

**EXPLANATORY MEMORANDUM TO
THE OFFSHORE FUNDS (TAX) REGULATIONS 2009**

2009 No.

1. This explanatory memorandum has been prepared by the Commissioners for HM Revenue and Customs, on behalf of HM Treasury, and is laid before the House of Commons by Command of Her Majesty.

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

2. **Purpose of the instrument**

- 2.1 These Regulations make new provision for the taxation of UK resident investors in offshore funds.

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

- 3.1 These Regulations are the first regulations to exercise the powers conferred by section 41(1) of the Finance Act 2008; and, in accordance with section 42A(2)(c) of that Act, have been laid in draft before the House of Commons for approval by resolution of that House. (Section 42A of the Finance Act 2008 was inserted by paragraph 5 of Schedule 22 to the Finance Act 2009.)

4. **Legislative Context**

- 4.1 The current legislation relating to the taxation of investors in offshore funds is contained in Chapter 5 of Part 17 of the Income and Corporation Taxes Act 1988 (consisting of sections 756A to 763 of that Act).
- 4.2 It is wished to make new provision for the taxation of those investors (see Part 7 of this Memorandum). Legislation providing for the making of regulations on this matter was accordingly introduced in sections 41 and 42 of the Finance Act 2008. Following the enactment of further legislation (to be found in Schedule 22 to the Finance Act 2009), the relevant primary legislation now consists of sections 40A to 42A of the Finance Act 2008. That legislation provides for the definition of the expression “offshore fund” and for the making of regulations.

5. **Territorial Extent and Application**

- 5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

The Financial Services Secretary to the Treasury (Lord Myners) has made the following statement regarding Human Rights:

“In my view the provisions of the Offshore Funds (Tax) Regulations 2009 are compatible with the Convention rights.”

7. Policy background

- 7.1 The purpose of these Regulations is to modernise the rules for the taxation of investors in offshore funds in line with the new definition in Finance Act 2009 so that, as far as possible, United Kingdom investors make their investment decisions for commercial reasons and not to obtain unintended tax advantages.
- 7.2 The Regulations originate from an announcement made by the Government in the 2007 Pre Budget Report proposing changes to the offshore funds regime. A principal objective of the proposals was to remove UK tax barriers to multi-tiered fund structures. In addition, the Government stated that it intended to legislate for a modernised offshore funds tax regime.
- 7.3 The Regulations will define certain offshore funds, as ‘reporting funds’. UK resident investors in these funds will be taxable on their share of the fund’s reported income each year. Any gain or loss on disposal will be treated as a capital gain or loss.
- 7.4 In particular it is intended to provide a facility for offshore reporting funds to enable UK investors to accumulate their taxed income in the fund, thus providing economic parity with the ownership of accumulation units in UK authorised investment funds.
- 7.5 The Regulations maintain the existing principle of treating untaxed accumulated income and gains in non-reporting offshore funds as offshore income on realisation. This is an anti-avoidance measure designed to reduce any incentive to accumulate untaxed income offshore on which an investor would, without these provisions, be subject only to tax on chargeable gains on disposal.
- 7.6 The regulations will replace, and therefore will repeal, the existing legislation relating to the taxation of UK investors in offshore funds.

8. Consultation outcome

- 8.1 The policy underlying these Regulations and drafts of these Regulations has been the subject of extensive formal public consultation. The consultation originated with “*Offshore funds: a discussion paper*” published in October

2007 followed by “Offshore funds: next steps” in March 2008”. Further consultation was carried out after the publication of “*Offshore funds: further steps*” containing draft Regulations and proposals for a new definition of an offshore fund in December 2008. As a result of the formal consultations, a number of changes have been made to the draft Regulations.

8.2 The Government intends to keep the regulations under review in the light of industry’s initial experiences of operating the new tax regime for offshore funds.

9. Guidance

9.1 Guidance on the definition of an offshore fund and on these Regulations will be published in a new HMRC Offshore Funds Manual.

10. Impact

10.1 The impact on fund businesses is to provide small positive administrative savings. The impact on business, charity or voluntary body investors is to widen potential investment options.

10.2 The impact on the public sector is negligible.

10.3 An Impact Assessment is attached to this memorandum.

11. Regulating small business

11.1 There was a wide ranging consultation on this measure and it is anticipated that the benefits and savings will be available proportionately to smaller firms.

12. Monitoring & review

12.1 The Government intends to monitor the effects of these Regulations on industry.

13. Contact

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