Explanatory Note

Clause 3 and its Schedule: Dividend tax credits etc.

Summary

1. This measure abolishes the dividend tax credit and makes consequential amendments. It is part of the changes proposed to dividend taxation, including abolition of the dividend tax credit, changes to dividend tax rates and the introduction of a new dividend allowance. The new rules will apply to dividends paid (and other distributions made) on or after 6 April 2016. Related changes are made by clause 2.

Details of the Clause

2. Clause 3 introduces the Schedule to Clause 3.

Details of the Schedule

3. Paragraph 1(1) amends the Income Tax (Trading and Other Income) Act 2005 (ITTOIA 2005). It repeals the sections that entitle a UK resident (or eligible non-UK resident) person to a tax credit in respect of dividends received from UK resident and non-UK resident companies (sections 397 and 397A of ITTOIA 2005). Section 398 of ITTOIA 3005 increases a person's taxable income by the amount of the dividend tax credit and is repealed.

4. Paragraph 1(1) also repeals the sections in ITTOIA 2005 that treat tax as paid at the dividend ordinary rate on "non-qualifying distributions", stock dividends from UK resident and non-UK resident companies, and loans to participators that are released or written off, all of which are treated as distributions (sections 400, 414 and 421 of ITTOIA 2005).

5. Paragraph 1(2) repeals tax credits for certain distributions received by companies (or that are treated as the income of a company).

Further amendments in Income Tax (Trading and Other Income) Act 2005 (ITTOIA 2005)

6. Paragraphs 2 to 10, 13 to 20 and 54 make consequential amendments following the abolition of the dividend tax credit.

7. Paragraph 11 rewrites section 399 ITTOIA 2005. A non-UK resident person who receives a distribution from a UK resident company is treated as having paid tax on that distribution at the dividend ordinary rate. This amendment makes the consequential adjustments necessary following the abolition of the dividend tax credit. It also restores the meaning of the legislation to what it was before an inadvertent amendment was made under the Tax Law Rewrite project.

8. Paragraph 12 amends section 401of ITTOIA 2005, which provides relief where a person receives a distribution that is linked to an earlier distribution of a special type. The amendment introduces the concept of a "CD distribution", which means a distribution that is

only a distribution because of section 1000(1) paragraphs C or D of the Corporation Tax Act 2010 (CTA 2010). The phrase "CD distribution" replaces "non-qualifying distribution", and accordingly "non-CD distribution" replaces the term "qualifying distribution" (see paragraph 14 below).

Further amendments in CTA 2010

9. Paragraphs 21, 24 to 28, 35, 37, 40 to 42 and 59 make consequential amendments following the abolition of the dividend tax credit.

10. Paragraphs 22 and 23 amend sections 279F and 279G of CTA 2010, which use the definition of "franked investment income" to determine when a company has ring fenced income. The concept of franked investment income is repealed (see paragraph 13 below), and a new definition introduced in its place.

11. Paragraphs 29 and 30 make similar amendment to sections 1070 and 1071 of CTA 2010, which deal with distributions made by a company carrying on mutual business.

12. Paragraphs 31 to 34 amend sections 1100 to 1106 of CTA 2010, which set out when a company must provide a certificate following a distribution. The amendments retain the requirement for a certificate, but remove the obligation to show the dividend tax credit and make minor consequential adjustments.

13. Paragraph 36 replaces "qualifying distribution" with "non-CD distribution".

14. Paragraph 38 repeals section 1126 of CTA 2010, the meaning of "franked investment income". This term was used to describe a dividend that had been "franked" with a dividend tax credit.

15. Paragraph 39 repeals section 1136 of CTA 2010, the meaning of "qualifying distribution". A qualifying distribution was one which qualified for a dividend tax credit, meaning a distribution under section 1000(1) but excluding paragraphs C and D.

Other Amendments

16. Paragraph 43 to 56, 58 and 60 to 64 make consequential amendments following the abolition of the dividend tax credit to a number of Acts.

Amendments to Corporation Tax Act 2009 (CTA 2009)

17. Paragraph 57(1) makes consequential amendments following the abolition of the dividend tax credit.

18. Paragraph 57(2) amends section 1222 of CTA 2009, which deals with reductions in amounts deductible as management expenses. The amendments are similar to those described at paragraph 9 above.

Commencement

19. Paragraph 65 provides for commencement. Paragraph 65(4) provides that paragraph 14 of Schedule 19 to Finance Act 2009, which deals with the commencement of provisions relating to income tax credits for foreign distributions, is not affected.

Background note

20. The Chancellor announced at the Summer Budget 2015 that the way that dividends are taxed

is to be reformed, with a new dividend allowance replacing the existing dividend tax credit. Clause 2 introduces the new allowance. This Schedule repeals the dividend tax credit, and deals with the consequential amendments.

21. If you have any questions about this change, or comments on the legislation, please contact Adrian Coates on 03000 586041 (email: Adrian.Coates@hmrc.gsi.gov.uk).