

Amendment	Page	Line
70	22	5
71	22	5
72	22	11
73	22	34
74	22	36

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**Amendment 70**

Clause 25, page 22, line 5, leave out ‘same expense’ and insert ‘expense in question’.

**Amendment 71**

Clause 25, page 22, line 5, leave out from ‘be’ to ‘for’ in line 6 and insert ‘otherwise deducted or allowed in computing the income, profits or losses of any person’.

**Amendment 72**

Clause 25, page 22, line 11, leave out from ‘amount’ to ‘for’ in line 12 and insert ‘otherwise deducted or allowed’ in computing the income, profits or losses of any person’

**Amendment 73**

Clause 25, page 22, line 34, leave out ‘For the purposes’ and insert ‘Without prejudice to the generality’.

**Amendment 74**

Clause 25, page 22, line 36, leave out ‘is ’ and insert ‘ shall be treated for the purposes of subsection (6)(c) as ’.

Amendment	Page	Line
70	22	5
71	22	5
72	22	11
73	22	34
74	22	36

## EXPLANATORY NOTE

### SUMMARY

1. Clauses 24 to 31 and Schedule 3 provide new rules to prevent avoidance through arbitrage. Arbitrage is the exploitation of differences between or within national tax codes. The clauses and schedule provide a set of circumstances in which deductions may be reduced or disallowed or under which receipts will be brought into charge.
2. Clause 25 sets out how the legislation applies to restrict the amount of the deduction allowable for corporation tax purposes (the deduction rules). The clause contains two rules. The first of these (Rule A) denies a deduction to the extent that it is also deductible elsewhere. The rule will apply regardless of to whom the second deduction arises. Amendments 71 and 72 ensure that the Rule will operate in this intended fashion. Amendment 70 replaces the phrase 'same expense' with 'expense in question'.
3. The second rule (Rule B), applies where, as part of a scheme, a deduction for tax purposes is given to one party to a transaction but the recipient under that transaction is not liable to tax.
4. Amendment 73 and 74 will ensure that rule B will apply where that recipient has reduced their liability because of credits or deductions that also arise under the scheme.

### DETAILS

5. Subsection (3) of Clause 25 provides for the first condition for the application of the section ( Rule A) which is that no deduction is allowed where that expense is allowed for the purposes of any

Amendment	Page	Line
70	22	5
71	22	5
72	22	11
73	22	34
74	22	36

other tax (except special taxes that apply to UK oil companies in addition to corporation tax).

6. Subsection (4) provides that Rule A applies where the amount in question would have been deducted or allowed twice but for the operation of “a rule” similar to that in subsection (3). The result is that a deduction may be disallowed in both the UK and in other territories.
7. Amendment 70 replaces the phrase ‘same expense’ with ‘expense in question’ to make it clear that it is the expenditure giving rise to the multiple deductions that is the identified in rule A. Amendments 71 and 72 put it beyond doubt that the second deduction can arise to any person.
8. Subsection (6) of Clause 25 provides the circumstances in which the second deduction rule, Rule B, has effect. The rule will apply where a transaction or series of transactions involves a payment which creates a deduction or allowance for the payer but the recipient is not liable to tax on the receipt or has his tax liability reduced as a result of the scheme.
9. Subsection (7) refines what is meant in subsection (6) by a person having his liability to tax reduced as a result of the scheme. It provides that this happens where the payee can set-off against his income an expense or relief arising out of the scheme.
10. Amendments 73 and 74 ensure that subsection (7) continues to clarify how subsection (6) applies without restricting that application in situations not covered by subsection (7).

### BACKGROUND NOTE

11. Arbitrage is the exploitation of differences between or within national tax systems. This can result, for example, in a tax deduction being given by both the UK and another country for the

Amendment	Page	Line
70	22	5
71	22	5
72	22	11
73	22	34
74	22	36

same expense (a double dip) or a deduction being given for a payment when tax on the corresponding receipt has been avoided. A significant number of disclosures under sections 306–319 of the Finance Act 2004 (the disclosure rules) identified arbitrage.

12. The new legislation will apply only if the arrangements have been entered into to reduce UK tax and only if HMRC issues a notice directing a company to make or amend its self-assessment taking into account the rule. When it does apply, deductions forming part of an arbitrage scheme will be denied to the extent of the arbitrage and certain receipts will become taxable.
13. Draft Guidance on the application of the new rules was issued by the Inland Revenue on 16 March 2005 and was updated on 26 May 2005. That guidance made it clear that rule B will apply in the circumstances identified in the summary.