These notes refer to the Corporation Tax Act 2010 (c.4) which received Royal Assent on 3 March 2010

CORPORATION TAX ACT 2010

EXPLANATORY NOTES

INTRODUCTION

Part 23: Company distributions

Overview

2954. This Part sets out what is and what is not a company distribution for the purposes of the Corporation Tax Acts. It rewrites Part 6 and section 418 of ICTA and elements of sections 477A, 486 and 490 of ICTA.

2955. The definition of "the Corporation Tax Acts" in the Interpretation Act 1978 refers to enactments relating to the taxation of company distributions and associated income tax provisions. Some income tax rules are included in this Act. But the income tax effect of some provisions (notably sections 249 and 252 of ICTA) are relocated in ITTOIA.

2956. Provisions of an administrative nature relating to specific aspects of distributions have been located alongside the provisions to which they relate. More general provisions about returns and information are in Chapter 6.

2957. The structure of the Part is as follows.

- Chapter 2 sets out what is treated as a distribution.
- Chapter 3 sets out what is not a distribution.
- Chapter 4 deals with certain special cases.
- Chapter 5 deals with demergers.
- Chapter 6 contains provisions about returns and information.
- Chapter 7 deals with tax credits in connection with distributions.
- Chapter 8 provides interpretation.

Chapter 1: Introduction

Section 997: Overview of Part

2958. This section sets out the scope of the Part. It is new.

2959. The section provides signposts to rules that define what is and is not a distribution, to rules that extend the meaning of distribution, and to the power in section 152 of FA 1995 to make modifications in relation to open-ended investment companies. Section 152 of FA 1995 is not being rewritten.

Chapter 2: Matters which are distributions

Section 998: Overview of Chapter

2960. This section sets out the scope of Chapter 2 and provides signposts to other provisions in the Chapter, including those setting out exceptions. It is new.

Section 999: Priority of negative rules

2961. This section directs that the Chapter is subject to any express exceptions, and lists some of those that most commonly affect what is to be treated as a distribution. It is based on section 209(1) of ICTA.

2962. The section specifically refers to paragraph 6 of Schedule 12 to FA 1988, which sets out a number of tax matters connected with the transfer of the whole of the business of a building society to a successor company. It was decided to keep this material together rather than take out one small part. The Schedule has, therefore, not been rewritten.

Section 1000: Meaning of "distribution"

2963. This section sets out the main circumstances that give rise to a distribution. It is based on sections 209(2) and (4) and 418 of ICTA.

2964. The section sets out the circumstances that give rise to a distribution in paragraphs A to H. A number of later sections refer to one or more of these paragraphs.

2965. The references to the source legislation are as follows:

Paragraph	*Origin (in ICTA).*
A	section 209(2)(a).
B	section 209(2)(b).
C	section 209(2)(c).
D	section 209(2)(c).
E	section 209(2)(d).
F	section 209(2)(e).
G	section 209(4).
H	section 209(2)(f).

2966. The section also provides signposts to extensions to the meaning of distribution in section 1064 and section 1072.

Section 1001: Provisions related to paragraphs A to H in section 1000(1)

2967. This section provides information and signposts to bring together in one place a table of the main provisions that explain, supplement or limit each of the categories of distribution. It is new.

2968. It is not exhaustive, but provides a set of signposts to aid navigation through the legislation.

Section 1002: Exceptions for certain transfers of assets or liabilities between a company and its members

2969. This section excludes two circumstances from the scope of paragraph B in section 1000. It is based on section 209(5) and (6) of ICTA.

2970. Section 209(5) and (6) of ICTA are written in slightly different terms. Subsection (5) first qualifies section 209(4) of ICTA. This qualification is rewritten in section 1021(1). Subsection (5) then goes on to disapply section 209(2)(b) of ICTA. Section 1002(1) picks up this link, which brings with it the interpretation material of section 209(7) of ICTA, rewritten in section 1021(2) and (3).

2971. Section 209(6) of ICTA is rewritten in section 1002(2) and section 1021(4). This ensures that the qualifications are located close to the rewritten provisions that they modify.

Section 1003: Redeemable share capital

2972. This section explains how the amount of a distribution is identified when a distribution falls within paragraph C in section 1000 because redeemable share capital is issued partly for new consideration. It is based on section 209(2) and (8) of ICTA.

2973. If a premium is payable to the holder of this type of share capital, either on redemption or otherwise, the amount of the premium is added to the value of the share capital for the purposes of calculating the amount of the distribution.

2974. For example, the nominal value of the share capital is £1000 and the premium payable on redemption is £100. The total value calculated by section 1003 is therefore £1100. If the recipient gives, say, £900 for those shares the amount of the distribution is £200.

Section 1004: Securities issued otherwise than for new consideration

2975. This section performs a role similar to that of section 1003, but in this case in relation to paragraph D in section 1000 – securities issued partly for new consideration. It is based on section 209(2) and (8) of ICTA.

Section 1005: Meaning of "non-commercial securities"

2976. This section sets out the definition of a non-commercial security for the purposes of paragraph E in section 1000. It is based on section 209(2)(d) of ICTA.

2977. Sections 1006 to 1014 also affect the scope and amount of a distribution within paragraph E in section 1000.

Section 1006: Distributions exceeding consideration received for issue of security

2978. This section qualifies the meaning of "the principal secured" for the purposes of section 1005 and of paragraph E in section 1000. It is based on section 209(3) of ICTA.

2979. The basic meaning of "principal secured" is not defined in tax statute and takes its general meaning, subject to any relevant specific tax rules.

2980. In measuring the extent to which there is more than a reasonable commercial return for the use of the principal, the "principal secured" cannot be greater than the amount given for the issue of the security.

2981. Section 1117(6) provides a further qualification if securities are issued at a price less than the amount repayable on them, and are not listed on a recognised stock exchange.

Section 1007: Securities issued at premium representing new consideration

2982. This section sets out the effect on the measurement of the "principal secured" if a security is issued at a premium representing new consideration. It is based on section 209(3A) of ICTA.

2983. The amount of the premium is taken into account in determining both the amount of the principal secured and the extent to which the return on the securities is more than a reasonable commercial return.

2984. Section 1008 qualifies this section, and there is a table at the end of the note on section 1013 summarising the interaction of sections 1006 to 1013.

Section 1008: Consideration for issue of security exceeding amount of principal

2985. This section explains what happens when the amount of the consideration paid for securities exceeds the principal secured. It is based on section 209(3AA) of ICTA.

2986. In such a case the principal secured is deemed to be increased to the amount of the consideration, for the purposes of determining whether or to what extent paragraph E in section 1000 applies. The rules in section 1007 concerning issue at a premium do not apply.

2987. An example is where the security is linked to movement in the value of a basket of shares. The amount received back by the investor could be lower than the amount paid for the security, so the value of the principal secured could be very small in such an example. This could on one view appear to be above a commercial return for that principal, but not so when viewed in relation to the amount actually paid by the investor for the security.

Section 1009: Securities reflecting dividends on certain shares etc: exclusion of section 1008

2988. This section is the first of two that qualify section 1008. It is based on section 209A(1), (2) and (4) of ICTA.

2989. The section applies where a security is linked to shares of the issuing company or any of its associated companies. The effect is that if the consideration given for the security exceeds the principal secured, the increase provided for by section 1008 is not made, but the rules in section 1007 concerning issue at a premium do apply.

2990. Section 1009 does not apply if the link to shares of a company or its associated companies arises solely because a bank or securities house has issued, as part of its normal business, securities based on a "qualifying index". This could happen if the basket of shares forming the subject matter of the index includes shares in the issuing bank itself or in one of its associated companies.

2991. The second qualification is in section 1012.

Section 1010: Meaning of "qualifying index" in section 1009

2992. This section defines "qualifying index". It is based on section 209A(3) of ICTA.

2993. The index must include shares of at least one company that is not either the issuing company or one of its associated companies, and those shares must be a "significant proportion" of the market value of the shares that make up the index.

Section 1011: Meaning of "associated company" in section 1009

2994. This section defines the term "associated company" as it applies in section 1009. It is based on section 209A(5) to (7) of ICTA.

2995. The section sets out how a person can control a company for this purpose. Any shares held on trading account (but not as part of an insurance company's long-term insurance fund) are disregarded for this purpose.

Section 1012: Hedging arrangements

2996. This section provides the second exception to section 1008. It disapplies section 1008 if there are "hedging arrangements" in place. It is based on section 209B(1) and (3) of ICTA.

2997. Section 1012 takes effect either from the time when the hedging arrangements come into effect, or from a later time in relation to earlier hedging arrangements (but only if those arrangements were in place on or after 17 April 2002). An example of the latter is where a distribution in respect of a security did not initially fall within paragraph E in section 1000, but did so subsequently and there were hedging arrangements in place before the distribution fell within paragraph E.

2998. At any time when section 1012 takes effect, paragraph E in section 1000 operates from that time as if the adjustment under section 1008, increasing the principal secured to the consideration given on issue, had not been made.

2999. For example, a security with principal secured of £100 is issued for £120. Section 1008 would normally deem the principal secured to be increased to £120, and the return would be evaluated against that amount for the purposes of paragraph E in section 1000. If hedging arrangements are subsequently put in place, the principal secured from that point onwards is £100.

3000. The definition of “hedging arrangements” is in section 1014.

Section 1013: Exception to section 1012

3001. This section sets out a series of circumstances in which section 1012 does not apply, and hence section 1008 does apply. It is based on section 209B(2), (4), (5), (6), (7) and (9) of ICTA.

3002. All the four conditions A to D must be met and have been met at all times in which any hedging arrangements have been in place in relation to that security (but only on or after 17 April 2002).

3003. Once any one of the conditions A to D in this section is not met, section 1012 applies from that point onwards, and continues to apply even if all the conditions are subsequently satisfied.

3004. The following table summarises the interaction of sections 1006 to 1013.

	Section 1008 applies?	***Section 1007applies?***
Security issued at a premium representing new consideration and the consideration is not greater than the principal secured – section 1007(1)	NO	YES
New consideration received exceeds the principal secured	YES	NO
Section 1009(1) applies – securities linked to shares	NO	YES
Section 1009(2) applies, overrides section 1009(1)	YES	NO
Section 1012 applies – hedging arrangements	NO	YES
Section 1013 applies, overrides section 1012	YES	NO

Section 1014: Meaning of "hedging arrangements"

3005. This section defines "hedging arrangements" for the purposes of sections 1012 and 1013. It is based on section 209B(8) of ICTA.

3006. The "hedging arrangements" are looked at from the point of view of the issuing company. The essence of the definition is that there is an amount of income or gain that offsets amounts that the company has to meet in relation to the security.

Section 1015: Meaning of "special securities"

3007. This section defines "special securities" for the purpose of paragraph F in clause 1000. It is based on, and covers, the various circumstances that are set out in section 209(2)(e) of ICTA.

3008. There are five sets of circumstances listed, corresponding as follows to the provisions in section 209(2)(e) of ICTA:

Condition A	section 209(2)(e)(i).
Condition B	section 209(2)(e)(ii).
Condition C	section 209(2)(e)(iii).
Condition D	section 209(2)(e)(vi).
Condition E	section 209(2)(e)(vii).

Section 1016: Meaning of "equity note" in section 1015

3009. This section provides the definition of "equity note". It is based on section 209(9) of ICTA.

Section 1017: Section 1015: other interpretation

3010. This section provides additional definitions for the purpose of section 1015. It is based on section 209(2), (3B), (10) and (11) of ICTA.

3011. *Subsection (1)* qualifies condition C in section 1015 if the return on a security is dependent on the results of the company's business. This is based on section 209(3B) of ICTA.

3012. *Subsection (2)* expands the meaning of "securities connected with shares in the company" for the purpose of condition Din section 1015. It is based on section 209(2)(e)(vi) of ICTA.

Section 1018: The principal secured: special securities

3013. This section qualifies the meaning of "principal secured" for the purposes of section 1015 if securities are issued at a premium. It is based on section 209(3) and (3A) of ICTA.

3014. The section performs the same function in relation to securities as section 1007(2) does in relation to shares. Note however that there is no equivalent of section 1007(3).

Section 1019: Relevant alternative finance return

3015. This section ensures that returns from certain alternative finance arrangements are not treated as distributions for the purposes of the Corporation Tax Acts. It is based on section 209(6A) of ICTA.

Section 1020: Transfers of assets or liabilities treated as distributions

3016. This section treats a company as making a distribution, and describes how to calculate the amount of the distribution, if assets or liabilities are transferred by a company to its members or vice versa (paragraph G in section 1000). It is based on section 209(4) of ICTA.

3017. The value of the benefit to the member is determined, and is then compared with the amount of any new consideration. If the amount given by the member is less than the value provided to the member, a distribution arises equal to the difference.

3018. This section is subject to the exceptions in section 1021.

Section 1021: Section 1020 exceptions

3019. This section sets out two circumstances where section 1020 does not apply. It is based on section 209(5) to (7) of ICTA.

3020. *Subsection (1)* sets out the two exceptions. *Subsections (2)* to *(5)* contain further interpretation.

3021. Note that if subsection (1) disapplies section 1020 and thereby takes something out of being a distribution, it is not to be treated as a distribution under paragraph B in section 1000. Section 1002(2) makes the necessary link.

Section 1022: Bonus issue following repayment of share capital treated as distribution

3022. This section sets out how a distribution can arise when a company makes a bonus issue of shares following a repayment of share capital. It is based on section 210(1) of ICTA.

3023. This section is qualified by section 1023.

3024. The rules for a repayment of share capital following a bonus issue of shares are in section 1026.

Section 1023: Exceptions to section 1022

3025. This section sets out certain exceptions to section 1022. It is based on section 210(2) to (4) of ICTA.

Section 1024: Premiums paid on redemption of share capital

3026. This section works with section 1025 to determine what is treated as a repayment of share capital. It is based on section 211(7) of ICTA.

3027. The starting point is that a premium paid on redemption of share capital is not treated as a repayment of share capital. This is further qualified by section 1025.

3028. The source legislation in section 211(7) of ICTA is not expressly limited in its application, but analysis of the legislation has shown that its practical application is limited to matters within the distributions legislation. This has now been made explicit by limiting its effect to this Chapter. See *Change 57*in Annex 1.

Section 1025: Share capital issued at a premium representing new consideration

3029. This section provides further interpretation of what constitutes a repayment of share capital. It is based on section 211(5) and (6) of ICTA.

3030. If a premium is paid by the purchaser on the issue of share capital, the amount of the premium is considered to be part of the value of that share capital for the purpose of determining what is subsequently to be treated as a repayment of share capital or as a distribution.

3031. For example, taking sections 1024 and 1025 together, if share capital with a nominal value of £100 is issued at par and is later repaid with a redemption premium of £20 then only £100 is considered to be a repayment of share capital.

3032. If, however, that same share capital was issued at an issue premium of £10, then £110 of the £120 would be regarded as a repayment of that share capital. However, all or part of the £10 issue premium is not regarded as a repayment of share capital to the extent that it has already been applied in paying up any share capital – see *subsection (3)*.

Section 1026: Distributions following a bonus issue

3033. This section sets out the circumstances in which certain distributions are not treated as repayments of share capital because they follow an earlier issue of bonus shares. It is based on section 211(1), (2) and (4) of ICTA.

3034. The section applies only if the issue of bonus shares does not fall to be treated as a qualifying distribution under another provision. A qualifying distribution is any distribution other than one that is a distribution solely because of paragraph C or D in section 1000 (see section 1136 for the definition).

3035. Distributions made more than ten years after any bonus issue can be treated as repayments of share capital provided that section 739 does not apply to the company, and provided that the shares are not redeemable share capital.

3036. Section 1027 contains a further qualification.

3037. Schedule 2 contains savings for certain bonus issues that took place before 7 April 1973.

Section 1027: Cap on amount of distributions affected by section 1026

3038. This section qualifies section 1026. It is based on section 211(1) and (3) of ICTA.

3039. The section limits the amount of the distribution to the total value of any previous bonus issues that:

- have not already been treated as distributions, and
- have not been met by new consideration (defined as the "cap").

Section 1028: Certain payments connected with exempt distributions

3040. This section affects section 1022 by treating chargeable payments made within five years of an exempt distribution as not being repayments of share capital for the purposes of those sections. It is based on sections 214 and 218(1)of ICTA.

3041. Exempt distributions and chargeable payments are dealt with in Chapter 5 (demergers). Chargeable payments are charged to income tax and corporation tax by section 1086.

Chapter 3: Matters which are not distributions

Section 1029: Overview of Chapter

3042. This section sets out the scope of the Chapter. It is new.

3043. The section refers to paragraph 6 of Schedule 12 to FA 1988. This Schedule is about change of status of building societies. It was decided to keep this material together rather than take out one small part. The Schedule has, therefore, not been rewritten.

Section 1030: Distribution in respect of share capital in a winding up

3044. This section excludes distributions made in a winding up from the scope of distributions for the purposes of the Corporation Tax Acts. It is based on section 209(1) of ICTA.

Section 1031: Distribution as part of a cross-border merger

3045. This section ensures that certain distributions made in the course of a cross-border merger are not treated as distributions for the purposes of the Corporation Tax Acts. It is based on section 209(1A) of ICTA.

3046. Provided certain conditions are met, if a company makes a distribution as part of a cross-border merger and then ceases to exist without being formally wound up, that distribution is not treated as a distribution.

Section 1032: Interest etc paid in respect of certain securities

3047. This section qualifies paragraph F in section 1000. It is based on section 212(1) and (3) of ICTA.

3048. The section excludes from the meaning of a distribution amounts paid to companies within the charge to corporation tax, but not if the distribution falls within the rules for non-commercial securities in paragraph E in section 1000.

3049. Schedule 2 contains savings for certain obligations entered into before 9 March 1982, or entered into before 1 July 1982 as a result of negotiations that were in progress before 9 March 1982.

Section 1033: Purchase by unquoted trading company of own shares

3050. This section sets out the conditions that must apply so that the purchase by an unquoted trading company of its own shares is not treated as a distribution for the purposes of the Corporation Tax Acts. It is based on sections 219 and 229(3) of ICTA.

3051. The consideration for the purchase of own shares potentially falls into the computation of a chargeable gain in the hands of the seller, subject to any necessary matters to be taken into account under the chargeable gains legislation. This was confirmed by the judgement in the Court of Appeal in Strand Options and Futures Ltd v Vojak [2004] STC 64.

3052. This section is supplemented by sections 1034 to 1048.

Section 1034: Requirements as to residence

3053. This section sets out requirements relating to the residence and ordinary residence (for tax purposes) of the seller, and includes cases where the shares are held through a nominee or by a personal representative. It is based on section 220(1), (3) and (4) of ICTA.

Section 1035: Requirement as to period of ownership

3054. This section sets a minimum period throughout which the shares disposed of must have been held, and contains rules to determine, in certain circumstances, when those shares were acquired. It is based on section 220(5), (8) and (9) of ICTA.

Section 1036: Determining the period of ownership

3055. This section deems the seller to own the shares in certain periods. It is based on section 220 (6) and (7) of ICTA.

3056. Subject to certain conditions, periods of ownership by a spouse or civil partner of the seller, or by a person whose shares are transferred to the seller under a will or intestacy, are treated as periods of ownership by the seller.

3057. The definition in section 1011 of ITA relating to married persons or civil partners living together applies for the purposes of the Income Tax Acts, which in turn include corporation tax provisions which relate to income tax. The purchase of own share rules fall within that scope. The definition of persons "living together" has been provided in this legislation to avoid the need to refer to section 1011 of ITA - see section 1116.

Section 1037: Requirement as to reduction of seller's interest as shareholder

3058. This section is the first of two that place conditions on the seller's interest in the company after the purchase by the company of its own shares. It is based on section 221(1), (2), (3) and (4) of ICTA.

3059. The seller's shareholding in the company must be reduced to no more than 75% of what it was before the company's purchase of its own shares took place. For this purpose, the shareholdings of the seller and any shareholdings of the seller's associates are looked at as one. The meaning of "associate" is provided by sections 1059 to 1061.

3060. The section is qualified generally by sections 1038 and 1043, and by sections 1039 to 1042 if the company making the purchase is a member of a group.

Section 1038: Section 1037: effect of entitlement to profits

3061. This section sets out the second condition concerning the seller's interest in the company after the purchase of its own shares. It is based on section 221(5), (6), (7) and (8) of ICTA.

3062. The seller's entitlement to the profits of the company after the purchase must be no more than 75% of what it was before the purchase. There are further requirements in section 1039 where the company is a member of a group.

Section 1039: Requirements where purchasing company is a member of a group

3063. This section supplements the requirements of sections 1037 and 1038 where the company is a member of a group. It is based on section 222(1) and (3) of ICTA.

3064. The seller's shareholding in all companies in the group must be substantially reduced after the purchase of own shares, taking into account any shares in the group held by any of the seller's associates – even if the seller holds no shares in the company making the purchase after the purchase has taken place.

3065. There are further qualifications in sections 1040 and 1043.

Section 1040: Determining whether interests as shareholders in a group are substantially reduced

3066. This section sets out how to determine whether the seller's shareholding in the purchaser's group is substantially reduced. It is based on section 222(2), (4), (5) and (6) of ICTA.

3067. The seller's shareholding in the group, taken together with any shareholdings of the seller's associates, must be no greater than 75% of what it was before the purchase of own shares took place.

Section 1041: Section 1040: effect of entitlement to profits

3068. This section stipulates that the seller's entitlement to the profits of the group must be no greater than 75% of what it was before the purchase of shares took place. It is based on section 222(7) and (8) of ICTA.

Section 1042: Other requirements

3069. This section places certain further requirements on the seller and on the transaction. It is based on section 223 of ICTA.

3070. The definition of "connected" for this purpose is in section 1062.

Section 1043: Relaxation of requirements in certain cases

3071. This section treats the seller as meeting the necessary conditions if the seller agreed to the purchase in order to permit an associate's shareholding to be substantially reduced. It is based on section 224 of ICTA.

Section 1044: Advance clearance of payments by Commissioners

3072. This section permits the company to apply to the Commissioners for HMRC for a decision whether or not section 1033 applies in respect of a particular purchase of own shares. It is based on section 225(1) of ICTA.

3073. The words "the Commissioners for Her Majesty's Revenue and Customs" have been substituted for the words "the Board" in the source legislation. This gives effect to section 50(1) and (2) of CRCA which requires references to the terms in the source legislation to be taken as references to the substituted terms.

Section 1045: Advance clearance: supplementary

3074. This section sets out time limits and further procedural rules in relation to the consideration of an application under section 1044. It is based on section 225(2) to (5) of ICTA.

Section 1046: Information and returns

3075. This section requires a company to make a return of a payment that it considers is within section 1033. It also provides fora company or any person connected with it to provide information about schemes or arrangements in relation to payments treated as falling within that section and for certain information to be provided where a payment falling within that section is received on behalf of another person It is based on section 226(1), (2) and (4) of ICTA.

Section 1047: Meaning of "group" and "51% subsidiary" in sections 1033 to 1047

3076. This section widens the general meaning of "group" and "51% subsidiary" for the purpose of the purchase of own share rules. It is based on section 222(9) to (12) of ICTA.

Section 1048: Sections 1033 to 1047: other interpretation

3077. This section contains definitions. It is based on section 229 of ICTA.

3078. The term "personal representatives" (used in *subsection (3)*)is defined for all purposes of this Act in section 1119.

3079. The reference to "trading activities" in the source is omitted as that term is not used in this part of the legislation.

Section 1049: Stock dividends

3080. This section sets out the treatment of a dividend taken in shares instead of cash, and an issue of bonus shares derived from rights attaching to those shares. It is based on sections 230 and 249 of ICTA.

3081. If the value of the shares is charged to tax as income of the recipient under ITTOIA, the issue of those shares is not treated as a distribution.

3082. The section is supplemented by sections 1050 and 1051, and there are special rules in Schedule 2 for share capital issued before 6 April 1975.

3083. Section 249(3) of ICTA is not rewritten as it is no longer needed. It introduces specific rules for income tax where two or more persons are entitled to the share capital that has been issued and provides how those rules are applied in such a case. This provision is already made for income tax by section 413(5) of ITTOIA, for the purposes of the rules in Chapter 5 of Part 4 of that Act, and has no effect for corporation tax.

3084. Schedule 1 contains consequential amendments to the provisions of ITTOIA that deal with the income tax provisions for stock dividends.

Section 1050: Application of section 1049 where bonus share capital is converted etc

3085. This section sets out the tax treatment of the shares issued in an exchange or conversion of shares that were themselves bonus shares taxed as a stock dividend. It is based on section 249(9) of ICTA.

3086. If the stock dividend was taxed as income then the issue of the replacement shares:

- is not taxed as a stock dividend,
- is not treated as a distribution, and
- is not regarded as issued for new consideration – *subsection (5).*

3087. Some bonus issues do not fall within the rules of the provisions that section 1049 rewrites, either because they were issued before the original rule was introduced (section 34 of the F(No 2)A 1975) or because the rights to the bonus issue were contained in shares issued before 6 April 1975 (the transitional rule in section 249(8) of ICTA, rewritten as paragraph 78A of Schedule 2 to ITTOIA).

3088. If this is the case, section 1049 does not apply to the replacement shares. Therefore, the issue of those shares is treated as a distribution and they are not treated as issued for new consideration – see *subsection (3).*

Section 1051: "Bonus share capital" and "in lieu of a cash dividend"

3089. This section provides interpretation for the stock dividend rules. It is based on sections 249(1) and 251(1) of ICTA.

Section 1052: Share capital to which section 1049 applies: returns

3090. This section makes provision for certain returns to be made in relation to stock dividends. It is based on section 250(1), (3), (4), (5) and (6) of ICTA.

Section 1053: Return periods

3091. This section sets out the return periods for the purposes of section 1052. It is based on section 250(2) of ICTA.

Section 1054: Building society payments

3092. This section ensures that interest or dividends paid in respect of accounts held with a building society are not treated as distributions for corporation tax purposes. It is based on section 477A(3)(b) and (9) of ICTA.

3093. Such payments are charged to income tax as interest by section 372 of ITTOIA, and to corporation tax by section 498 of CTA 2009.

Section 1055: Industrial and provident societies: interest and share dividends

3094. This section states that payments made to members by an industrial or provident society in the form of a share of profits – for example the traditional "divi" from the Co-op – is not treated as a distribution for corporation tax purposes. It is based on section 486(1) and (12) of ICTA.

3095. Such payments are charged to income tax as interest by section 379 of ITTOIA, and to corporation tax, as interest under a loan relationship, by section 499 of CTA 2009.

Section 1056: Dividend or bonus relating to transactions

3096. This section ensures that any payment made by an industrial and provident society that is deductible for corporation tax by virtue of section 132 of CTA 2009 is not treated as a distribution. It is based on section 230A of ICTA.

Section 1057: UK agricultural or fishing co-operatives: interest and share dividends

3097. This section provides the same treatment for payments made to members in the case of UK agricultural or fishing co-operatives as section 1055 provides for an industrial and provident society. It is based on section 486(1), (9) and (12) of ICTA.

Section 1058: Meaning of "UK agricultural or fishing co-operative"

3098. This section provides definitions for the purpose of section 1057. It is based on section 486(9) and (12) of ICTA.

3099. The reference in section 486(12) of ICTA to "the Department for Agriculture for Northern Ireland" is rewritten in *subsection (4)* as "the Department of Agriculture and Rural Development", its current title.

Section 1059: Associated persons

3100. This section contains the basic definition of "associate" for the provisions contained in Chapter 3. It is based on section 227(1), (2), (3), (4) and (7) of ICTA. As for section 1036 the definition of persons "living together" has been brought directly into the legislation – see section 1116.

3101. Further rules in sections 1060 and 1061 extend the meaning in the case of trustees and personal representatives.

Section 1060: Associated persons: trustees

3102. This section supplements the definition of "associate" in section 1059. It is based on section 227(5), (8) and (9) of ICTA.

Section 1061: Associated persons: personal representatives

3103. This section also supplements the definition of "associate" in section 1059. It is based on section 227(6) and (9) of ICTA.

3104. The term "personal representatives" is defined for all purposes of this Act in section 1119.

Section 1062: Connected persons

3105. This section sets out rules for identifying a "connected person" for the purposes of Chapter 3. It is based on section 228(1) to (5) of ICTA.

3106. These rules are supplemented by section 1063.

Section 1063: Section 1062: supplementary

3107. This section supplements the definitions in section 1062. It is based on section 228(6), (7) and (8) of ICTA.

Chapter 4: Special rules for distributions made by certain companies

Section 1064: Certain expenses of close companies treated as distributions

3108. This section extends the meaning of "distribution" to include certain expenses incurred by a close company in providing benefits for participators. It is based on section 418(1), (2) and (4) of ICTA.

3109. Expenses that fall within the rules are treated as distributions, the amount of the distribution being measured in the same way as under the income tax code if a benefit is provided to an employee.

3110. Clarification has been provided in *subsection (2)(b)* in relation to the question of amounts "made good" by the participator. The source legislation measures the amount of the "expense" in section 418(4) of ICTA by reference to the income tax legislation relating to employee benefits in kind – see *subsection (3)*. The amount found under those rules is the net amount after any amounts made good or contributed by the employee.

3111. The purpose of section 418(2) of ICTA is to set out the conditions for an amount to be treated as a distribution. Section 418(2) also provides that the amount of the "expense" is reduced by any amount "made good". In plain words, an amount can only be "made good" if it has been borne by the company – and if the participator has already made good any amount in arriving at the calculation in section 418(4) of ICTA then it is not possible to make it good again because the company has not borne the expense (or that part of it). Subsection (2)(b) makes this explicit.

3112. Where an amount contributed by the participator is not taken into account in the computation made using the employee benefit in kind rules, the reduction provided for in section 418(2) of ICTA can then take effect.

3113. Sections 1065 and 1066 set out two exceptions. Section 1067 contains supplementary material.

Section 1065: Exception for benefits treated as employment income etc

3114. This section sets out the first circumstance where section 1064 does not apply. It is based on section 418(3) of ICTA.

3115. The exceptions are set out in a table. The exceptions arise where the participator is also an employee within the benefit in kind rules of ITEPA (the benefits in kind rules apply instead), or in the case of certain death or retirement benefits for dependents of participators.

Section 1066: Exception for certain transfers between UK resident companies

3116. This section sets out the second exception to section 1064. It is based on section 418(5) and (6) of ICTA.

Section 1067: Companies acting in concert or under arrangements

3117. This section deals with the situation where two or more close companies act together to provide benefits to each other's participators. It is based on section 418(7) of ICTA.

3118. In such a case the benefits are deemed to be provided by a close company to its own participator and hence treated as a distribution.

3119. *Subsection (2)* makes clear that this provision applies only for the purposes of the sections rewriting section 418 of ICTA.

Section 1068: Meaning of "participator" in sections 1064 to 1067

3120. This section defines "participator" for the purposes of sections 1064 to 1067. It is based on section 417(1) and (2) of ICTA.

Section 1069: Additional persons treated as participators

3121. This section makes two extensions to the meaning of "participator" in section 1068. It is based on sections 416(2) to (6), 417(1) and (3) and 418(8) of ICTA.

Section 1070: Companies carrying on a mutual business

3122. This section restricts the application of the rules about distributions in the case of a company carrying on a mutual business. It is based on sections 6(4), 490(1) to (3) and 834(2) of ICTA.

3123. The rules about distributions only apply to such a company to the extent that distributions are made out of taxable profits or franked investment income (FII). But this limitation applies only if the distribution is made to persons who participate in the mutual business.

3124. The inclusion of FII allows the company in effect to pass dividend income to its members as its own distribution so that the members are taxable on the amount received as if they had received the dividends directly instead of earning them "through" the mutual company.

3125. If the business is a mutual life business then the distribution rules do not apply at all (that is, there is no qualification in terms of being made out of taxable profits or FII) in the case of distributions made to persons participating in that business.

Section 1071: Companies not carrying on a business

3126. This section restricts the application of the rules about distributions in the case of a company that does not carry on, or has never carried on, a trade or a business of holding investments nor has held an office. It is based on sections 6(4), 490(4) and 834(2) of ICTA.

3127. In such a case the rules about distributions are limited to amounts distributed out of taxable profits or franked investment income.

3128. Although the section reflects the application of the definition of "trade" in section 6(4) of ICTA, as applied to section 490 of ICTA by section 834(2) of ICTA, the term does not include any reference to a profession or vocation. See *Change 4* in Annex 1.

Section 1072: Members of a 90% group

3129. This section extends the meaning of distribution in the case of a company and its 90% subsidiaries. It is based on section 254(1), (3) and (4) of ICTA.

3130. If this provision applies, the distribution rules are expanded to encompass anything distributed out of assets of the company in respect of shares or securities of any company in the group, unless the distribution is to another company in the group which is UK resident.

Chapter 5: Demergers

Overview

3131. This Chapter rewrites the provisions concerning exempt distributions and chargeable payments in sections 213 to 218 of ICTA.

Section 1073: Key terms etc

3132. This section provides signposts to the key terms used in this Chapter, and to the reference to chargeable payment in section 1028. It is new.

Section 1074: Purpose of provisions about demergers

3133. This section explains the purpose of the rules concerning demergers and explains what provisions are included within the term "the provisions about demergers". It is based on section 213(1) of ICTA.

Section 1075: Exempt distributions

3134. This section states that an exempt distribution is not a distribution for the purposes of the Corporation Tax Acts, and provides a signpost to the categories of exempt distribution set out in the following three sections. It is based on sections 213(2) and (3), 213A(1) and (2) and 218(1) of ICTA.

Section 1076: Transfer of shares in subsidiaries to members

3135. This section defines the circumstances giving rise to the first type of exempt distribution. It is based on section 213(2) and (3) of ICTA.

3136. Conditions A to D are in section 1081, conditions E and F are in section 1082 and conditions L and M are in section 1085.

Section 1077: Transfer by distributing company and issue of shares by transferee company

3137. This section defines the circumstances giving rise to the second type of exempt distribution. It is based on section 213(2) and (3) of ICTA.

3138. Conditions A to D are in section 1081, conditions G to K are in section 1083 and conditions L and M are in section 1085.

Section 1078: Division of business in a cross-border transfer

3139. This section defines the circumstances giving rise to the third type of exempt distribution. It is based on section 213A(1) of ICTA.

Section 1079: "The distributing company"

3140. This section defines the term "the distributing company" for the purposes of sections 1080 to 1099. It is based on sections 213(3) and 213A(3) of ICTA.

Section 1080: Meaning of "relevant company"

3141. This section defines the term "relevant company" for the purposes of sections 1076, 1077 and 1078. It is based on sections 213(3) and 213A(3) of ICTA.

Section 1081: General conditions

3142. This section sets out the conditions (A to D) for an exempt distribution to be treated as such, and covers all exempt distributions of the first or second type – see sections 1076 and 1077. It is based on section 213(4), (5), (10) and (11) of ICTA.

3143. *Subsection (1)* reflects the amendment of section 213(4) of ICTA by the Corporation Tax (Implementation of the Mergers Directive) Regulations 2009 (SI 2009/2797). The regulations substituted the words "resident in a memberState" for the words "UK resident" to ensure that the United Kingdom is fully compliant in this context with its obligations under Directive 90/434/EEC of the European Council on cross-border mergers etc of limited liability companies.

3144. The section is supplemented by sections 1082 and 1083 which set out conditions that must be met in relation to specific types of exempt distribution.

Section 1082: Conditions for distributions within section 1076(a)

3145. This section supplements section 1081 by requiring additional conditions (E and F) to be met if the exempt distribution is of a type involving the distribution by a company to its members of shares in one or more of its 75% subsidiaries. It is based on section 213(6), (7) and (12) of ICTA.

3146. *Subsection (1)* sets out conditions relating to the company whose shares are transferred and *subsection (2)* sets out conditions relating to the company making the transfer.

3147. Condition F in *subsection (2)*, the requirement for the company making the transfer to be a trading company after the distribution, does not apply if that company is itself a 75% subsidiary. Instead, section 1085 applies.

Section 1083: Conditions for distributions within section 1077

3148. This section supplements section 1081 by requiring additional conditions (G to K) to be met if the exempt distribution consists of the transfer of a trade or trades, or shares in one or more 75% subsidiaries, followed by the issue of shares in the receiving company to the members of the company making the transfer. It is based on section 213(8) of ICTA.

3149. The company making the transfer must dispose of substantially the whole of its interest in the trade or shareholding that it transfers.

3150. Section 1084 further qualifies this section.

Section 1084: Cases where condition K does not apply

3151. This section qualifies section 1083 by setting out circumstances where one of its conditions, condition K, does not apply. It is based on section 213(9) and (12) of ICTA.

Section 1085: Conditions to be met if the distributing company is a 75% subsidiary

3152. This section applies instead of either condition F in section 1082 or condition K in section 1083 if the distributing company is itself a 75% subsidiary. It is based on section 213(12) of ICTA.

3153. Without this section a 75% subsidiary would not be able to meet the overarching requirement in section 1074(1), namely that the outcome of an exempt distribution is that a trade must be divided between two companies not in the same group or two independent groups. The categories of exempt distribution all involve transfers of shares to the members of the distributing company, and in the case of a 75% subsidiary the members would be the immediate holding company. Hence the conditions could not be met as everything would remain within the one group.

3154. The "trading company or group" condition in condition F or K of the relevant section is replaced by a requirement in *subsection (1)*about the group to which the company belongs.

3155. This section then requires further distributions, each of which must meet all the relevant tests – apart from condition F or K where the distributing company is a 75% subsidiary. The final exempt distribution in this process must therefore be made by a company which is not itself a 75% subsidiary and which is capable of meeting the requirements of section 1074(1).

Section 1086: Chargeable payments connected with exempt distributions

3156. This section sets out how a chargeable payment is charged to corporation tax or income tax, together with the condition that the charge only applies where the payment is made within five years after an exempt distribution. It is based on sections 214(1), (1A), (1B), and (6) and 215(4) of ICTA.

Section 1087: Chargeable payments not deductible in calculating profits

3157. This section sets out the corporation tax treatment for the payer of a chargeable payment made within five years after an exempt distribution. It is based on section 214(1) of ICTA.

3158. The chargeable payment is treated as a distribution for corporation tax purposes in the case of the payer. That is, the payer does not get a deduction for the payment. If the recipient is a company it is chargeable to corporation tax on the receipt – see section 1086 – despite the treatment in the hands of the payer as a distribution.

Section 1088: Meaning of "chargeable payment"

3159. This section sets out four conditions A to D, all of which must be met for a payment to be treated as a chargeable payment. It is based on section 214(2) and (3) of ICTA.

3160. This section is supplemented by section 1089 if any company concerned in the exempt distribution is an unquoted company.

Section 1089: Meaning of "chargeable payment": unquoted companies

3161. This section expands the circumstances in which Condition A in section 1088 is met if a company concerned in an exempt distribution is an unquoted company. It is based on section 214(2) and (3) of ICTA.

3162. The section sets out conditions B1, C1 and D1. These are the parallel conditions to conditions B, C and D of section 1088. They have been given different but related labels to highlight the relationship.

Section 1090: Meaning of "company concerned in an exempt distribution"

3163. This section defines the term "company concerned in an exempt distribution" for the purposes of the Chapter. It is based on section 214(4) and (5) of ICTA.

3164. This term is used in the conditions in section 1088 and the extension in section 1089.

Section 1091: Advance clearance of distributions

3165. This section allows a company to seek a ruling from the Commissioners for HMRC as to whether a distribution is treated as an exempt distribution. It is based on section 215(1) of ICTA, and is supplemented by section 1093.

3166. The words "the Commissioners for Her Majesty's Revenue and Customs" have been substituted for the words "the Board" in the source legislation. This gives effect to section 50(1) and (2) of CRCA which require references to the terms in the source legislation to be taken as references to the substituted terms.

Section 1092: Advance clearance of payments

3167. This section provides companies with an opportunity to seek advance clearance that a payment is not treated as a chargeable payment. It is based on section 215(2) and (3) of ICTA.

Section 1093: Requirements relating to applications for clearance

3168. This section sets out how an application under section 1091 or section 1092 must be made and the time limits that must be observed by the Commissioners and the company. It is based on section 215(5) of ICTA.

Section 1094: Decision of the Commissioners or tribunal

3169. This section sets out the time limit in which the Commissioners must make a decision on an application under section 1091 or section 1092 and the process for referring the application to the tribunal. It is based on section 215(6) to (8) of ICTA.

Section 1095: Exempt distributions: returns

3170. This section requires a company to make a return of an exempt distribution. It is based on section 216(1) of ICTA.

Section 1096: Chargeable payments etc: returns

3171. This section requires returns to be made in relation to chargeable payments connected with an exempt distribution. It is based on section 216(2), (3) and (4) of ICTA.

Section 1097: Information about person for whom a payment is received

3172. This section enables an officer of Revenue and Customs to require certain information of a person who receives a chargeable payment on behalf of another person, or the person on whose behalf it is received. It is based on section 217(4) of ICTA.

Section 1098: "Unquoted company"

3173. This section defines "unquoted company" for the purposes of the Chapter. It is based on section 218(1) of ICTA.

Section 1099: Other definitions etc

3174. This section contains further interpretation for the purposes of the Chapter. It is based on section 218(1), (2) and (3) of ICTA.

Chapter 6: Information and returns: further provisions

Overview

3175. This Chapter contains sections of an administrative nature that apply generally across the distributions legislation.

Section 1100: Qualifying distributions: right to request a statement

3176. This section enables the recipient of a qualifying distribution to require certain information from the payer. It is based on section 234(1) and (2) of ICTA.

Section 1101: Non-qualifying distributions etc: returns and information

3177. This section requires the payer of a distribution that is not a qualifying distribution to make certain returns and provide certain information to HMRC. It is based on section 234(5) to (8) of ICTA.

3178. The definition of what is and is not a qualifying distribution is in section 1136.

Section 1102: Non-qualifying distributions etc: additional information

3179. This section enables an officer of Revenue and Customs to require the provision of certain information in relation to distributions that are not qualifying distributions. It is based on section 234(9) of ICTA, and paragraphs 3 and 4 of Schedule 12 to FA 1989.

3180. Paragraphs 3 and 4 of Schedule 12 to FA 1989 have been rewritten here rather than being applied by cross-reference.

Section 1103: Power to modify or replace sections 1101 and 1102

3181. This section enables the Commissioners for HMRC to lay regulations amending sections 1101 and 1102. It is based on section 253 of ICTA.

Section 1104: Company distributing dividend or interest: duty to provide tax certificates

3182. This section requires a company to provide a tax certificate when it makes a distribution. It is based on section 234A(1), (2) and (3) of ICTA.

3183. The meaning of "company" is that in section 1 of the Companies Act 2006, which came into effect from 1 October 2009 as a result of article 3(a) of The Companies Act 2006 (Commencement No 8, Transitional Provisions and Savings) Order 2008, SI 2008/2860. The Companies Act 2006 (Consequential Amendments) (Taxes and National Insurance) Order 2009, SI 2009/1890 article 3 made the necessary amendment of section 234A of ICTA.

3184. Section 234A(6) has been omitted as having no effect because interest that is treated as a distribution can only be a qualifying distribution. See *Change*58 in Annex 1.

Section 1105: Duties of nominees

3185. This section places certain duties on nominees who receive distributions on behalf of others. It is based on section 234A(4) and (5) of ICTA.

Section 1106: Meaning of "tax certificate" etc

3186. This section sets out what is required in a "tax certificate" in this Chapter and provides certain other definitions. It is based on section 234A(7), (8) and (8A) of ICTA.

3187. Section 234A(6) has been omitted as having no effect because interest that is treated as a distribution can only be a qualifying distribution. See *Change*58 in Annex 1.

Section 1107: Penalties

3188. This section provides for penalties to be charged for failure to provide a tax certificate. It is based on section 234A(9) of ICTA.

Section 1108: Alternative means of compliance with sections 1104 and 1105

3189. This section enables the Commissioners for HMRC to lay regulations providing for alternative methods by which a person may comply with obligations under section 1104 or section 1105. It is based on section 234A(10) and (11) of ICTA.

Chapter 7: Tax credits

3190. This Chapter provides the rules under which a company is entitled to a tax credit and related administrative provisions. It is based on sections 231 and 252 of ICTA and paragraphs 3 and 4 of Schedule 12 to FA 1989.

3191. Sections 231AA and 231AB of ICTA are rewritten in Part 17 of this Act (see sections 808, 809 and 810). Section 231B of ICTA is not rewritten as it has only a very limited future application.

Section 1109: Tax credits for certain recipients of exempt qualifying distributions

3192. This section sets out the conditions to be met for a company to be entitled to a tax credit in relation to a distribution that it receives. It is based on section 231 of ICTA and paragraphs 3 and 4 of Schedule 12 to FA 1989. The corresponding provision for income tax is section 397 of ITTOIA.

3193. One of the conditions is that the distribution is a qualifying distribution. This term is defined in section 1136.

Section 1110: Recovery of overpaid tax credit etc

3194. This section enables an officer of Revenue and Customs to make assessments to recover tax and/or interest where a tax credit has been overpaid or a set-off of tax credit is excessive. It is based on section 252(1) and (2) of ICTA.

3195. Schedule 1 inserts the equivalent income tax provision into ITTOIA as section 401A.

Section 1111: Section 1110: supplementary

3196. This section makes further provision relating to the recovery provisions in section 1110. It is based on section 252(3) and (5) of ICTA.

Chapter 8: Interpretation of Part

Section 1112: Arrangements between companies

3197. This section extends the meaning of distribution to encompass arrangements between two or more companies to make distributions to each other's members. It is based on section 254(8) of ICTA.

Section 1113: "In respect of shares"

3198. This section provides interpretation of the term "in respect of shares in the company". It is based on section 254(1), (2), (4) and (12) of ICTA.

Section 1114: "In respect of securities"

3199. This section provides interpretation of the term "in respect of securities in the company". It is based on section 254(1), (2), (4) and (12) of ICTA.

Section 1115: "New consideration"

3200. This section provides interpretation of the term "new consideration". It is based on section 254(1), (5), (6) and (7) of ICTA.

Section 1116: References to married persons, or civil partners, living together

3201. This section contains the definition of "living together". It is based on section 1011 of ITA.

Section 1117: Other interpretation

3202. This section provides further interpretation. It is based on sections 218(1) and 254(1), (9), (10), (11) and (12) of ICTA.