EXPLANATORY MEMORANDUM TO

THE OFFSHORE FUNDS (TAX) (AMENDMENT NO. 3) REGULATIONS 2013

2013 No. 1770

1. This explanatory memorandum has been prepared by HM Revenue & Customs and is laid before the House of Commons by Command of Her Majesty.

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

2. Purpose of the instrument

2.1 These Regulations remove the duty to withhold sums in respect of basic rate income tax on certain annual payments when made to investors in Offshore Funds by payers in the UK.

2.2 The instrument implements the intentions set out in the Written Ministerial Statement by the Economic Secretary to the Treasury of 21 May 2013 as regards payments made in respect of holdings in Offshore Funds. This statement can be found at http://www.parliament.uk/documents/commons-vote-office/May-2013/21-05-13/2-Chancellor-HMRCBrief.pdf .

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

3.1 These Regulations have effect for the current tax year (2013-14) and subsequent tax years. Authority for this limited retrospective effect is given by section 354(6) of the Taxation (International and Other Provisions) Act 2010.

4. Legislative Context

4.1 Where an annual payment is a qualifying annual payment the payer will (subject to certain exceptions) normally have a duty to deduct a sum representing basic rate income tax under section 900 or section 901 of the Income Tax Act 2007.

4.2 These Regulations provide that an annual payment made to a participant in an offshore fund will not be a qualifying annual payment if certain conditions are met (so the obligation to deduct tax does not arise).

5. Territorial Extent and Application

5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

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

7. Policy background

7.1 The policy objective is to ensure that the UK is not competitively disadvantaged as a centre for fund management.

7.2 Distributions from offshore funds are not subject to UK withholding tax.

7.3 It is common practice in the industry for investors to negotiate an effective reduction on the regular fund management fees and this is often paid directly to the investor by the fund manager instead of being rebated to the fund.

7.4 Where paid by a UK manager or other UK intermediary, such payments are subject to tax as 'annual payments' from the fund manager to the investor but, economically, they are extra distributions from the fund.

7.5 The regulations ensure that non-UK residents can also receive these payments without deduction of UK tax.

8. Consultation outcome

8.1 These Regulations are considered to be urgently needed by industry and so have been subject to a reduced four week consultation period. . Industry responses have been supportive of the Regulations. Some drafting suggestions contained in industry responses are reflected in the final Regulations.

9. Guidance

9.1 Draft guidance on this legislation will be published as soon as possible by HM Revenue & Customs.

10. Impact

10.1 There is negligible impact on business, charities or voluntary bodies as the Regulations restore what had generally been treated by UK payers as the status quo.

10.2 The impact on the public sector is negligible. There may be some initial impact on the work of Revenue and Customs in providing support to the sector.

10.3 A Tax Information and Impact Note covering this instrument was published on 29 May 2013 alongside a draft of this instrument and is available

on the HMRC website at http://www.hmrc.gov.uk/thelibrary/tiins.htm. It remains an accurate summary of the impacts that apply to this instrument.

11. Regulating small business

11.1 The legislation applies to small business.

11.2 It is unlikely to impact on small business for the reason given in paragraph 10.1 above.

12. Monitoring & review

12.1 HMRC has an established programme of liaison with the industry, which will capture issues around implementation and ongoing compliance and administrative costs. In addition, companies are required to prepare tax returns and computations which will provide data to inform any such monitoring and evaluation.

13. Contact

John Buckeridge at HM Revenue & Customs Tel: 020 7147 2560 or email: john.buckeridge@hmrc.gsi.gov.uk can answer any queries regarding the instruments.