These notes refer to the Income Tax (Trading and Other Income) Act 2005 (c.5) which received Royal Assent on 24 March 2005

INCOME TAX (TRADING AND OTHER INCOME) ACT 2005

EXPLANATORY NOTES

COMMENTARY ON SECTIONS

Part 4: Savings and investment income
Chapter 3: Dividends etc. from UK resident companies etc.

Introduction

Section 382: Contents of Chapter

1537. This section explains the scope of the Chapter. The Chapter contains the charge to tax on dividends and other distributions (and amounts treated as dividends) from companies resident in the United Kingdom. It also contains special provisions about dividends paid in respect of shares awarded under approved share incentive plans ("SIPs"). And, it contains provisions about tax credits and deduction of tax.

1538. Exemptions from the charge to tax under this Chapter are signposted in *subsection (3)*.

1539. The exemptions include section 498 of ITEPA which is part of the SIP code (see further the commentary on section 392 of this Act and the overview to the SIP provisions). The SIP code provides various exemptions from tax for persons participating in an approved SIP. The code also imposes tax charges in certain circumstances, for example, if shares are not held within the plan for the prescribed period of time. Section 498 of ITEPA provides an exemption from the charge to income tax that arises if dividend shares cease to be subject to the plan, if the participant is a "good leaver". In the source legislation, section 498 of ITEPA is expressed as a proviso to section 251C of ICTA (see section 251C(6) of ICTA). But as the charge to tax in respect of all dividends and other distributions of a UK resident company falls under Chapter 3 of Part 4 of this Act, section 498 of ITEPA is signposted as an exemption from the tax charge under this Chapter.

1540. S*ubsection (4)* replicates the position under the source legislation by ensuring that stock dividends that are taxed under Chapter 5 of Part 4 of this Act are not dividends for the purposes of this Chapter. (Despite their name, they do not count as dividends for the purposes of Schedule F. See further the commentary on Chapter 5 of Part 4 of this Act.)

1541. See the commentary on paragraph 10 of Schedule 1 to this Act for an explanation of the repeal of Schedule F.

Section 383: Charge to tax on dividends and other distributions

1542. This section charges to tax dividends and other distributions from UK resident companies. It is based on Schedule F in section 20 of ICTA.

1543. The section charges to tax "dividends and other distributions". The expression "distribution" is not defined in this Act except by reference to section 832(1) of ICTA (see the index of defined expressions in Part 2 of Schedule 4 to this Act).

1544. The main reason for not rewriting "distribution" in this Act is the importance of the expression in a corporation tax context (because, for example, distributions of companies resident in the United Kingdom are not taken into account in computing profits for corporation tax purposes - see section 208 of ICTA - and do not give rise to a tax deductible expense for the distributing company - see section 337A of ICTA). The expression therefore needs to be retained in a corporation tax context. Rewriting it in an income tax context would mean maintaining similar but not identical provisions for different purposes (some of the provisions - for example, section 209(5) to (7) of ICTA - are not relevant for income tax purposes). This is not thought to be straightforward or convenient for users of the legislation.

1545. Section 20(1) paragraph 1 of ICTA charges to tax all dividends and other distributions. But this is subject to section 95(1A)(a) of ICTA (taxation of dealers in respect of distributions). Section 95(1A)(a) of ICTA provides that tax is not charged under Schedule F where a dealer receives a "relevant distribution". Instead, tax is charged under Schedule D Case I or II. Section 383 does not explicitly rewrite the proviso in section 20(1) of ICTA but the effect of the proviso is replicated by section 366(1) of this Act (which gives charging priority to Chapter 2 of Part 2 of this Act for income which is a receipt of a trade). So a distribution made by a UK resident company which is a receipt of a trade is charged to tax under Part 2 of this Act and not under this Chapter.

1546. The charge to tax under Schedule F in the source legislation is also subject to section 171(2) of FA 1993 (Lloyd's underwriters: taxation of profits and allowance of losses) (see section 20(2) of ICTA). As with dealers, the tax charge in the source legislation is Schedule D Case I and not Schedule F. But section 171(2) of FA 1993 additionally provides that the amount of the profits arising from assets in an ancillary trust fund is calculated under the relevant Schedule or Case. Again, section 383 does not explicitly rewrite the proviso in section 20(2) of ICTA but the effect of that section is replicated by section 366(1) of this Act (which gives charging priority to Chapter 2 of Part 2 of this Act). And section 2(4) of this Act ensures that the calculation can be made under this Chapter.

1547. *Subsections (2)* and *(3)* confirm that the distribution is regarded as income for all income tax purposes even if it would otherwise be treated as capital (a capital dividend is a distribution – see section 209(2)(a) of ICTA).

Section 384: Income charged

1548. This section sets out the amount charged to tax and is based on section 20(1) paragraphs 1 and 2 of ICTA. The amount charged is the amount or value of the dividends paid and distributions made in the tax year. But if the recipient of the distribution is entitled to a tax credit, the amount charged is the amount or value of the distribution plus the tax credit (see *subsection (3)*).

1549. Dividends are treated as paid for the purposes of the Corporation Tax Acts "on the date when they become due and payable, except in so far as Chapter III of Part XII makes other provision for dividends treated as paid by virtue of that Chapter" (see section 834(3) of ICTA).

1550. The "Corporation Tax Acts" means the enactments relating to the taxation of the income and chargeable gains of companies and company distributions (including provisions relating to income tax) (see section 831(1) of ICTA). Chapter 3 of Part 12 of ICTA (referred to in the previous paragraph) specifies the date on which dividends which an authorised unit trust is treated as paying, are paid. So in all other cases the date on which a dividend is paid is the date on which the dividend becomes due and payable.

1551. The date when a final dividend becomes due and payable is usually established by a resolution of the company. The dividend becomes due when the date on which it is expressed to be payable arrives. Only then is payment enforceable. In the case of a final dividend where a date for payment is not specified, an immediately enforceable debt is created so that the date of declaration of the dividend is the due and payable date.

1552. An interim dividend can be varied and rescinded at any time before payment and can therefore only be regarded as "due and payable" when the date for payment arrives.

1553. The main case law authority for the above propositions is Potel v CIR (1970), 46 TC 658 HC (which particularly indicates that the declaration of a dividend by a company and its payment are two separate matters). Paragraph 2007b of the Inland Revenue's Company Taxation Manual (CT2007b) provides the Inland Revenue's interpretation of section 834(3) of ICTA and the meaning of "paid".

Section 385: Person liable

1554. This section states who is liable for any tax charged.

1555. Under the source legislation there is no provision expressly stating who is liable for the tax charged. Although section 20(1) paragraph 1 of ICTA makes it clear that the charge to tax encompasses all distributions of a UK resident company made in a tax year, and includes a reference to the recipient, it does not actually specify the person liable.

1556. The person liable can however be deduced from the legislation as a whole (and this has been reflected in *subsection (1)*).

1557. Section 20(1) of ICTA refers to recipients of distributions and persons entitled to tax credits. Paragraph 1 of section 20(1) of ICTA provides that distributions are regarded as income "…however they fall to be dealt with in the hands of the recipient"; paragraph 2 of that section provides that where "…a person is entitled to a tax credit" in respect of a distribution it is the aggregate of the distribution and the tax credit which is taxed.

1558. Section 231(1) of ICTA (tax credits for certain recipients of qualifying distributions) provides that a UK resident "receiving" a qualifying distribution is entitled to a tax credit. And section 232 of ICTA (tax credits for non-UK residents) refers to distributions "received" by certain individuals. Section 231(4) of ICTA deals with the case where a distribution "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 recipient", so that other person is treated as receiving the distribution for the purposes of section 231 of ICTA. So, section 231(4) of ICTA suggests that where the distribution actually belongs to someone other than the recipient, or under any provision of the Tax Acts is treated as belonging to someone other than the recipient, that other person is liable for the tax charged.

1559. Section 209 of ICTA is the main provision which defines the term "distribution". Section 209(1) of ICTA provides that "The following provisions of this Chapter, together with section 418 of ICTA, shall, subject to any express exceptions, have effect with respect to the meaning of "distribution" and for determining the persons to whom certain distributions are to be treated as made ...".

1560. Where an asset or liability is transferred by a company to a member, section 209(4) of ICTA requires an amount to be treated as a distribution made to the member.

1561. Distributions are made, in most circumstances, to shareholders. For the purposes of Part 6 of ICTA (company distributions, tax credits etc) section 254(12) of that Act regards something done "in respect of a share" as being done to the shareholder, or to someone who has at a particular time been the shareholder. This suggests that someone to whom a distribution is treated as made for the purposes of Part 6 of ICTA is liable.

1562. The definition of distribution is extended by section 418(1) of ICTA to include any amount which is required to be treated as a distribution by section 418(2) of ICTA. Under section 418(2) of ICTA, where a close company incurs expense in providing a benefit or facility for a participator "the company shall be treated as making a distribution to him of an amount equal to so much of that expense as is not made good to the company". While it does not explicitly identify the person liable in respect of the distribution, in practice the participator is regarded as the person liable.

1563. So, while there is no express person liable provision (as there is for Schedule D for example), there are provisions covering:

- the person to whom a distribution is made or to whom it is treated as made for the purposes of Part 6 of ICTA – sections 209(1) and (4), 254(12) and 418(2) of ICTA;
- the person receiving a distribution – sections 20(1)1, 231(1) and (4) and 209(4) of ICTA;
- the person entitled to the distribution – sections 20(1)2 and 231(4); and
- the person to whom the distribution, under any provision of the Tax Acts, is treated as belonging (where that person is not the recipient) – section 231(4) of ICTA.

1564. A provision stating who is liable for any tax charged on distributions from UK resident companies needs to cover all these possibilities save the last one. If a distribution is treated under any provision of the Tax Acts as the income of a person other than the recipient, that legislation will provide who is liable for the tax.

Section 386: Open-ended investment company dividend distributions

1565. This section and the two sections that follow provide investors, who are liable to income tax, with the information required to determine their taxable income from the open ended investment company (OEIC). The tax provisions relevant to the OEIC, which is liable to corporation tax, are not in this Act.

1566. This section is based on section 468J of ICTA and the Open-ended Investment Companies (Tax) Regulations 1997 SI 1997/1154. These regulations provide that the tax treatment of investors (shareholders) in an OEIC generally follows the tax treatment of investors (unit holders) of an authorised unit trust (AUT). For an outline of the treatment of investors in an AUT see the commentary on section 376.

1567. The section provides for amounts that are not dividends and would otherwise be something else to be treated as dividends received by the investors. The amounts so treated are charged by section 383 and the provisions about tax credits or tax being treated as paid at sections 397 to 399 will apply as appropriate.

Section 387: Date when dividends paid under section 386

1568. This section is based on sections 468, 468H and 468J of ICTA and the Open-ended Investment Companies (Tax) Regulations 1997 SI 1997/1154. It applies to the amounts treated as dividends.

Section 388: Interpretation of sections 386 and 387

1569. This section is based on sections 468H and 832 of ICTA and the Open-ended Investment Companies (Tax) Regulations 1997 (SI 1997/1154).

1570. The regulations contained in SI 1997/1154, in so far as they apply to invoke the AUT rules for the tax charge on OEIC investors liable to income tax, are rewritten in the preceding sections. The regulations remain in place in respect of investors liable to corporation tax and all other aspects concerning OEICs. A saving has been made in paragraph 78 of Schedule 2 to this Act to preserve the power in section 152 of FA 1995 so that regulations may continue to be made for achieving any purpose that could be achieved by such regulations before enactment of these sections.

Section 389: Authorised unit trust dividend distributions

1571. This section and the two sections that follow provide investors, who are liable to income tax, with the information required to determine their taxable income from the authorised unit trust (AUT). The tax provisions relevant to the AUT are not in this Act. This is because the AUT trustees are treated as a company liable to corporation tax under section 468(1)(a) of ICTA.

1572. This section is based on section 468J of ICTA which is part of the special tax rules for AUTs. For an outline of the treatment of investors in an AUT see the commentary on section 376.

1573. The amounts treated as dividends received by the investors are charged by section 383 and the provisions about tax credits or tax being treated as paid at sections 397 to 399 will apply as appropriate.

Section 390: Date when dividends paid under section 389

1574. This section is based on sections 468H and 468J of ICTA. It applies to the amounts treated as dividends.

Section 391: Interpretation of sections 389 and 390

1575. This section is based on sections 468H and 832 of ICTA.

Shares in approved share incentive plans ("SIPs")

Overview

1576. Section 392 and the following four sections are based on sections 251A to 251C of ICTA which are part of the legislation relating to SIPs. The SIPs legislation was originally contained in Schedule 8 to the FA 2000 (introduced by section 47 of FA 2000) and was rewritten in ITEPA. The majority of the SIP code is contained in Chapter 6 of Part 7 of and Schedule 2 to ITEPA.

1577. The SIP code is designed to encourage employee share ownership. The core of the SIP code is that a company establishes a share incentive plan. Under the plan various types of share can be acquired or awarded - free shares, partnership shares and matching shares. In addition, scheme participators may, with the dividends paid on their shares, acquire "dividend shares".

1578. The shares awarded or acquired under the plan are held on behalf of the scheme participant by the trustees of the scheme. Therefore, any dividend paid by the company on those shares is paid to the trustees.

1579. The participant may choose (or the company may require) that all cash dividends paid on the shares be reinvested in further shares. If so, the cash dividend is used by the trustees of the scheme to acquire further shares. Those shares are called dividend shares.

1580. Section 493 of ITEPA (which is rewritten as section 770(2)(a) of this Act) provides that a scheme participant is not liable to income tax on the amount applied by the trustees in acquiring dividend shares on the participant's behalf.

1581. But a tax charge may arise if the dividend shares subsequently cease to be subject to the approved SIP. The special rules applying when dividend shares cease to be subject to the plan are rewritten in section 394.

1582. If the trustees cannot reinvest the cash dividend either because the amount of the cash dividend is not sufficient to acquire a share or because there is an amount remaining after acquiring shares, the trustees may keep the cash dividend and carry it forward with a view to reinvestment at a later date (see paragraph 68(2) of Schedule 2 to ITEPA). In that case, section 496 of ITEPA (rewritten as section 770(1)(b) of this Act) provides that the participant is not liable to income tax in respect of the amount of the cash dividend held by the trustees.

1583. But if the trustees subsequently pay over the cash dividend to the participant, the tax charge may revive. The special rules applying when the cash dividend held by the trustees is paid over to the participant is rewritten in section 393.

Section 392: SIP shares: introduction

1584. This section introduces the special rules about SIPs. It is based on section 251A of ICTA.

1585. *Subsections (2)* to *(7)* ensure that sections 393 to 396 apply only if the participant has benefited from the tax advantages of an approved SIP. Those tax advantages apply to an individual who is chargeable to tax under Part 2 of ITEPA in respect of eligible employment (as defined in *subsection (4)*) or, if the shares were awarded before ITEPA came into force, under Schedule E.

Section 393: Later charge where cash dividends retained in SIPs are paid over

1586. This section is based on section 251B of ICTA.

1587. The trustees of the scheme may only hold on to a cash dividend and carry it forward for three years from the date the dividend is paid by the company. Additionally, any amount not reinvested must be paid to the participant if the participant ceases to be in “relevant employment” or if a termination notice is issued in respect of the plan (see paragraph 68(4) of Schedule 2 to ITEPA).

1588. *Subsection (2)* ensures that in any of these circumstances, the participant is charged to income tax for the tax year in which the dividend is paid over.

1589. Tax is charged on the amount of the cash dividend paid over and not on the amount of the cash dividend originally paid by the company (*subsection (3)*).

1590. Whether the participant is entitled to a tax credit and, if so, the amount of it, is determined by reference to the tax year in which the cash dividend is paid over by the trustees and not by reference to the tax year the company actually paid the dividend (see *subsection (5)*).

1591. Section 251B of ICTA is rewritten so that the original tax charge is postponed (contrast section 394 which deems a further distribution to be made). This approach has rendered the phrase “except to the extent that it represents a foreign cash dividend” redundant. In effect, the cash dividend paid over by the trustees does not lose its original character as either a cash dividend paid by a UK resident company (in which case it is dealt with under this Chapter) or a cash dividend paid by a non-UK resident company (in which case it is dealt with under Chapter 4 of Part 4 of this Act).

1592. But the definition of “foreign cash dividend” in section 251D of ICTA does suggest that it is the date that the company originally paid the dividend that determines, under the source legislation, whether the tax charge falls under Schedule F (if UK resident company) or Schedule D Case V (if non-UK resident company). This is rewritten in *subsection (6)*.

Section 394: Distribution when dividend shares cease to be subject to SIP

1593. This section is based on section 251C of ICTA and applies if the dividend shares acquired with the cash dividend cease to be subject to the approved SIP within three years of acquisition.

1594. *Subsection (2)* deems a distribution to have been made to the participant in the tax year in which the dividend shares cease to be subject to the plan.

1595. *Subsection (3)* confirms that tax is charged on the amount of the cash dividend applied to acquire the shares (which have ceased to be subject to the plan) rather than, for example, the amount or value of the dividend shares.

Section 395: Reduction in tax due in cases within section 394

1596. This section is based on section 251C of ICTA and applies if tax has been paid in respect of any capital receipts received in connection with the holding of the dividend shares which cease to be subject to the approved SIP.

1597. *Subsection (2)* operates to reduce the amount of tax due under section 394.

Section 396: Interpretation of sections 392 to 395

1598. This section is based on section 251D of ICTA.

Section 397: Tax credits for qualifying distributions: UK residents and eligible non-UK residents

1599. This section and the following four sections deal with:

- a person's entitlement to a tax credit attaching to qualifying distributions;
- the tax treatment of qualifying distributions where the person is not entitled to a tax credit; and
- the tax treatment of non-qualifying distributions.

1600. The sections are based on sections 231, 232 and 233 of ICTA.

1601. By virtue of sections 231(1) and 232 of ICTA tax credits are available to certain recipients in respect of certain qualifying distributions from companies resident in the United Kingdom.

1602. Tax credits attach to qualifying distributions which are made either to residents of the United Kingdom or to certain non-UK resident persons. The source legislation has been rearranged so that there is a single provision dealing with both categories of recipients (UK resident and non-UK resident) who are entitled to tax credits.

1603. Most distributions of companies resident in the United Kingdom are "qualifying distributions" (see section 14(2) of ICTA). Only the issue of redeemable share capital (unless that share capital is taxed under the stock dividends legislation) or the issue of securities in respect of shares or securities of a company otherwise than wholly for new consideration, are non-qualifying distributions.

1604. In line with the decision not to define the expression "distribution" in this Act, the expression "qualifying distribution" is likewise not defined (other than by reference to section 832(1) of ICTA).

1605. *Subsection (1)* sets out who is entitled to the tax credit, in what circumstances and what the value of that tax credit is. Those entitled to the tax credit include "eligible non-UK residents".

1606. *Subsection (2)* deals with how the tax credit may be used and rewrites section 231(3) of ICTA. Section 231(3) in the source legislation is subject to section 231(3AA) of ICTA. This is rewritten in a slightly different way. *Subsection (3)* treats the tax credits attaching to qualifying distributions as reduced if those distributions are not brought into charge to tax. So, for example, if an individual's total income is reduced by deductions (for example, personal allowances) such that the qualifying distributions are not, or are not wholly, brought into charge to tax, the value of the tax credits attaching to those distributions are correspondingly reduced. So a person may be entitled to a tax credit whose value is nil.

1607. Although companies resident in the United Kingdom are expressly excluded in section 231(3) of ICTA, (because section 231(3) of ICTA applies to a person “not being a company resident in the United Kingdom”) this exclusion has not been adopted. See *Change 84* in Annex 1.

1608. *Subsection (4)* defines eligible non-UK resident. Section 232 of ICTA extends the entitlement to tax credits to certain non-UK resident individuals. These are referred to as individuals who:

“having made a claim in that behalf, [are] entitled to relief under Chapter I of Part VII by virtue of section 278(2) …

1609. The words about making the claim in section 232 of ICTA are unnecessary because the individual will have to make a claim for personal allowances under section 278(8) of ICTA before the tax credit can be taken into account.

1610. Also, section 278 of ICTA does not specify whether the individual concerned has to come within one of the given categories (eg Commonwealth citizen or EEA national) throughout the tax year in question or merely at any time during the tax year in question. However, given personal allowances are available to these individuals simply for falling within a particular category, subsection (4) has followed this approach and has used the words “at any time”.

1611. *Subsection (5)* rewrites section 231(4) of ICTA. The words “(and accordingly the question whether he is entitled to a tax credit in respect of it shall be determined by reference to where he, and not the actual recipient, is resident)” have been omitted. The revised wording of the section makes the words unnecessary.

Section 398: Increase in amount or value of dividends where tax credit available

1612. This section is based on section 20(1) of ICTA (including the proviso “other than section 95(1)”). It applies for all income tax purposes including the case where the recipient of the distribution is a member of Lloyd’s. But the section does not apply if the recipient of the distribution is a dealer (in which case only the net amount of the distribution is taken into account in calculating the profits of the dealer).

Section 399: Qualifying distributions received by persons not entitled to tax credits

1613. This section deals with the tax treatment of qualifying distributions received by persons not entitled to a tax credit (for example, because they are non-resident and do not fall within the definition of “eligible non-UK resident”). As mentioned in the commentary on section 397(3), a person may be entitled to a tax credit whose value is nil. The person is nevertheless entitled to a tax credit and therefore this provision does not apply to such a person. It is based on section 233(1) and (1A) of ICTA.

1614. *Subsection (2)* provides that the non-UK resident is treated as having paid income tax at the dividend ordinary rate (Schedule F ordinary rate in the source legislation) on the amount or value of the distribution.

1615. The amount or value of the distribution will either be the actual amount of the distribution (if the person is a non-UK resident company receiving the qualifying distribution in a beneficial capacity) or that amount is “grossed up” by reference to the dividend ordinary rate. *Subsections (3)* and *(4)* explain when the grossed up amount (as defined in *subsection (5)*) is substituted for the actual amount.

1616. The words “not being a company resident in the United Kingdom” in section 233(1) of ICTA and “any person who is not a company” in section 233(1A) of ICTA create the same difficulties as those in section 231(3) of ICTA. So this section follows a similar approach to that taken in section 397(2) by rewriting sections 233(1) and 233(1A) of ICTA without any exclusion for companies. See *Change 84* in Annex 1.

1617. Section 233(1)(c) of ICTA treats the amount or value of the distribution as not brought into charge to tax for the purposes of sections 348 and 349 of ICTA. Section 233(1)(c) of ICTA is not rewritten in this Act. But rather than leaving the provision "stranded" in section 233 of ICTA, it has been incorporated in section 348 of ICTA as paragraph (a) of a new subsection (4) (see paragraph 147(3) of Schedule 1 to this Act).

Section 400: Non-qualifying distributions

1618. This section is based on section 233(1) of ICTA and applies when a person receives a non-qualifying distribution.

1619. A non-qualifying distribution is defined as any distribution which is not a qualifying distribution (see *subsection (6)*). A qualifying distribution is defined in section 14(2) of ICTA. Broadly, a non-qualifying distribution is an issue of redeemable share capital (unless the share capital is taxed as a stock dividend) or of securities in respect of shares or securities of the issuing company otherwise than wholly for new consideration. A non-qualifying distribution does not carry a tax credit.

1620. *Subsection (2)* treats the recipient of the non-qualifying distribution as having paid income tax at the dividend ordinary rate (Schedule F ordinary rate in the source legislation) on the actual amount of the non-qualifying distribution (that is, there is no grossing up).

1621. The words "not being a company resident in the United Kingdom" in section 233(1) of ICTA create similar difficulties to those in sections 231(3) and 233(1A) of ICTA. See *Change 84* in Annex 1.

1622. *Subsections (4)* and *(5)* are based on section 233(1B) of ICTA. In the case of trustees of accumulation or discretionary trusts, the trustees are taxed on the amount or value of the distribution at the dividend trust rate (Schedule F trust rate in the source legislation). However, the trustees' tax liability is reduced by an amount of income tax equivalent to the dividend ordinary rate (Schedule F ordinary rate in the source legislation).

Section 401: Relief: qualifying distribution after linked non-qualifying distribution

1623. This section is based on section 233(2) of ICTA.

1624. A non-qualifying distribution is generally the first part of an event that will eventually be a qualifying distribution. So the issue of redeemable share capital (unless a stock dividend) is a non-qualifying distribution (see section 14(2)(a) of ICTA) but the repayment of that share capital is a qualifying distribution. So section 233(2) of ICTA provides relief to avoid double taxation for higher rate taxpayers.

1625. The section applies where a taxpayer pays income tax at the dividend upper rate (Schedule F upper rate in the source legislation) on the receipt of a non-qualifying distribution and is liable to income tax at the dividend upper rate (Schedule F upper rate in the source legislation) on the receipt of the linked qualifying distribution. *Subsection (1)* enables a taxpayer to set his or her extra tax liability (ie, the higher rate element) arising on the non-qualifying distribution against the extra liability arising on the qualifying distribution so that the taxpayer is only liable to pay the balance.

1626. *Subsections (5)* and *(6)* explain how the extra liability is calculated in earlier tax years (because the rates at which higher rate taxpayers have paid tax have changed over the years).