HMRC - CTM80085 - Elections

The parts of ICTA88/S247 relating to payments of dividends were repealed from 6April 1999 onwards. The remainder of S247 was repealed by FA01 in relation to payments of interest or charges made after 11 May 2001. The following page relates to periods prior to these changes.

Paying and receiving companies can make elections under:

ICTA88/S247 (1) CTM80070,

and

ICTA88/S247 (4) CTM80080,

only where both are bodies corporate resident in the UK. Where the companies are subsidiaries of the same parent company, the parent company must also be resident in theUK.

To determine whether one company is a 51% subsidiary of another, the parent company is not treated as owning share capital either:

directly or indirectly owned in a body corporate not resident in the UK,

or

indirectly owned, where the direct owner is a body corporate for which a profit on the sale of the share capital concerned would be a trading receipt.

In relation to dividends paid prior to 27 July 1989, the test of whether a company is a 51% subsidiary of another for the purposes of Section 247 (1)(a), was defined in terms of a percentage of ordinary share capital, whether held directly or indirectly.

Ordinary share capital is defined in ICTA88/S832 (1) as capital other than that giving a right only to a dividend at a fixed rate. So shares could be devised which had no practical purpose or effect other than to meet the definition of ordinary share capital. As a result of this, the holder might have 51% of the ordinary share capital as defined in Section 832 (1), yet have little economic interest in a company. Dividends could then be paid without accounting for ACT.

This was particularly significant in relation to preference share lending schemes (see CTM15210). In such a scheme, a paying company may be tax exhausted. This means that it has more losses than it can expect to use. This company will not mind whether it pays:

interest of £100 on a loan, or

a distribution of £80 and ACT of £20 in respect of shares.

However, the lending company that is liable to CT will normally prefer to receive a dividend on shares that is not taxable. Where there is no Section 247 (1) election, the Revenue receives ACT of £20, while the lending company escapes CT (at the full rate) ofsay £33. However, if the lending company holds shares which:

have rights which mean they fall within the definition of ordinary share capital, and

bring the borrowing company within the definition of a 51% subsidiary,

then the companies can make a Section 247 (1) election, which ensures that no ACT is payable.

So a ‘lending’ company would acquire enough shares to ensure that it achieved a 51% interest in ordinary share capital. To prevent such abuse FA89/S99 imposed several additional requirements for a company to meet the definition of a 51% subsidiary for Section 247 purposes. These additional requirements are now in ICTA88/S247 (8A) and ICTA88/S247 (9A). Note that these apply for the purposes of elections under Section 247(1) and Section 247 (4).

Section 247 (8A) requires that a 51% holding must:

give also a beneficial entitlement to more than 50% of any profits available for distribution to equity holders of the subsidiary, and

give the parent company beneficial entitlement to more than 50% of any assets of the subsidiary available for distribution to its equity holders on a winding-up.

Section 247 (9A) applies ICTA88/SCH18 for the purposes of Section 247 (8A), that is for determining a company’s entitlement to:

profits available for distribution, and

assets on a winding-up.

ICTA88/SCH18 contains the group relief anti-avoidance provisions (CTM81000 onwards).

Subject to this, the provisions of ICTA88/S838 on ‘ownership’, ‘ordinary share capital’ and the determination of fractional shareholdings apply.

Although a paying company may be a subsidiary within the above, an election cannot be made in respect of:

either dividends or other payments received by a company on any investments, if a profit on the sale of the investments would be a trading receipt of the company,

or

in respect of dividends, if the company receiving the dividends is an exempt person.

An election cannot apply to FID except in the very limited circumstances outlined at ICTA88/S247 5(B) to 5(D).

Guidance on the effect of the winding-up of a company on elections under Section 247 is at CTM36125.

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