EXPLANATORY MEMORANDUM TO

THE OFFSHORE FUNDS (TAX) (AMENDMENT) REGULATIONS 2017

2017 No. 240

1. Introduction

1.1 This explanatory memorandum has been prepared by Her Majesty's Revenue and Customs ("HMRC") and is laid before the House of Commons by Command of Her Majesty.

2. Purpose of the instrument

2.1 This instrument makes changes to ensure that UK taxpayers are taxed fairly on returns from investments in offshore reporting funds.

3. Matters of special interest to Parliament

Matters of special interest to the Select Committee on Statutory Instruments

3.1 None.

Other matters of interest to the House of Commons

3.2 As this instrument is subject to negative resolution procedure and has not been prayed against, consideration as to whether there are other matters of interest to the House of Commons does not arise at this stage.

4. Legislative Context

4.1 The Offshore Funds (Tax) Regulations 2009 (SI 2009/3001) (the principal Regulations) set out the rules for the taxation of investors in offshore funds.

4.2 This instrument amends provisions in Chapter 5 of Part 3 of the principal Regulation with regard to the computation of reportable income.

5. Extent and Territorial Application

5.1 The extent of this instrument is the United Kingdom.

5.2 The territorial application of this instrument is the United Kingdom.

6. European Convention on Human Rights

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

7. Policy background

What is being done and why

7.1 UK taxpayers with investments in offshore reporting funds pay tax on their share of a fund's reportable income and tax on any capital gains when they dispose of their shares or units.

7.2 A review of reports made by reporting funds has shown that where performance fees are charged by investment managers to such funds they can substantially reduce or eliminate investors' reportable income, even though they are charged by reference to the increase in value of a fund's assets rather than by reference to its reportable income.

7.3 This instrument makes changes to the principal Regulations so that such fees will no longer be deductible against reportable income but will instead reduce any gain on disposal.

7.4 The changes will apply to the calculation of reportable income for reporting periods commencing on or after 1 April 2017.

Consolidation

7.5 This instrument makes minor changes to the principal Regulations. There are no current plans to consolidate these changes into the principal Regulations.

8. Consultation outcome

8.1 A draft instrument was published on 5 December with comments invited by 27 January 2017, and two responses were received. Only one of the comments directly concerned the Regulations, and it explained an alternative method used by some offshore funds to reward their managers. A minor amendment has been made to the Regulations to ensure such arrangements are brought within scope of the new provision.

9. Guidance

9.1 The existing guidance in the HMRC Offshore Funds Manual (available at https://www.gov.uk/hmrc-internal-manuals/offshore-funds-manual) will be updated at the next general update, which is expected to be by July 2017. In the interim, representative bodies and professional advisers have been briefed on this minor change to the rules.

10. Impact

10.1 The impact on business, charities or voluntary bodies is expected to be negligible. Affected businesses will incur negligible one-off costs of familiarisation with the new rules and making a minor adjustment to a calculation. There are not expected to be any on-going costs, or any impact on charities or voluntary bodies.

10.2 The impact on the public sector is negligible.

10.3 A Tax Information and Impact Note covering this instrument will be published on the website at https://www.gov.uk/government/collections/tax-information-and-impact-notes-tiins.

11. Regulating small business

11.1 The legislation applies activities that are undertaken by small businesses.

11.2 No specific action is proposed to minimise regulatory burdens on small businesses.

11.3 The basis for the final decision on what action to take to assist small businesses was that, although the changes do not discriminate between businesses few, if any, small businesses are affected. The impact on small and micro businesses is negligible.

12. Monitoring & review

12.1 HMRC will monitor this measure through ongoing contact with the investment management industry.

13. Contact

13.1 Wayne Strangwood at HM Revenue & Customs Telephone: 03000 585 493 or email: wayne.a.strangwood@hmrc.gsi.gov.uk can answer any queries regarding the instrument.