance with paragraph (3).

Duty to keep and preserve records

23.—(1) A company must—

(a) keep such books, records and other documents as may be needed to enable the company to demonstrate that the information supplied in any written statement for the purposes of section 234A of ICTA is correct and complete,

(b) keep copies of all declarations made under Part 3 of these Regulations received by the company,

(c) keep such books, records and other documents as may be needed in relation to amounts distributed as interest distributions (whether or not the interest distributions were made without deduction of tax) for the purposes of demonstrating when and to whom those amounts were distributed, and

(d) preserve those books, records, other documents and declarations in accordance with this regulation.

In this regulation the books, records, other documents and declarations a company is required to keep and preserve are referred to as the "relevant records".

(2) The relevant records must be preserved until the end of the day that is the sixth anniversary of the end of the tax year in which the distribution is made to which the relevant records relate.

(3) Subject to paragraph (4), the duty under paragraphs (1) and (2) to preserve relevant records may be discharged—

(a) by preserving them in any form and by any means, or

(b) by preserving the information contained in them in any form and by any means.

(4) Paragraph (3) does not apply in the case of any kind of record or document to which paragraph 22(3) of Schedule 18 to the Finance Act 1998 (preservation of information etc)(**c**) applies.

(**a**) 1970 c. 9. Section 100 was substituted by section 167 of the Finance Act 1989 (c. 26). There are amendments to section 100 but none is relevant.

(**b**) Section 100A and 100B were substituted by section 167 of the Finance Act 1989. Section 100A was amended by paragraph 29 of Schedule 24 to the Finance Act 2007 (c. 11) subject to transitional rules in article 3 of S.I. 2008/568. Section 100B was amended by paragraph 31 of Schedule 19 to the Finance Act 1994 (c. 9), section 115(7) of the Finance Act 1995 (c. 4) and by S.I. 1994/1813. Section 102 was amended by section 164(4) of the Finance Act 1989. Section 118(2) was amended by Part VII of Schedule 8 to the Finance Act 1970 (c. 24) and by section 94 of the Finance (No. 2) Act 1987 (c. 51).

(**c**) 1998 c. 36. Paragraph 22 was amended by paragraph 16 of Schedule 12 to the Finance Act 2004 (c. 12), paragraph 385 of Schedule 1 to the Income Tax Act 2007 (c. 3) and by paragraph 9 of Schedule 37 to the Finance Act 2008 (c. 9).

Dave Watts
Frank Roy
21st July 2009 Two of the Lords Commissioners of Her Majesty's Treasury

EXPLANATORY NOTE

(This note is not part of the Regulations)

Section 45 of the Finance Act 2009 confers powers to make provision about the tax treatment of the dividends of investment trusts (or prospective investment trusts). Investment trusts are collective investment vehicles constituted as companies and which pool investments with a view to spreading investment risk for their investors. Companies are investment trusts for tax purposes if approved as such by the Commissioners for Her Majesty's Revenue and Customs ("the Commissioners") in accordance with section 842 of the Income and Corporation Taxes Act 1988 ("ICTA"). The investment return to investors in such companies takes the form of dividends. These Regulations enable an investment trust or prospective investment trust (i.e. a company that expects to be approved as an investment trust) to treat its dividends as payments of interest rather than as dividends on shares for tax purposes.

Part 1 of these Regulations contains preliminary provisions and provides for interpretation. Regulation 1 provides for the citation, commencement and effect of these Regulations; and regulation 2 sets outs the structure of these Regulations. Regulation 3 contains interpretive provisions.

Part 2 of these Regulations provides an option to an investment trust company to treat its dividends as payments of interest (referred to as "interest distributions") and deals with the tax treatment of dividends treated as interest distributions. Regulation 4 provides that in order to treat a dividend as an interest distribution the company paying the dividend must be an investment trust or prospective investment trust for the accounting period to which the dividend relates. Regulation 5 provides that where the company is an investment trust or prospective investment trust for an accounting period it may opt to treat all or part of its dividend or dividends for that period as interest distributions and provides a mechanism for dealing with cases where the dividend may relate to more than one accounting period. Regulation 6 provides that where a company treats dividends as interest distributions for an accounting period it must notify the Commissioners of that fact when applying for approval as an investment trust under section 842 of ICTA. Regulation 7 provides that amounts distributed as interest distributions are not to be treated as distributions for the purposes of the Tax Acts. Regulation 8 provides that the amount that may be treated as interest distributions by an investment trust for an accounting period is the amount of its "qualifying interest income". This is the amount of the excess of the investment trust's total credits over the total debits arising from its loan relationships and derivative contracts. Regulation 9 contains supplementary provisions dealing with the determination of the amount of qualifying interest income. Regulation 10 deals with the tax treatment of interest distributions from the perspective of the investment trust or prospective investment trust. Regulation 11 deals with the tax treatment of interest distributions from the perspective of recipients. Regulation 12 prevents dividends being treated as interest distributions by a company where it has been informed by the Commissioners that it is not approved for the purposes of section 842 of ICTA.

Part 3 deals with the investment trust's duty to deduct tax from interest distributions. Regulation 13 provides for the investment trust's general obligation to deduct a sum representing tax when any yearly interest is paid ("the deduction obligation") to be relaxed in a number of cases. The cases in question include those where the reputable intermediary condition is met and those where the residence condition is met. Regulations 14 to 16 deal with the reputable intermediary condition; regulations 17 to 20 deal with the residence condition.

Part 4 deals with information and record keeping in relation to distributions. Regulation 21 provides for section 234A of ICTA (information relating to distributions) to apply in a modified form. Regulation 22 provides that a company making interest distributions without deduction of

tax must report this information to the Commissioners and imposes a penalty for failure to comply with this requirement. Regulation 23 imposes record and document keeping requirements on a company in relation to the interest distributions it makes.

A full Impact Assessment of the effect that this instrument will have on the costs of business and the voluntary sector is available from the HMRC website at http://www.hmrc.gov.uk/ria/index.htm#full and is annexed to the Explanatory Memorandum which is available alongside this instrument on the OPSI website at www.opsi.gov.uk.

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