HM Treasury

HM Revenue & Customs

Non-resident companies chargeable to income tax and non-resident CGT:

summary of responses

December 2017

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Executive summary

Following consultation in spring 2017, non-UK resident companies that carry on a UK property business or have other UK property income will be charged to corporation tax, rather than being charged to income tax as at present. A non-UK resident company that has chargeable gains on the disposal of UK residential property will also be charged to corporation tax instead of capital gains tax as at present.

These changes will level the playing field, and help ensure that non-UK resident companies and UK resident companies face the same tax rules and rates on similar types of income.

The government plans to publish draft legislation in summer 2018 for technical consultation and to legislate the change in Finance Bill 2018-19. The change will come into effect on 6 April 2020.

Chapter 1
Introduction

Background

1.1 On 20 March 2017, the government published a consultation document[1] seeking views on changing the way the UK taxes rental income from UK property owned by non-UK resident companies, and gains on disposals of UK residential properties by certain non-resident companies.

1.2 The consultation focused on exploring the case for non-resident companies who are currently chargeable to income tax on UK property income and/or to non-resident Capital Gains Tax (NRCGT) on gains from UK residential property disposals to be charged to Corporation Tax (CT) instead.

1.3 The consultation document set out the background and the various reforms taking place for UK companies which gave rise to the consultation. These included the interest expense restriction and carried-forward loss reforms. These changes to the CT regime were legislated in Finance Act 2017 (No.2).

Objective of consultation

1.4 Following recent changes to the CT rules facing UK companies, the government announced that it would consider the case and options for applying the same tax rules across both non-UK resident and UK resident companies.

Overview of responses received

1.5 The government received 21 written responses to the consultation mostly from accountants and tax professionals but also from lawyers, investment businesses and representative bodies. This was followed up by four stakeholder meetings with various respondents in which further representations were made.

1.6 Most respondents agreed it would be more straightforward to bring non-resident companies within the corporate interest restriction and loss reform through the CT regime rather than try to replicate the reforms in the income tax regime.

[1] 'Non-resident companies chargeable to income tax and non-resident capital gains tax'; HM Revenue & Customs and HM Treasury, March 2017.

1.7 The respondents wanted to understand better the expected fiscal impact of the policy change and the administrative burdens that new corporation tax rules could place on the affected companies.

1.8 Many respondents felt that non-resident companies who rented UK property were specialist investors with limited familiarity with UK taxation and could face a transition cost to comply with the corporation tax regime without professional advice. If the changes were to go ahead, it was suggested that a long lead-in time would be required to enable investors to understand the requirements of the CT regime.

1.9 Most respondents felt that the NRCGT regime should remain a standalone regime.

1.10 The responses to the consultation and the government's conclusions are set out in the following chapter.

Chapter 2

Responses

Question 1a: Do you agree that it is more appropriate to apply interest restriction and loss reform to UK real property income within the CT regime rather than the income tax regime?

Table 2.A: Summary of responses to question 1a

Agreed	Disagreed	No comment/difficult to say
52%	29%	19%

2.1 Most respondents agreed that it was more appropriate to apply the corporate interest restriction and loss reforms to UK real property income within the CT regime rather than the income tax regime.

2.2 The main reason for this view was simplicity – recognising that it would be challenging to draft complex provisions for the income tax regime.

2.3 Some of the respondents who disagreed wanted to understand better whether the extra tax that might be raised from this change would be worth the additional compliance burden placed on the affected companies.

2.4 One respondent stated that corporate interest restrictions should not apply to non-resident companies investing in UK property because this could result in deductions being disallowed where the debt is entirely third party lending on commercial terms. This in turn could result in non-resident companies reducing their investment in UK property.

2.5 Another respondent questioned the proposed treatment of commercial property held through non-resident trusts, such as "Jersey property unit trusts".

2.6 Most respondents favoured April 2019 as the earliest date for change.

Government response

2.7 The government agrees that there is a good case to bring the UK property income of non-UK resident companies within the corporation tax regime. This will ensure that the interest and loss rules are applied in the same way to UK and non-UK resident companies. This change will include non-UK resident companies who have invested in non-resident property unit trusts in respect of UK property. The government proposes to bring in this change with effect from 6 April 2020 which will allow affected companies sufficient time to familiarise themselves with the CT regime and its requirements. An assessment of the impact of this change will be published in due course.

Question 1b: If you consider that they could be applied within income tax, how would the interest restriction and loss reforms be applied in a consistent manner to companies within CT?

2.8 Some respondents observed that in order to mirror the corporate interest restriction and loss reform rules in the current income tax regime, the legal concept of an income tax grouping would first have to be introduced.

2.9 One respondent did recommend that that the government should amend the income tax code and introduce similar reforms. However, most respondents recognised that it would be challenging and complex to draft consistent provisions for the income tax regime.

Government response

2.10 The government agrees that it is simpler to apply the existing CT rules rather than replicate these rules within income tax.

Question 2: If non-resident companies liable to NRCGT are brought within CT, what features of the NRCGT provisions do you think may give rise to difficulties if adapted for CT?

2.11 Most respondents felt that the NRCGT regime should remain as a stand-alone regime. However, if the regime was brought into corporation tax, the payment date of the related capital gains tax should be aligned with the CT payment date, rather than the current time frame of within 30 days of completion.

2.12 The replacement of pooling rules with grouping rules and indexation were identified as provisions that could give rise to difficulties when adapted for CT. Some responses recommended that if NRCGT became part of the CT regime, an election (under section 171A of TCGA 1992) to reallocate gains and losses to another member of a company group should be made available and that the existing exemptions should be maintained.

2.13 Unrelated to the question posed by the consultation, there was a consensus that if NRCGT was brought within CT then this should also apply to gains related to the Annual Tax on Enveloped Dwelling (ATED). ATED and ATED-related gains were highlighted as an area of complexity and simplification in this area was encouraged.

Government response

2.14 The government intends that a non-UK resident company that has chargeable gains on the disposal of UK residential property under the existing NRCGT regime will be charged to corporation tax instead of capital gains tax as at present.

2.15 As announced at Autumn Budget 2017, the government will tax gains arising on all disposals of UK immoveable property by non-UK resident companies from April 2019. Together with the measure that is the focus of this document, these complementary changes introduce a comprehensive approach to taxing non-residents' gain on UK property. The changes bring the UK in line with other countries' approach to taxing non-resident property gains and removes an advantage which non-residents have over residents. Further consideration to ATED-related gains will be given alongside the technical consultation of this policy.

2.16 Subject to the government's response to the new consultation, it is intended that the existing NRCGT computational rules will continue to apply and for an election under section 171A of TCGA 1992 to be available. Consideration will be given to the repeal of the NRCGT pooling arrangements at section 188D of TCGA 1992.

2.17 Notification of chargeability and payment of any liability will be aligned with corporation tax requirements. The non-UK resident company will be required to register for CT Self-Assessment (CTSA), and will return the gain or loss within the CTSA framework, and pay any tax to the CTSA timescales as applicable. If the seller is within the CTSA framework already for other reasons, they will use their normal accounting period. Otherwise the accounting period will be a period of one day beginning and ending on the date of disposal.

Question 3: Is there an alternative approach that could be taken in calculating the taxable profits or losses of a UK property business carried on by a non-resident company? If they differ to those applied to a UK resident company carrying on a similar property business, please explain why different rules should apply.

2.18 A number of respondents agreed that profits should be calculated in the same manner as a UK resident company, as outlined by the consultation document.

2.19 Real Estate Investment Trusts (REITs) allow for payable interest to be given as a deduction in computing profits. Some respondents proposed that the treatment of interest payable by REITs could be applied to non-UK resident companies with a UK property business, rather than require its separate calculation of its interest expense under the loan relationship regime.

2.20 One respondent suggested that the final basis period for income tax purposes should end on 31 March since this is a commonly used accounting period end date. Another respondent suggested applying the corporation tax rules from 6 April but applying a light touch on 31 March accounting periods, and deem them to end on 5 April. The property business would be deemed to be a continuing business with profits being apportioned to corporation tax on a time apportioned basis with adjustments being made for any profits which would fall out of account during the transition from income tax to CT.

2.21 A further proposal was that only companies of a certain size should be subject to the CT regime. For example, it was suggested that a company with assets in excess of £50 million would be subject to CT, whereas a company with assets of £10 million would be subject to income tax.

Government response

2.22 The government intends that corporation tax will apply to non-UK resident companies with a UK property business from 6 April 2020. This means that the final basis period for income tax purposes will end on 5 April 2020.

2.23 Since the basis period for property profits under the income tax rules is the same as the tax year, the government does not envisage that this will create any difficulty. The government has identified that a change to the income tax basis period will be needed if the non-UK resident company is a partner in a firm which also has property income. Transitional provisions will be made to ensure that no profits fall out of account or are doubly taxed because of this change.

2.24 The government intends for the existing rules for loan relationships, financial derivatives and the anti-hybrid rules to apply to non-UK resident companies with a UK property business in the same way as they are applied to a UK resident company with a UK property business outside of a REIT.

2.25 The government has no plans to differentiate between the size of companies before the corporation tax regime can apply to them as it believes that this will introduce considerable complexity into the tax system.

Question 4: Irrespective of the tax regime, what would be the effect on non-resident companies from the application of corporate interest restriction? Please explain how any effect is different to the effect on UK resident companies.

2.26 It was acknowledged that the consistent application of the CT regime would level the playing field between resident and non-UK resident companies. However, requiring compliance with a new regime with additional rules could introduce a transitional administrative burden for non-UK resident companies, and could make the UK property market less attractive to investors.

2.27 The proposal to allow non-UK resident companies access to the £2 million de minimis provision and public benefit infrastructure exemption was welcomed. One of the respondents identified that to benefit from the public infrastructure rules the non-resident company would have to be fully taxed in the UK on all its activities.

2.28 The application of the Disregard Regulations was discussed in a number of responses. It was raised whether an election under Regulation 6A of the Disregard Regulations would need to be made where there is a hedging treatment of an interest rate contract to which Regulation 9 could potentially apply. One of the respondents proposed deeming an election to have been made under the Disregard Regulations unless the customer opts out.

Government response

2.29 The government firmly believes that the UK remains an attractive place for domestic and foreign investment in real estate.

2.30 The government welcomed the recognition of the principle of a level playing field between resident and non-UK resident companies.

2.31 The interest restriction has been through detailed consultation with interested stakeholders. The government intends that the rules will apply to non-UK resident companies in the same way as they apply to UK resident companies.

2.32 The Disregard Regulations will be available once the company comes within the charge to corporation tax. The government is reviewing the application of the Disregard Regulations so that in certain situations the existing treatment of fair value movements can be maintained. This will ensure that the right amounts are brought into account over the term of the derivative contract.

Question 5a: Do you agree that relief for management expenses for non-resident companies should be limited to those which are directly linked to the taxable UK sourced income?

Table 2.B: Summary of responses to Question 5a

Agreed	Disagreed	No comment
65%	10%	25%

2.33 The majority of the respondents agreed that CT relief for management expenses for non-resident companies should be limited to those which are directly linked to the taxable UK sourced income.

2.34 It was also suggested that expenses such as audit fees, legal and accounting costs should be deductible on a just and reasonable basis.

Government response

2.35 The government intends for the rules on management expenses to be applied to non-UK resident companies carrying on a UK property business or in receipt of other UK property income in the same way as they are applied to UK resident companies.

Question 5b: What are your views on the extinguishing of unused property losses at the point the UK property business has ceased?

2.36 If a UK property business comes to an end and has unutilised losses (i.e. it is not able to surrender the losses as group relief), those losses are generally carried forward as management expenses if the company continues to be a company with investment business.

2.37 Most respondents thought that a non-UK resident company would not have other profits chargeable to corporation tax if its UK property business ceased. Consequently, it was unlikely that any unused loss would be converted to management expenses going forward.

2.38 The respondents on this issue thought that the unused loss should be capable of being reinstated if the UK property business recommenced at a later date. An example was cited of the due diligence required before entering into an investment in real estate, which could create a time period from the disposal of the old investment and the acquisition of the new investment outside of the control of the investing company during which there was no rental activity.

2.39 It was also suggested that group relief should be available during the period of cessation since this is the treatment available to UK resident companies. The availability of terminal loss relief was recommended, as well as the ability of the non-resident company to be able to set the losses off against future profits or investments.

Government response

2.40 The government intends that the rules for loss relief and group relief will apply to a CT property loss from a UK property business of a non-UK resident company in the same way as they are applied to a UK resident company.

2.41 Terminal loss relief is only available in respect of trading losses and that rule applies for all companies, UK resident or otherwise.

Question 6: Do you think that the suggested treatment of the unused income tax losses carried forward is reasonable? If you consider that there is an alternative approach, please explain what that would encompass.

Table 2.C: Summary of responses to Question 6

Agreed	Disagreed	No comment
70%	10%	20%

2.42 All respondents welcomed the proposal that the affected companies would not be required to recalculate the losses incurred under the income tax rules by reference to the CT rules.

2.43 The majority of the respondents agreed that the proposed "grandfathering" of the unused income tax losses was reasonable subject to the assumption that the losses could be offset without the 50% carried-forward loss restriction. Clarification was sought about whether these Income Tax Property Losses ("ITPL") could be set against property profits arising from property acquired after the date when the UK property business profits or other UK property income of the non-UK resident company came within the CT regime.

2.44 One respondent asked whether the 50% loss restriction was to be calculated before or after the use of any brought forward ITPL. Another asked if the ITPL would need to be partially recalculated if any non-trade loan relationship profits were to be separately taxable.

2.45 One respondent proposed that ITPL arising after the introduction of the CT loss reform should also benefit from the flexibility provided by the reform. It was proposed that in-year group relief should be permitted for both brought forward and current year losses to be surrendered to non-UK resident group companies with a taxable UK source income.

2.46 Other respondents suggested that while the streaming of the ITPL added a level of complexity, it was nevertheless a logical approach and was consistent with the treatment of CT losses incurred prior to April 2017.

2.47 Some respondents proposed alternative treatments. It was suggested that it would be simpler to treat all income tax losses as converting to UK property business losses on transition rather than having two different types of losses. There was also a recommendation that the unused losses should be permitted to be offset against any gain on the property should the rental business cease prior to the disposal of the property.

Government response

2.48 As indicated in the consultation document, the government intends to import the unused ITPL into the corporation tax regime without requiring that historic loss to be recomputed under corporation tax principles. The government thinks that it would be overly burdensome to do this because of the different treatment of the interest expense between the income tax and corporation tax regimes.

2.49 The ITPL can be carried forward and used without restriction so long as the company continues to carry on its UK property business. Only the residual taxable property profits will be subject to the 50% loss restriction.

Case study

Assume that a non-UK resident company has UK property income of £500. It has carried-forward ITPL of £50 and carried-forward CT property losses of £150. The property profits are the company's only profits. For simplicity, ignore the £5 million deductions allowance available to groups or standalone companies that are not subject to restriction:

- the unused ITPL will automatically reduce the property income to £450
- the property profits of £450 will be included in the figures of non-trading profits and total profits
- for the purposes of the loss restriction the company's relevant profits are £450
- the relevant maximum for carried-forward loss relief is: £450 x 50% = £225

This means that the company can use its brought-forward CT property loss of £150 in full. It also has capacity to claim group relief up to an amount of £75 (£225 - £150) from a fellow group company which meets the relevant conditions to surrender its losses to the non-UK resident company.

2.50 As the above case study shows, corporation tax losses and the ITPL are to be carried forward separately so that the reform to the CT loss relief rules will apply in the same way to the corporation tax losses of non-UK resident companies as to CT losses of UK resident companies. Since CT losses from 1 April 2017 are to be tracked separately from CT losses incurred before that date, the government does not think that also separately tracking the unused ITPL will be burdensome.

Question 7: Are there other CT principles that you think would require transitional arrangements to be provided for?

2.51 A common concern centred on the administrative transitional arrangements potentially required such as iXBRL tagging of returns, timing of payments, payments on account, apportionment of profits for a period which straddled both the income tax and corporation tax regimes and whether new unique taxpayer references for CT would be needed. There was a consensus that there should not be a requirement for balancing allowances or charges for Capital Allowances purposes.

2.52 Some respondents identified an impact on the Non-resident Landlord Scheme ("NRLS") and sought confirmation that credit for any income tax suffered would be available to offset against any CT liability and to exclude those companies who would be within the Quarterly Instalment Payments regime.

2.53 Most respondents identified the need for transitional provisions with regard to the loan relationship and derivative contracts regime together with the Disregard Regulations. The concern mainly centred on the date when it was possible to make an election under the Disregard Regulations and the valuation of existing loan relationships and derivatives at the time the UK property business came within the scope of corporation tax. It was questioned how those rules applied to loan waivers of debts attributable to the income tax period and how the connected party rules applied at the date of transition. Some of the respondents also proposed grandfathering existing hedging agreements.

2.54 One respondent proposed that existing long-term loan relationships should be grandfathered so that the Distribution rules at Part 23 of the Corporation Tax Act 2010 would not apply to them. Another respondent highlighted that the transition adjustments under IFRS and FRS102 accounting standards and the 10-year spreading rule might be impacted by the proposed change in tax regime.

2.55 Making Tax Digital was highlighted in a large number of the responses, with a recommendation that it should not apply to non-resident companies until the same time as it is applied to UK resident companies.

2.56 One respondent sought confirmation that the proposed change in tax regimes would not alter the existing view that payments of interest under the NRLS have a UK source. Some sought confirmation that group relief would be available as it is for UK resident companies. Others sought confirmation that a non-UK resident company would be able to make a claim for land remediation relief.

2.57 Another respondent proposed that any accrued expenses or rent received in advance should be treated as incurred or received by the CT property business as a simplification. Reference was also made to the then draft clause in the Finance Bill 2017 to apply cash basis accounting to property businesses liable to income tax under which it was thought that non-UK resident property rental companies could find themselves moving in and out of the cash basis. A provision to prevent this was sought.

2.58 One respondent questioned whether CT would apply to non-property income where, under double tax agreements, the UK had ceded its taxing rights.

2.59 A number of respondents highlighted the importance of tax education of the non-resident companies, especially in complex areas such as the loan relationship regime.

Government response

2.60 The government will consider the suggestions and recommendations put forward as it finalises the details of the policy. To ensure the provisions work as intended, the government will conduct a technical consultation on the draft legislation in due course. There will be a need for transitional provisions to help manage the change from income tax to corporation tax.

2.61 The government confirms that the corporation tax rules will apply to non-UK resident companies as those rules are applied to UK resident companies. That will include, for example, the operation of rules such as group relief, land remediation relief, anti-hybrid rules and the unallowable purpose rules. The same filing requirements for tax returns and to notify chargeability under corporation tax will apply to UK and non-UK resident companies.

2.62 The government is confident that bringing the profits of a UK property business within the corporation tax rules and the consequent application of the loan relationship rules to that business will be in compliance with the UK's international obligations.

2.63 The government will ensure that affected companies are informed of the changes to their tax records, such as its new corporation tax taxpayer reference. The government acknowledges the importance of providing clear guidance to those customers about this change.

Question 8: Do you have any comments on the assessment of equality and the impact on business as a result of this potential change in tax regimes?

2.64 A number of respondents wanted to understand better the administrative impact of this change, particularly on smaller non-UK resident companies. It was proposed that ways should be explored to help smaller non-UK resident companies with the new regime.

2.65 Other respondents asserted that this change would complicate the tax code and introduce changes to the UK tax system thus affecting the attractiveness of the UK as an investment location. In order to reduce this negative impact, it was recommended that this change was communicated clearly and implemented smoothly.

2.66 Several respondents suggested there should be a 12-month period before implementation which would allow international businesses to understand and adjust to the regime accordingly.

Government response

2.67 An assessment of the impact of the changes will be published in due course.

2.68 The government considers that this change will create a fairer regime by helping ensure that UK and non-UK resident companies will be subject to the same tax rates and rules on similar types of income.

2.69 The UK's competitive tax regime mean it will continue to be an attractive destination for investors.

Chapter 3
Next steps

Legislation

3.1 The government will consider the suggestions and recommendations put forward as it finalises the details of the policy.

3.2 The government plans to publish an Explanatory Note and draft legislation in summer 2018 as part of a technical consultation for legislation in Finance Bill 2018/19.

3.3 The government will ensure that affected customers are informed of the changes to their customer records such as its new CT taxpayer reference as part of this proposed change and will develop clear guidance about this change.

3.4 Advisors are requested to ensure that they have obtained authority from their clients to act for them in relation to their corporation tax affairs.

Annex A
List of stakeholders consulted

One individual

Ashurst LLP

The Association of Investment Companies

BDO LLP

BlackRock

British Property Federation

The Chartered Institute of Taxation (two responses)

Deloitte LLP

Ernst & Young LLP

Eversheds Sutherland (International) LLP

Fladgate LLP

FTI Consulting LLP

Grant Thornton UK LLP

The Institute of Chartered Accountants in England and Wales

Kingston Smith LLP

KPMG LLP

The Law Society of England and Wales

MK Tax LLC

PricewaterhouseCoopers LLP

The Society of Trust and Estate Practitioners

HM Treasury contacts

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If you require this information in an alternative format or have general enquiries about HM Treasury and its work, contact:

Correspondence Team
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Tel: 020 7270 5000

Email: public.enquiries@hmtreasury.gsi.gov.uk