DechertOnPoint

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A legal update from Dechert's International and Domestic Tax Group

Offshore Funds: Changes to the New Reporting Fund Regime

Reporting Funds: Transitional Arrangements

The Offshore Funds (Tax) Regulations 2009 ('the Regulations') were finally enacted on 12 November. The Regulations implement the incoming reporting funds regime that will change the taxation treatment of UK investors in offshore funds and which take effect for accounting periods of offshore funds commencing on or after 1 December 2009.

However, on 27 November, HMRC announced proposals to amend the Regulations to change the transitional arrangements applying on the switch from the distributing to the reporting fund regime and to make other improvements. Separately Dechert have also obtained specific clarification on a number of points from HMRC.

For more information on this regime, please refer to the *DechertOnPoint* of September 2009, available at www.dechert.com/library/Tax%20_09-09_Offshore_Funds.pdf.

Points of Amendment

Provision for new funds launched during transitional period

An existing distributing fund can remain as such through its first accounting period starting after 1 December 2009. This means that an existing fund with a 31 December year end could choose to remain a distributing fund for the period ending 31 December 2010. However, HMRC have now imposed a long stop date so that this rule does not apply in respect of any accounting period ending after 31 May 2011.

When a new sub-fund or class of an existing distributing fund is launched after 1 December 2009, amendments to the Regulations will allow the transitional rules to apply to that sub-fund or class as they do to the existing fund with the result that the new sub-fund or class can also apply for distributing status.

Cross investment between reporting funds and distributing funds during the transitional period

If a reporting fund holds an investment in a distributing fund then it can treat that investment as being in a reporting fund. In other words, the reporting fund will treat whatever distribution it receives (which should be at least 85% of total income but may be more) as the reported income of the fund and will use that figure to calculate its reportable income.

If a distributing fund holds investments in a reporting fund then it can treat the investment in that reporting fund as being an investment in a qualifying fund (in other words, it will not form part of the 5% investment limit in non certified or certifiable distributing funds). For the purposes of making its own distributions, it must treat the reported income (and not just any distributed income) as income.

Exchanging an interest in a distributing fund for an interest in a reporting fund

During the transitional period, exchanging an interest in a distributing fund for an interest in a reporting fund as a part of a share reorganisation scheme will not constitute a disposal for the purposes of chargeable gains.

Grandfathered rights

If investments have been made in a fund which was not an offshore fund before 1 December 2009 then not only is capital gains treatment preserved but if that fund then becomes a reporting fund the investor will only pay tax on the amount actually distributed rather than on the whole reported amount.

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Timing

In the case of an existing fund already marketed abroad, but which is to be launched in the UK for the first time, the three months deadline for applying for reporting fund status will run from the date of the UK launch and not the start of the accounting period.

White list

HMRC have confirmed that the 'white list' which gives certain offshore funds (in particular, UCITS) certainty that qualifying transactions will not be treated as trading in nature only applies to reporting funds and not distributing funds (including those continuing to be certified as distributing funds under the transitional rules).

Practice group contacts

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