Clause 1 and Schedule 1: Corporate interest restriction

Summary

1. Clause 1 and Schedule 1 introduce a restriction on the amount of interest and other financing amounts that a company may deduct in computing its profits for corporation tax purposes. The legislation takes effect from 1 April 2017.

Details of the clause and schedule

2. Clause 1 introduces Schedule 1.

Schedule 1

Part 1: New Part 10 of TIOPA 2010

3. Part 1 of Schedule 1 introduces a new Part 10 into the Taxation (International and Other Provisions) Act 2010 (TIOPA). In consequence, the existing Part 10 of TIOPA is renumbered as Part 11, and certain further consequential changes are made (see paragraph 10 in Part 3 of the schedule).

Chapter 1: Introduction

4. New Section 372 sets out an overview of the new Part 10 and provides brief details about the contents of each chapter. Chapters 2 to 5 contain the main rules by which any interest restriction is calculated. In particular, section 372(4) introduces key terms defined in Chapter 3 involving “tax-interest”. This is a company’s or group’s interest and similar amounts which are included in the UK tax computations. These are the amounts that are potentially restricted under these provisions.

5. Chapters 6 and 7 define key concepts. In particular, section 372(7)-(8) introduces key terms defined in Chapters 6 and 7 involving “tax-EBITDA”. This is a company’s or a group’s taxable earnings before interest, tax, depreciation and amortisation, and is an important part of the calculation of an interest restriction. These are the amounts that form the basis of the worldwide group’s interest capacity for the period, and hence determine the amount of tax-interest amounts that may be deducted.

6. New section 373 sets out the meaning of certain terms used in the new Part 10. Those terms are described by reference to a “period of account” for a “worldwide group”. Throughout this legislation “period of account” is used to describe the period by reference to which the group draws up its accounts. That period may not necessarily match the accounting periods used by some of the companies within the group. The

term "accounting period" is used to refer to the period by reference to which a company computes its profits chargeable to UK corporation tax.

7. New Section 374 introduces new Schedule 7A to TIOPA. This schedule contains administrative provisions including the interest restriction return, enquiry powers and information powers.

Chapter 2: Disallowance and reactivation of tax-interest expense amounts

8. New Section 375 sets out how tax deductions are disallowed where a full interest restriction return is submitted (section 376 covers the situation where only an abbreviated return, or no such return, is submitted). Section 375(2) specifies that a company must disallow deductions in the amounts set out in the return. There is further provision in section 377 as to which deductions must be disallowed.

9. Section 375(3)-(5) covers the situation where a "non-consenting company", as defined in paragraph 10 of Schedule 7A, does not give its agreement (or withdraws its agreement) to be bound by the amount allocated to it in the return. The distinction between consenting and non-consenting companies is made to help the group manage possible conflicts of interest where a member of the group has a significant shareholder who holds a minority interest in the company, or where insolvency arrangements come into effect. In such a case, the company may elect not to disallow the amount allocated to it in the interest restriction return. It might so elect if it disagrees with the way the amount to be allocated has been calculated. Such an election may be withdrawn. Where an election is in effect the company must disallow a pro-rated amount as allocated to the accounting period under paragraphs 23 and 24 of Schedule 7A.

10. New Section 376 sets out how tax deductions are disallowed where only an abbreviated interest restriction return, or no such return, is submitted (section 375 covers the situation where a full return is submitted). This section takes effect after 12 months have elapsed from the end of the period of account. Section 376(6) specifies that a company must disallow deductions in any accounting period in accordance with the amount of disallowance due to it under the pro-rating rules in paragraph 24 of Schedule 7A.

11. New Section 377 sets out how to identify the amounts to be restricted under section 375(2), 375(4) or 376(6). Section 377(2) sets out the default order in which amounts are disallowed. Section 377(3) allows a company to elect out of the default order and choose what tax-interest expense amounts it disallows.

12. New Section 378 provides that any deduction that has been disallowed under section 375 or section 376 may be carried forward to a later period where it may potentially be the subject of a "reactivation". Section 378(3) stops the carry-forward of disallowed trading expenses once the company ceases to trade or the trading activities have become small or negligible. Section 378(4)-(5) applies in a similar way where the trade becomes uncommercial and is not carried on in the exercise of a statutory function (within the meaning of section 44 of the Corporation Tax Act 2010

(CTA 2010)). Section 378(7) specifies, for the avoidance of doubt, that if a disallowed deduction is reactivated and allowed in a subsequent period, then it is extinguished and cannot be carried forward again.

13. New Section 379 provides for disallowed amounts to be reactivated and allowed in later periods. Section 379(1) allows the reactivation of amounts brought forward only in a period for which a full interest restriction return has been submitted (see paragraph 20(3) of Schedule 7A) and where that return includes a statement of allocated interest reactivations (see paragraph 20(3)(f)(iii) of Schedule 7A). Section 379(2)-(4) requires a company that has an accounting period to which a reactivation is allocated to give effect to that allocation.

14. New Section 380 sets out the amounts to be reactivated by a company when required to do so under section 379. Section 380(2) sets out the default order in which amounts are reactivated where the company does not exercise its right to choose. Section 380(3) allows a company to elect out of the default order and choose what tax-interest expense amounts it reactivates. Section 380(4) specifies that the tax-interest expense amounts reactivated are to be included in the company's election.

15. New Section 381 covers the uncommon situation where a company, in relation to one of its accounting periods, must disallow a deduction of that period and also reactivate an amount carried forward from an earlier period. The amounts of disallowance and reactivation must in effect be set off against each other, with only the net result being given effect.

Chapter 3: Tax-interest amounts

16. New Section 382 sets out the meaning of the term "tax-interest expense amount" by reference to three conditions, only one of which needs to be met to satisfy the definition. In particular the amount must be a relevant loan relationship debit (section 383), a relevant derivative contract debit (section 384) or a financing cost implicit in amounts payable under a relevant arrangement, which includes finance leases, debt factoring and service concession arrangements accounted for as a financial liability (section 382(5)).

17. Section 382(7)-(9) sets out the treatment of a "disregarded period", which is where the company's accounting period does not exactly align with the group's period of account. Amounts are attributed to the disregard period on a just and reasonable basis, for example having regard to:

- The period in which amounts would be recognised in the company's financial statements if they were drawn up for particular periods.
- The period in which amounts would be brought into account by the company if it had a different accounting period.
- Ensuring that the amounts are in total fully attributed. In other words, if the accounting period is broken up into a number of periods which do not overlap and which, taken together, completely align with the

accounting period in question, the total of the amounts attributed to those periods must equal the amount being attributed.

18. Section 382(10)-(11) operates in certain cases where tax rules provide for a deduction and amounts have previously been disallowed. Where the disallowed amounts would have been an amount of tax-interest expense then the amounts now deductible are likewise treated as being amounts of tax-interest expense.

19. New Section 383 sets out the meaning of "relevant loan relationship debits". These are debits brought into account under the loan relationship provisions provided they are not excluded debits. A debit will be excluded if it is in respect of an exchange loss or impairment loss.

20. New Section 384 sets out the meaning of "relevant derivative contract debits". These are certain debits brought into account under the derivative contract provisions, depending on the underlying subject matter of the derivative. A debit will be excluded if it is in respect of an exchange loss or impairment loss. A debit will also be excluded where it arises from a derivative that is not related to the capital structure of the company or the group.

21. New Section 385 sets out the meaning of "tax-interest income amounts" by reference to four conditions, only one of which needs to be met to satisfy the definition. In particular the amount must be a relevant loan relationship credit (section 386), a relevant derivative contract credit (section 387), a financing cost implicit in amounts receivable under a relevant arrangement which includes finance leases, debt factoring and service concession arrangements accounted for as a financial asset, (section 385(5)) or an amount receivable for providing a guarantee (section 385(6)).

22. Section 385(8)-(10) sets out the treatment of a "disregarded period" which is where the company's accounting period does not exactly align with the group's accounting period. Amounts are attributed to the disregarded period on a just and reasonable basis, for example having regard to:

    - The period in which amounts would be recognised in the company's financial statements if they were drawn up for particular periods.
    - The period in which amounts would be brought into account by the company if it had a different accounting period.
    - Ensuring that the amounts are in total fully attributed. In other words, if the accounting period is broken up into a number of periods which do not overlap and which, taken together, completely align with the accounting period in question, the total of the amounts attributed to those periods must equal the amount being attributed.

23. New Section 386 sets out the meaning of "relevant loan relationship credits". These are credits brought into account under the loan relationship provisions provided they are not excluded credits. A credit will be excluded if it is in respect of an exchange

gain or reversal of an impairment loss.

24. New Section 387 sets out the meaning of "relevant derivative contract credits". These are certain credits brought into account under the derivative contract provisions, depending on the underlying subject matter of the derivative. A credit will be excluded if it is in respect of an exchange gain or reversal of an impairment loss. A credit will also be excluded where it arises from a derivative that is not related to the capital structure of the company or the group.

25. New Section 388 provides for double taxation relief. It does this by excluding from the "tax-interest income amount" any amount to the extent that it consists of "notional untaxed income". The section sets out the formula used to calculate this amount, which is the amount of credit for foreign tax given by section 18(2) of TIOPA, divided by the rate of Corporation Tax. So, for example, where the amount of credit for foreign tax is £100 and the rate of Corporation Tax is 19%, the notional untaxed income is £526 (= £100 ÷ 19%).

26. New Section 389 sets out the meaning of the "net tax-interest expense" and "net tax-interest income" of a company. These are calculated by comparing the company's "tax-interest income amounts" (section 385) with its "tax-interest expense amounts" (section 382).

27. New Section 390 sets out the meaning of the worldwide group's "aggregate net tax-interest expense" and "aggregate net tax-interest income". These are the difference between the sum of each relevant company's "net tax-interest expense amount" and the sum of its "net tax-interest income amount" for the period.

28. New Section 391 sets out the meaning of "impairment loss". This is important for looking at which credits and debits are excluded from the definition of "tax-interest" (see, for example, section 383(3)(b)).

Chapter 4: Interest Capacity

29. New Section 392 defines the "interest capacity" of a worldwide group for a period of account. Interest capacity is the aggregate of the interest allowance of the period and any unused interest allowance carried forward from an earlier period that is available in the current period. However a *de minimis* amount of £2m per annum is used if that gives a bigger capacity. "Interest allowance" is defined in Chapter 5.

30. New Section 393 sets out how much interest allowance of a period ("the originating period") is available in a later period for the group. It is nil if a full interest restriction return has not been submitted for the period of account (section 393(5)). Otherwise it is the lower of two amounts: A and B:

    - "A" is a measure of how much interest allowance is available because it has not yet been used up. See section 394.
    - "B" is a measure of how much interest allowance is available because it has not yet expired (the carry-forward of unused interest allowance is subject to a five year time limit). See section 395.

31. New Section 394 determines the extent to which interest allowance is "used", for the purpose of calculating how much interest allowance of an originating period is available in a later period. Interest allowance is "used" where it allows the group to obtain a deduction for tax-interest amounts. Section 394(2) sets out how much interest allowance is used in the originating period, and section 394(3)-(5) sets out how much interest allowance of the originating period is used in a later "receiving" period. The sum of these two amounts is the amount of interest allowance that has been "used".

32. Section 394(3) sets out the amount of the interest allowance from the originating period that is used in a receiving period. It is the amount calculated in section 394(4), but this is limited so that it cannot exceed the total amount of the allowance from the originating period that is available in the receiving period (section 394(5)).

33. Section 394(4) defines "the relevant part of the aggregate net tax-interest expense of the group for the receiving period". This is the amount of the interest expense of the receiving period that is not covered or franked by either: (i) the interest allowance of the receiving period; or (ii) the interest allowance of any period that is earlier than the originating period, that is carried forward and used in the receiving period. It is therefore the amount of the interest expense of the receiving period left over that can consume the interest allowance carried forward from the originating period.

34. The formula used can give a negative amount where the amount of interest allowance of the receiving period exceeds the aggregate net tax-interest of the receiving period. In such a case, the amount calculated is set to nil by section 394(5).

35. New Section 395 determines the extent to which interest allowance is "unexpired", for the purpose of calculating how much interest allowance of an "originating period" is available in a later period under section 393. The rules set out how the five year limit for carrying forward unused interest allowance should be applied. Section 395(2) and (3) sets out the circumstances where, respectively, all or none of the interest allowance of the originating period is unexpired in a later "receiving period". The remainder of the section deals with situations where part is unexpired.

36. Section 395(4), (6), and (8) describes three different scenarios. There is a different result for each scenario, as laid out respectively in section 395(5), (7) and (9). Note that that the result in section 395(9) is the lower of the amounts given by section 395(5) and 395(7).

37. To understand the different scenarios, it can be helpful to think of the notional period that would result from moving the originating period forward five years.

- Section 395(4): the receiving period falls entirely within the notional period.
- Section 395(6): the notional period falls entirely within the receiving period.
- Section 395(8): the receiving period overlaps the notional period, but

starts after the notional period starts and ends after the notional period ends.

38. Section 395(5) determines the amount of interest allowance for the originating period that is unexpired in the receiving period where section 395(4) applies. This is an amount equal to the interest allowance of the originating period to the extent (if any) that it exceeds the aggregate net tax-interest expense for the originating period, multiplied by a fraction. The fraction is the number of days in the notional period that fall after the start of the receiving period, divided by the total number of days in the originating period. This effectively expires the amount of interest allowance generated in the part of the originating period that falls more than five years before the receiving period starts.

39. Section 395(7) determines the amount of interest allowance for the originating period that is unexpired in the receiving period where section 395(6) applies. In the circumstances described in section 395(6), all of the interest allowance from the originating period is "in time" to be used for the start of the receiving period. However not all of the interest expense in the receiving period can access the allowance. So section 395(7) prevents the inappropriate set off of interest allowance from the originating period against interest expense that arises more than five years after the originating period ends. This is achieved by looking at the aggregate net tax-interest expense in the receiving period to the extent it exceeds the interest allowance of that period, and excluding on a pro-rata basis the expense that arises more than five years after the originating period ends

40. The amount calculated under section 395(7) is equal to the aggregate net tax-interest expense of the receiving period to the extent (if any) that it exceeds the interest allowance for the receiving period, multiplied by a fraction. The fraction is the number of days in the receiving period that fall before the end of the notional period, divided by the total number of days in the receiving period.

41. The calculation could give an amount that exceeds the total interest allowance of the originating period. However, the calculation can never lead to an inappropriately large amount of interest allowance being available in a later period because of the way it feeds into section 393(4) and then section 393(2), which will ensure that the amount available cannot exceed the total amount of unused interest allowance from the originating period.

42. Section 395(9) determines the amount of interest allowance of the originating period that is unexpired in the receiving period where section 395(8) applies. In this case only part of the interest allowance from the originating period is in time and only part of the interest expense of the receiving period is in time. Both partial amounts must therefore be calculated (the partial amount of interest allowance under section 395(5) and the partial amount of interest expense under section 395(7)) and the lower amount used.

Chapter 5: Interest Allowance

43. New Section 396 defines the interest allowance for a period of account as, by default, the amount given by the "fixed ratio method" (section 397) or, by election, the amount given by the "group ratio method" (section 398). In addition, where in a period a group has an aggregate net tax-interest income then this is added to the interest allowance for the period.

44. New Section 397 sets out the calculation of the interest allowance by the fixed ratio method. It is the lower of two amounts. The first is 30% of a measure of the group's aggregate tax-EBITDA (defined at section 405). The second is a cap (see section 400) based on the "adjusted net group-interest expense" of the group (defined at section 413).

45. New Section 398 sets out the calculation of the interest allowance by the group ratio method. It is the lower of two amounts. The first is a proportion ("the group ratio percentage") of the group's aggregate tax-EBITDA (defined at section 405). The second is a cap based on the "qualifying net group-interest expense" of the group (see section 414), the calculation of which differs from the cap in section 397.

46. New Section 399 defines the "group ratio percentage". This is calculated as the ratio of the qualifying net group-interest expense for the group (see section 414) to the group-EBITDA for the group (see section 416). The percentage is capped at 100%, including where the group-EBITDA is zero or negative for the period. So, for example, where the qualifying net group-interest expense is £36m and the group-EBITDA is £80m then the group ratio percentage is 45%.

47. New Section 400 sets out how to calculate the "fixed ratio debt cap" (used in section 397) and the "group ratio debt cap" (used in section 398). In particular, this allows a group to carry forward an amount of "the excess debt cap" and for this to be included in the debt cap figures for the following period. This amount arises where there is a restriction in a period and there is "headroom" under the fixed ratio debt cap or the group ratio debt cap (as applicable for the period). The excess debt cap can accumulate over successive periods, but reduces in a period in which it is "used".

48. New Section 401 sets out the consequences of making a "group ratio (blended) election" in accordance with paragraph 14 of schedule 7A. This election allows a group to calculate its group ratio percentage with reference to the group ratio percentage of one or more related party investors. In this case the group ratio percentage is determined by calculating a weighted average of the applicable percentages for each investor. Each applicable percentage is the highest of 30%, the ratio for the group calculated in accordance with section 399, and (if the investor is a member of a separate worldwide group) the group ratio for that investor's group. Each applicable percentage is weighted by that investor's interest in the group. Section 401(5) and (6) is used where the relevant periods of account of an investor overlap the relevant period of account of the worldwide group.

49. New Section 402 sets out the calculation of the "blended net group-interest expense". Where a group ratio (blended) election is made, the blended net group-interest

expense is used in place of the qualifying net group-interest expense for the purposes of the group ratio debt cap at section 398(1)(b). The calculation of the blended net group-interest expense is described in the four steps in section 402(3).

50. New Section 403 allows the reporting company of the worldwide group for which the "blended" group ratio is being calculated to specify under the blended group-ratio election that particular elections under schedule 7A are to be treated as being made or as not being made in respect of an investor's worldwide group.

51. New Section 404 defines "investor", "related party investor" and investor's "share" for the purposes of the interest restriction rules.

Chapter 6: Tax-EBITDA

52. New Section 405 sets out the meaning of the key term "aggregate tax-EBITDA" for the worldwide group in respect of a period of account. This total is used in sections 397 and 398 in determining any restriction under the fixed ratio method and the group ratio method.

53. New Section 406 sets out the meaning of "tax-EBITDA" for an individual company in respect of a period of account. In particular, it identifies particular amounts in respect of the period of account in question. The resultant amounts form the basis for the calculation of aggregate tax-EBITDA in section 405.

54. The amounts are identified through satisfying either condition A or condition B. Condition A covers amounts that are brought into account by the company in determining its taxable profits for the period. Condition B extends this to also include amounts that would be so brought into account if the company had sufficient taxable profits in the period. This ensures that amounts leading to a tax loss for the period are included in the definition. Tax-EBITDA can be a positive or negative amount for a particular company. Certain amounts are excluded from conditions A and B (see section 407).

55. Section 406(5) to 406(8) also sets out the rules for calculation where the company does not have a single, complete accounting period which coincides with the period of account of the worldwide group. Amounts are attributed to the disregarded period on a just and reasonable basis, for example having regard to:

- The period in which amounts would be recognised in the company's financial statements if they were drawn up for particular periods.
- The period in which amounts would be brought into account by the company if it had a different accounting period.
- Ensuring that the amounts are in total fully attributed. In other words, if the accounting period is broken up into a number of periods which do not overlap and which, taken together, completely align with the accounting period in question, the total of the amounts attributed to those periods must equal the amount being attributed.

56. New Section 407 provides details of the amounts to be excluded in arriving at a company's tax-EBITDA figure for a period of account. In particular, it excludes:

    - Tax-interest income and tax-interest expense amounts (as defined in Chapter 3 of Part 10).
    - Allowances and charges in connection with capital expenditure under the Capital Allowances Act 2001.
    - Certain amounts of intangible debits under the Intangible Fixed Asset rules (Part 8 of the Corporation Tax Act 2009 (CTA 2009)) which relate to amounts capitalised in the company's accounts, and credits representing the reversal of such amounts.
    - Losses (such as trading losses, property losses, losses on the disposal of shares, miscellaneous losses, non-trading losses on intangible fixed assets, but excluding capital losses), non-trade loan relationship deficits, management expenses from an earlier or later accounting period.
    - Group relief (including consortium relief) except to the extent of any claim for group relief from a company outside of the group. This includes amounts of losses brought forward that are deducted under section 188CK of CTA 2010.
    - Amounts of qualifying tax reliefs (as specified in section 407(3)).

57. Tax-EBITDA is to be calculated on the basis of including net chargeable gains under the Taxation of Chargeable Gains Act 1992 (TCGA 1992). As a result, section 407(4) provides that capital losses are only taken into account in the period in which they are actually deducted from a chargeable gain.

58. New Section 408 provides further interpretation for the purposes of section 407 in respect of the treatment of intangible fixed assets. This specifies certain debits arising in respect of intangible fixed assets which are always excluded from tax-EBITDA. It also specifies certain debits and credits in respect of intangible fixed assets which are excluded to the extent that they reflect debit and credit amounts that would have been excluded previously.

59. New Section 409 adjusts for circumstances where the corporation tax charge is reduced by reason of a credit for foreign tax. An amount derived by the formula at section 409(3) is treated as "notional untaxed income" (as in the calculation of tax-interest income, see section 388) and will not form part of the company's adjusted corporation tax earnings within section 406(2).

Chapter 7: Group-interest and group-EBITDA

60. New Section 410 sets out the meaning of the "net group-interest expense" of a worldwide group for a period of account. This comprises the amounts in respect of "relevant interest expense matters" and "relevant interest income matters" as recognised in the group's financial statements as items of profit or loss for the period.

61. Section 410(2) to 410(5) ensures that amounts are included in net group-interest expense where the amounts are capitalised in respect of an asset that is not a relevant asset and the cost of the asset is expensed or otherwise written off (for example as part of cost of sales). Amounts in respect of a relevant asset are not included to avoid amounts being included in both net group-interest expense and as part of the depreciation and amortisation adjustment. This ensures that group-EBITDA is calculated correctly (see section 416).

62. New Section 411 sets out the meaning of "relevant expense amount" and "relevant income amount". This aims to mirror the types of item that would be included within the scope of tax-interest expense amounts (see section 382), and tax-interest income amounts (see section 385). So, for example, it includes amounts which are loan relationships of a company within the group and also specific arrangements that would be treated as loan relationships of a company under UK tax rules. However, section 411(3) excludes amounts in respect of a group pension scheme.

63. New Section 412 provides further interpretation for the purposes of section 411.

64. New Section 413 sets out the meaning of "adjusted net group-interest expense" of a worldwide group for a period of account. This is used in the calculation of the fixed ratio debt cap (see section 400). This is based on the net group-interest expense of the group, adjusted for certain items.

- Section 413(3)(a), 413(3)(b), 413(4)(a) and 413(4)(b) makes adjustments for amounts of interest and other items that are capitalised in the carrying value of an asset or liability of the company. These ensure that capitalised interest is included in adjusted net group-interest expense at the time it is capitalised and excluded at the time it is expensed in profit or loss.

- Section 413(3)(c) and 413(4)(c) makes adjustments for amounts of interest and other items that are recognised in equity in respect of instruments where amounts would be brought into account for tax under a "relevant enactment". These relate to (a) instruments entered into before an accounting period commencing on or after 1 January 2016 that are grandfathered under the F(No.2)A 2015 changes; and (b) instruments falling within the Regulatory Capital Securities Regulation 2013 (S.I. 2013/3209).

- Section 413(3)(d) and 413(4)(d) makes adjustments for amounts in respect of debt releases and modifications of debt that would be

excluded from tax under sections 322 and 323A of CTA 2009.

- Section 413(4)(e) makes adjustments to exclude amounts of dividends payable on preference shares that are recognised as a liability in the group's financial statements.

65. New Section 414 sets out the meaning of "qualifying net group-interest expense". This is used in the calculation of the group ratio percentage (see section 399) and the group ratio debt cap (see section 400). This is based on the adjusted net group-interest expense of the group, were the following non-qualifying amounts of interest expense to be excluded.

- Section 414(3)(a) excludes amounts arising on financial liabilities owed to related parties.
- Section 414(3)(b) excludes amounts arising on results dependent securities.
- Section 414(3)(c) excludes amounts arising on perpetual and very long-dated instruments.

66. New Section 415 provides interpretation for section 414. Guarantees, indemnities or other financial assistance provided by a related party of the debtor in respect of a liability under a loan relationship generally confer related party treatment for that loan relationship (see section 466(2)), but are ignored where the guarantee (i) is provided before 1 April 2017, (ii) is provided by a member of the group, (iii) is simply a share or loan pledge in respect of the group, or (iv) is a "performance guarantee" (a non-financial guarantee provided in respect of obligations to provide goods or services).

67. New Section 416 sets out the meaning of "group-EBITDA". This is based on the profit of the worldwide group recognised in its consolidated financial statements, before the inclusion of amounts relating to interest, taxation, depreciation and amortisation. This is based on the following concepts:

- Profit (or loss) before tax (PBT) is based on the consolidated financial statements as the profit for the period before taxation.
- Net group-interest expense (I) is the amount defined at section 410.
- Depreciation and amortisation adjustment (DA) is the aggregate of three adjustments to remove depreciation and amortisation, as well as revaluation movements. It also re-computes any profit or loss arising on the disposal of the asset in question.

68. New Section 417 sets out the meaning of the "capital (expenditure) adjustment". This adjustment removes amounts of capital expenditure on relevant assets from group-EBITDA. This will typically be amounts of depreciation and amortisation, but also

includes for example amounts written off as incurred and provision for future capital expenditure. The reference to capital expenditure includes capitalised interest and other relevant expense amounts included in the carrying value of relevant assets.

69. It also excludes income amounts of a capital nature relating to relevant assets. In particular, this will exclude income recognised in respect of contributions received towards the costs of capital expenditure incurred by the group.

70. Relevant assets are defined at section 417(5) as comprising (i) plant, property and equipment; (ii) investment property; (iii) intangible assets; (iv) goodwill; (v) shares in a company; and (vi) interests in an entity which entitle the holder to a share of profits.

71. New Section 418 sets out the meaning of the "capital (fair value movement) adjustment". This adjustment removes revaluations and other fair value movements in respect of relevant assets from group-EBITDA.

72. New Section 419 sets out the meaning of the "capital (disposals) adjustment". This adjustment removes the actual profit or loss recognised in respect of relevant assets from group-EBITDA and replaces it with a re-computed profit on disposal. This is calculated disregarding any amounts written off or any revaluation adjustments. As such it calculates the profit on the assumption that the asset in question was not depreciated or amortised, and was not revalued. In most cases this should be the actual proceeds from the disposal less the actual cost of acquiring the asset.

73. New Section 420 deals with derivative contracts that are recognised at fair value in the accounts. This applies the effect of regulations 7, 8, and 9 of the Disregard Regulations (S.I. 2004/3256) to the calculation of amounts of group-interest and group-EBITDA. As such, it removes the fair value movements arising from derivative contracts in particular circumstances where they form part of an intended hedge. Instead, amounts under the derivative contract will be recognised in the calculation of group-interest and group-EBITDA in line with the hedged item.

74. New Section 421 provides interpretation for the purposes of section 420.

75. New Section 422 adapts the computation of relevant gains and losses on relevant assets under section 419 when a group-EBITDA (chargeable gains) election has effect (see paragraph 15 of schedule 7A). This calculates the profit or loss on disposal of the asset in line with the provisions of TCGA 1992 on the assumption that all members of the group are within the charge of Corporation Tax. However, in making this calculation no regard is taken of the Substantial Shareholdings Exemption or of Double Taxation Relief.

76. New Section 423 adapts the computation under section 413 when an interest allowance (alternative calculation) election has effect (see paragraph 16 of schedule 7A). This turns off the basic rules at section 413 in respect of amounts capitalised where the member of the group in question calculates (or would calculate if it were within the charge to Corporation Tax) the taxable profits from the asset in line with its accounting value. In particular, this will typically be the case in respect of interest capitalised as part of items of trading stock. This aligns the calculation of group-interest with the operation of sections 320 and 604 of CTA 2009.

77. New Section 424 adapts the computation under section 416 in relation to employers' pension contributions into a registered pension scheme when an interest allowance (alternative calculation) election has effect (see paragraph 16 of schedule 7A). This replaces the accounting entries in respect of the registered pension scheme with the amounts that would fall to be deductible under sections 196 to 200 of FA 2004. Typically amounts would therefore be included on a paid basis. However, a different basis may be required for example where the amounts are being spread under section 197 of FA 2004.

78. New Section 425 adapts the computation under section 416 in relation to employees' share acquisition arrangements when an interest allowance (alternative calculation) election has effect (see paragraph 16 of schedule 7A). This replaces the accounting entries in respect of employee share schemes which would fall within Part 11 or Part 12 of CTA 2009, with the amounts that would fall to be deductible under those provisions. This applies on the assumption that all members of the group are within the charge of Corporation Tax

79. New Section 426 applies when there is a change of accounting policy where an interest allowance (alternative calculation) election has effect (see paragraph 16 of schedule 7A). This applies where there has at any time been a change in the accounting policy in the financial statements of the worldwide group. Where relevant, the tax provisions relating to changes of accounting policy are applied in the context of the worldwide group (ie: on the assumption that the worldwide group was a single company within the charge to Corporation Tax).

80. New Section 427 amends certain definitions where an interest allowance (non-consolidated investment) election has effect (see paragraph 17 of schedule 7A). This election amends the financial statements of the worldwide group in respect of the group's interest in an associated worldwide group (for example, as investment in a joint venture). This election allows the principal group to include the appropriate proportion of the adjusted net group interest expense and of the qualifying net group interest expense for an associated group in its adjusted net group interest expense and its qualifying net group interest expense respectively. The group-EBITDA of the principal group is also increased by the same proportion of the group-EBITDA for the associated group.

81. New Section 428 provides further interpretation for the purposes of section 427.

82. New Section 429 provides the meaning of "non-consolidated associate" used in section 427. This defines a non-consolidated associate as an entity being accounted for in the financial statements as a joint venture or an associate using the equity or gross method of accounting or a partnership that has elected into the interest allowance (consolidated partnership) election.

83. New Section 430 adapts the computation when an interest allowance (consolidated partnerships) election has effect (see paragraph 18 of schedule 7A). This has the effect of taking the items of profit or loss out of the financial statements of the worldwide group in respect of the consolidated partnership, and instead uses the equity method of accounting to adjust the financial statements of the worldwide

group.

84. New Section 431 sets out additional interpretation for the Chapter about the meaning of amounts recognised as items of profit or loss, or as items of other comprehensive income.

Chapter 8: Public infrastructure

85. New Section 432 sets out an overview of the Chapter, which provides for the corporate interest restriction to have an altered effect for "qualifying infrastructure companies". To qualify, a company's income and assets must be referable to activities related to "public infrastructure assets", be fully taxable in the UK and the company must make an election, as explained in sections 433 to 437.

86. Amounts in respect of certain loans and other financial liabilities, if meeting further conditions explained in sections 438 and 439, are excluded from being tax-interest expense amounts. In addition, no amounts of the company are included in tax-interest income amounts and tax-EBITDA for the period. The Chapter also acts to adjust other amounts within the corporate interest restriction.

87. New Section 433 explains the conditions which must be met for a company to be a "qualifying infrastructure company". A company must be fully taxable in the UK and meet the "public infrastructure assets" and "public infrastructure income" tests throughout an accounting period and make an election to be a qualifying infrastructure company throughout an accounting period.

- The "public infrastructure income test" requires all but an insignificant proportion of a company's income to derive from a "qualifying infrastructure activity", or shares in, or loan relationships or other financing arrangements with "qualifying infrastructure companies";

- The "public infrastructure assets test" requires all but an insignificant proportion of the value a company's assets to derive from any of (i) tangible assets or (ii) service concession arrangements relating to a "qualifying infrastructure activity"; (iii) financial assets relating to a "qualifying infrastructure activity" of that company or an associated "qualifying infrastructure company"; (iv) shares in a "qualifying infrastructure company" and (v) loan relationships or other financing arrangements to which a "qualifying infrastructure company" is a party. If the "public infrastructure assets" test is failed as a result of circumstances which existed, and were always intended to exist, for a temporary and insignificant period within an accounting period, a company may still be a "qualifying infrastructure company" in that period.

88. New Section 434 sets out that an election to be a "qualifying infrastructure company" must be made in advance of an accounting period in which it is to have effect. It can be revoked after a period of five years, but will continue to have effect until the

accounting period after a revocation. If a revocation is made, a company's subsequent election cannot have effect for an accounting period which begins less than five years after the revocation. Transferees in a transfer of a part of a business of a "qualifying infrastructure company" inherit any election made by the transferor. Once an election has been made by a company, it cannot make a claim for double taxation relief under Chapter 2 of Part 2 of TIOPA, or an election for foreign permanent establishment exemption under section 18A of CTA 2009.

89. New section 435 sets out an election available to members of the same worldwide group to make jointly which modifies the public infrastructure income test, public infrastructure asset test and how the election in section 433 works. A group election has effect from a date specified in the election, until the date specified in a joint revocation made by all members subject to that election, or a notification by one member to HMRC and all the other members. While a group election has effect:

    - in determining whether amounts are insignificant for the purpose of the public infrastructure income and public infrastructure assets test, each elected company is treated as having (in addition to its own) all the income and assets of all of the other elected companies;
    - if one elected company fails the public infrastructure income test or the public infrastructure asset test, or is not fully taxed in the UK in an accounting period, all elected companies are treated as failing those tests for so much of their accounting periods that overlap and are within the period for which the election has effect. If, for the majority of elected companies that have also made an election under section 433, that election has had effect for at least five years, the rule in section 434 which prevents revocation of such an election less than five years after it took effect is turned off.

90. New Section 436 explains that a "qualifying infrastructure activity" is the "provision" of a "public infrastructure asset" including any ancillary or facilitating activities.

    - A tangible infrastructure asset may be a "public infrastructure asset" if it meets a "public benefit test". That is, the asset is procured by a relevant public body, or its use is or could be regulated by an "infrastructure authority" (section 436(3) and (4)).
    - Any building may also be a "public infrastructure asset" if it is part of a UK property business, and intended to be let on "short-term basis" to persons who are not related parties. "Short-term basis" is set out as having an effective duration of less than 50 years and not being considered a structured finance arrangement (section 436(5) to (9)).
    - A "public infrastructure asset" must have, have had, or be likely to have an expected economic life of at least 10 years and be recognised on the

balance sheet of a group company subject to corporation tax.

- "Provision" for these purposes includes acquisition, design, construction, conversion, improvement, operation and repair.

91. New Section 437 provides examples of what "infrastructure" might include, and also what would be considered an "infrastructure authority".

92. New Section 438 sets out the amounts of interest and similar financial expense which may be excluded from tax-interest expense. These are amounts in relation to a financial liability due to an unrelated party or to another qualifying infrastructure company, and amounts in relation to a "qualifying old loan relationship" (section 438(2) and (3)). In all cases amounts in respect of a financial liability cannot be excluded unless the creditor's recourse is limited to the income and assets of, or the shares in, or debt issued by, a qualifying infrastructure company (section 438(4)). Guarantees, indemnities or other financial assistance are ignored for the purposes of considering recourse where (i) provided before 1 April 2017, (ii) provided by a relevant public body or a person not related to the company, or (iii) if considered a "non-financial guarantee" provided in respect of obligations to provide goods or services by the guarantor (or a related party to them) and does not exceed the consideration for those goods or services (section 438(5) and (6)).

93. New Section 439 explains that a loan relationship entered into on or before 12 May 2016 is a "qualifying old loan relationship" if, at that date, at least 80% of the present value of the debtor's future "qualifying infrastructure receipts" for a period of 10 years (or, if shorter, the term of the loan relationship) are highly predictable by reference to "qualifying public contracts" ("the 80% test"). It must also meet the creditor's recourse conditions in section 438. Amendments to the loan relationship after 12 May 2016 are treated as having no effect for the purposes of section 438.

94. A loan relationship ceases to be a qualifying old loan relationship of a company if at any time it would not meet "the 80% test". In making this assessment, the following assumptions are made:

    - The assets held at that time were the only assets held by the company on 12 May 2016;
    - The assets held at that time by any other company in which it has interests (whether direct or indirect) arising as a result of shares or loans were the only assets that the other company held on 12 May 2016; and
    - A "qualifying infrastructure receipt" could not be regarded as highly predictable if, on 12 May 2016, the "public infrastructure asset" in question did not exist or was not in the course of being constructed or converted.

95. For the purposes of section 439, the following definitions are used:

    a. "Qualifying infrastructure receipts" are receipts arising from "qualifying infrastructure activities" carried on by the company and any company it holds shares in or has lent to;

b. "Qualifying public contracts" are contracts with a relevant public body, or entered into as a result of an auction run by one. In both cases the contract must have been entered into on or before 12 May 2016, and as at that time, was expected to have effect for at least 10 years.

96. New Section 440 provides that if in an accounting period a company is a "qualifying infrastructure company" it is treated as having no "tax-interest income amounts" in that period.

97. New Section 441 provides that if in an accounting period a company is a "qualifying infrastructure company" it has a "tax-EBITDA" of nil for that period.

98. New Section 442 provides that if in an accounting period a company is a "qualifying infrastructure company", exempt amounts must be excluded from the "adjusted net-group interest expense" and the "qualifying net group-interest expense" of the worldwide group for that period. Similarly the "group EBITDA" of the worldwide group is to be calculated as if the "qualifying infrastructure company" is not included.

99. New Section 443 turns off the "de minimis amount" of interest capacity (see section 392) for a worldwide group with a "qualifying infrastructure company". An exception is provided where the total interest restrictions calculated including the rules in Chapter 8 would exceed those which would arise if Chapter 8 did not apply and the interest capacity for the period equalled the "de-minimis amount". In this case the rules in Chapter 8 are ignored and the interest capacity of the group is set to the "de minimis amount".

100. New Section 444 sets out how the rules for infrastructure companies apply in the case of a joint venture company that is a qualifying infrastructure company and has at least one investor that is a qualifying infrastructure company and at least one investor that is not. It can mitigate the adverse tax consequences that might otherwise arise under this Part if such investors together formed a joint venture. Section 444(2) and (3) amends how section 401 and section 427 apply to a joint venture company that has elected into section 444. Section 444(5) and (6) affects the amounts of qualifying exempt amounts for this joint venture company. Section 444(9) allows the joint venture to have tax-EBITDA and determines this value of tax-EBITDA.

101. New Section 445 extends the rules of new section 444 for a joint venture company that has subsidiaries and forms a multi-company group. This replicates the effect of section 444 across the whole of the group.

102. New Section 446 contains supplementary rules and definitions for section 444.

103. New Section 447 sets out how the public infrastructure asset test is applied where a company has a significant interest in a partnership or other "transparent entities". In such cases, (i) where the company recognises that interest on its balance sheet, the value of that interest is considered to be derived from the underlying assets of that partnership or "transparent entity" in order to apply the "the public infrastructure assets test" (see section 433); and (ii) obligations of the partnership or "transparent entity" are considered to be obligations of the company for the purposes of

determining the exempt amounts of interest expense under section 438(4). Transparent entities are defined for the purposes of this section as not chargeable to corporation tax or income tax as a person (ignoring the effect of any exemptions).

104. New Section 448 provides that the Chapter can apply to the "decommissioning" of a public infrastructure asset as well as the "provision" of one. It also provides that in considering whether a company is a qualifying infrastructure company, shares in or any loan relationship or other financing arrangement with a "decommissioning fund" can be ignored. A "decommissioning fund" is regarded as a qualifying infrastructure company. A "decommissioning fund" is defined as a company which holds investments for the sole purpose of funding decommissioning of public infrastructure assets and is prevented from using the proceeds for any other purpose other than returning surplus funds.

105. New Section 449 sets out some definitions for the purposes of the Chapter.

Chapter 9: Cases involving particular types of company or business

106. New Section 450 sets out how a banking company is to determine the amount of its tax-interest. Section 450(2) and (4) provides that debits and credits will be included within the definition of tax-interest (see sections 382 and 385) if they arise directly from dealing in financial instruments while section 450(5) and (6) aims to mirror this for the group ratio method (see section 411).

107. Section 450(1) ensures that this treatment is appropriate only if the dealing in financial instruments is part of the activities of the trade while section 450(7) sets out the meaning of banking company and financial instruments.

108. New Section 451 provides specific exemption from the interest restriction calculation of oil and gas ring-fence income, within the meaning of section 275 of CTA 2010, and gains/losses within the meaning of section 197(3) of TCGA 1992.

109. New Section 452 provides special rules for Real Estate Investment Trusts (REITs). The exempt property rental business and the residual business of the REIT are deemed to be regarded as separate members of the worldwide group. In addition the profits of the property rental business are assumed not to be exempted from Corporation Tax for the purposes of calculating tax-interest and tax-EBITDA. It specifies how the restricted interest should be allocated between these two businesses and allows for excess amounts to be carried forward in accordance with the rules in Chapter 2. These streamed amounts are then to be included within an interest restriction return.

110. New Section 453 provides special rules for investments held by insurance companies as part of a portfolio. Where such an investment would otherwise be a subsidiary that would be part of the insurer's worldwide group, this provision will ensure that it is not. In such a case the subsidiary is not considered to be a consolidated subsidiary of any member of the worldwide group of the insurer. This allows the subsidiary to form its own worldwide group separate from the insurance company's group.

111. New Section 454 provides that any interest of a company in respect of its

underwriting business as a member of Lloyd's is included within the definition of tax-interest where brought into account under Part 3 of CTA 2009.

112. New Section 455 adapts the rules in the case of shipping companies subject to tonnage tax.

113. New Section 456 provides an option by way of an election for insurers and other companies which hold loan receivables (creditor relationships) at fair value to disapply that treatment and instead apply the corporate interest restriction rules on the basis that the loans had been accounted for on an amortised cost basis of account.

114. New Section 457 supplements section 456. It applies where a company applies an amortised cost basis of accounting in respect of a loan under section 456 and this would result in notional debit amounts being included within tax-interest. To facilitate the operation of the disallowance of such amounts, the company concerned must bring into account matching debit and credit amounts equal to the amount of the notional debits. This allows the company to make any disallowance of those debits required under this Part. Otherwise the recognition of the matching debit and credit amounts should leave the company unaffected.

115. New Section 458 applies to certain amounts payable by co-operative societies, community benefit societies, UK agricultural co-operatives or UK fishing co-operatives. Where amounts of distributions are treated as interest under a loan relationship solely by virtue of section 499 of CTA 2009, they are excluded from being a tax-interest expense amount or a tax-interest income amount for the purposes of Part 10 of TIOPA.

116. New Section 459 provides that certain interest payments to charity will be excluded from the "tax-interest expense amount". These are payments made to a charity parent under a loan relationship where the company would be able to claim relief on any donation it made to the parent under section 190 of CTA 2009.

117. New Section 460 makes provision for the calculation of tax-EBITDA in respect of long funding operating leases and finance leases that are not long funding finance leases. This will ensure that the treatment of amounts excluded from tax-EBITDA in respect of leases is aligned with the accounting classification of whether a lease is an operating lease or a finance lease, and not based on whether it is a long funding lease or not. This aligns the treatment with the definition of tax-interest which is based on whether a lease is a finance lease. The accounting classification is subject to section 53 of FA 2011, which disregards changes made since 1 January 2011 to accounting standards in respect of leasing.

118. Section 460(2) makes an equivalent adjustment for the purposes of the group ratio method, to ensure that amounts of "depreciation" in respect of an asset held under a finance lease are included in the capital (expenditure) adjustment.

Chapter 10: Anti-avoidance

119. New Section 461 is an anti-avoidance rule. This applies where there are arrangements that seek to obtain a tax advantage and that tax advantage derives, in whole or in part, from the interest restriction rules. The tax advantage arising from that arrangement is counteracted. Transitional provision is made by paragraph 34 in part 2 of this schedule.

Chapter 11: Interpretation, etc

120. New Section 462 introduces the provisions that specify where a person is a "related party" for the purposes of Part 10 of TIOPA. In particular, it makes it clear that sections 468 to 472 take priority over sections 466 and 467.

121. New Section 463 sets out the main definition of a related party. A person is a related party where (i) they are part of the same consolidated group; (ii) there is common participation in the management, control or capital of the parties; or (iii) the 25% investment condition is met. Specific provision is made for securitisation companies held by a trustee (section 463(6)).

122. New Section 464 sets out the meaning of 25% investment in a company or other person. This is based on the "equity" in the company or other entity.

123. New Section 465 attributes rights and interests when considering where two persons are related parties. In particular, it applies:

- Between connected persons (e.g. relatives and companies under common control).
- Between partners in partnership (including through connected persons).
- Between persons where there are arrangements under which a person "acts together" with another person.
- Between persons where there is a "qualifying arrangement", being an arrangement whereby persons can reasonably be expected to act together to exert greater influence or to achieve a particular outcome.

124. New Section 466 sets out additional cases in which parties are to be considered to be related parties in respect of a particular instrument. Section 466(2) applies where a related party guarantees a particular instrument. Section 466(4) applies where a related party can be seen as the real lender or counterparty by virtue of a series of loan relationships or other arrangements.

125. New Section 467 sets out a further rule that parties are to be considered to be related parties in respect of a particular loan instrument where a number of loan investors also hold equity stakes in a company or other entity in the same, or similar, proportions. This also applies where loans were originally held in such a manner (e.g. because they were marketed in this way), even where the loans have since been separated from the equity stakes.

126. New Section 468 sets out a rule under which loans which would otherwise be regarded as being between related parties are not to be so regarded where at least 50% of debt with the same rights is held by unrelated parties.

127. New Section 469 sets out a rule under which loans which would otherwise be treated as being between related parties are not to be so treated where the loan becomes a related party debt as a result of a debt restructuring exercise in respect of distressed debt.

128. New Section 470 sets out a rule which treats the debtor and creditor of a loan relationship as not being related parties in certain situations, despite them being related parties as a result of particular circumstances. The rule can only apply where the creditor is not party to the loan relationship as a result of, or in any way connected with, any of the circumstances which make the two parties related. This could be relevant where, for example, rights of another person are attributed to the lender under section 465(1) and the lender had no knowledge of that the other person held those rights.

129. New section 471 excludes certain loans made by relevant public bodies (see section 491) from being loans made by a related party for the purposes of this legislation.

130. New Section 472 provides an exclusion for finance lease arrangements that are entered into before 20 March 2017. Such instruments are treated as not being between related parties for the purpose of the corporate interest restriction rules.

131. New Section 473 sets out the meaning of the key terms "worldwide group" and "ultimate parent". To be an "ultimate parent" the entity will need to be a relevant entity which is not a consolidated subsidiary of another entity that could be an "ultimate parent". The "worldwide group" will then be the ultimate parent and all of its consolidated subsidiaries. This is based on the treatment under International Accounting Standards.

132. New Section 474 sets out the meaning of a "relevant entity" for the purposes of section 473. This includes companies or other entities which have shares or other interests which are listed on a recognised stock exchange and are sufficiently widely held. Certain exclusions are listed at section 474(3).

133. New Section 475 sets out the meaning of "non-consolidated subsidiary" and "consolidated subsidiary". This provides that a subsidiary company held at fair value (and not consolidated on a line-by-line basis) is a "non-consolidated subsidiary". A non-consolidated subsidiary will not be a member of a parent's group. This is based on the treatment under International Accounting Standards.

134. New Section 476 sets out how to determine whether the identity of the worldwide group has changed when the entities which constitute the worldwide group change over time. This is done by reference to who the ultimate parent is at a given point in time.

135. New Section 477 provides for the treatment of "stapled entities". Section 477(3) sets out when an entity is to be treated as "stapled" to another and deems them to be

consolidated subsidiaries of another entity.

136. New Section 478 provides for business combinations where, absent this section, two entities would each be treated as an ultimate parent despite their being treated as a single economic entity under international accounting standards. The section has effect as if both entities were consolidated subsidiaries of a deemed parent.

137. New Section 479 sets out the meaning of "financial statements". The financial statements will be based on the consolidated financial statements for a multi-company worldwide group and on the entity accounts for a single-company worldwide group where these are drawn up and are considered "acceptable".

138. New Section 480 sets out the meaning of "period of account" for a worldwide group. This is based on the period for which financial statements of the worldwide group are drawn up.

139. New Section 481 explains what is meant by "acceptable" financial statements and the consequence of such statements not being drawn up for a worldwide group. Acceptable statements are drawn up under International Accounting Standards (IAS), UK generally accepted accounting practice or in accordance with the accounting principles and policies of Canada, China, India, Japan, South Korea or the United States of America. Financial statements that do not materially differ from IAS statements are also acceptable. HMRC may by regulations update the circumstances in which accounts are considered to be "acceptable".

140. Where financial statements are drawn up and they are not acceptable, then these statements are to be ignored and IAS financial statements of the worldwide group treated as having been drawn up.

141. New Section 482 deals with the case where acceptable financial statements have been prepared but either include the results of companies that are not in the group or do not include the results of companies that are in the worldwide group. This could arise where the accounts are prepared under an accounting framework that differs to IAS. In this case, these statements should be ignored and statements treated as having been drawn up which align with the composition of the worldwide group, which is defined by reference to IAS (see sections 475 and 476). The statements treated as drawn up should be prepared in accordance with the same accounting principles and practice as was used to draw up the original statements.

142. New Section 483 deals with the case where the ultimate parent prepares accounts for a period and it is not the ultimate parent for the whole of the period. In this case these accounts are ignored and the ultimate parent is treated as if it had instead prepared consolidated financial statements including itself and its IAS subsidiaries for the period for which it was the ultimate parent of the worldwide group in question.

143. New Section 484 deals with the case where the worldwide group does not prepare consolidated accounts but the ultimate parent does prepare its own financial statements for a particular period. In this case, IAS accounts are treated as having been drawn up for that period. The ultimate parent may elect that this section does

not apply (see section 486).

144. New Section 485 deals with the case where a multi-company worldwide group does not prepare consolidated financial statements, or a single-company worldwide group does not prepare entity accounts and where section 484 is not relevant. In this case it treats the ultimate parent as preparing financial statements for that period. Where this period extends for more than 12 months, it is treated as preparing financial statements for each 12 month period

145. New Section 486 allows the ultimate parent to elect for a different period to be used in place of a 12 month period under section 485, within limits set down in section 486(4). Section 485(4)(b) and (4)(c) would then apply from the end of the elected period to treat the group as preparing financial statements for each 12 month period.

146. New Section 487 requires financial statements to be prepared for no more than 18 months and to be drawn up within 30 months of the start of the period, otherwise they are to be ignored for the purpose of this Part.

147. New Section 488 sets out the meaning of "IAS financial statements" of a worldwide group.

148. New Section 489 sets out the meaning of "recognised" in financial statements. This clarifies that where an amount is included as part of another amount which is recognised in the financial statements, that amount is also regarded as being recognised. In addition, where an amount is expressed in a currency other than sterling then it is to be translated into sterling based on the average rates for the period.

149. New Section 490 sets out the definition of "relevant accounting period".

150. New Section 491 sets out the meaning of a "relevant public body". Section 491(1) lists specific bodies which fall into this definition, but also includes any other body which acts under any enactment for public purposes and not for its own profit. Some of these bodies cannot be a "relevant entity" (see section 474(3)).

151. New Section 492 sets out the meaning of a "UK group company". This covers UK resident companies and non-resident companies which have a permanent establishment in the UK. These are the members of a worldwide group that may be subject to disallowances or reactivations of tax-interest expense amounts.

152. New Section 493 applies the definitions in sections 415 and 585 of CTA 2009. This ensures that the definitions of loan relationship and derivative contract function correctly where a particular financial instrument is treated as being split for accounting purposes.

153. New Section 494 contains further interpretation for the purposes of Part 10.

154. New Section 495 contains a power to allow HMRC to make regulations to address differences between the way amounts are recognised in the group's financial statements and how they are recognised for accounting or tax purposes by any member of the group. Regulations may in such cases adjust the calculation of

amounts in chapter 7 based on the worldwide group's financial statements (principally adjusted net group-interest expense, qualifying net group-interest expense and group-EBITDA).

155. In particular, regulations will be introduced under this power to apply from 1 April 2017 in the following two situations.

- As at 31 March 2017 a loan relationship is recognised in the worldwide group's financial statements such that it is subject to fair value accounting in the group accounts and is recognised at the amortised cost basis of accounting in the financial statements of the issuer company.

  In this case, the financial statements for the worldwide group are to be assumed to be prepared recognising this loan relationship on the amortised cost basis of accounting.

- As at 31 March 2017, there is a loan relationship between two group members. This loan relationship was previously recognised in the worldwide group's financial statements and the loan was derecognised before 31 March 2017 as a result of either (i) the loan being acquired by a group member; or (ii) the creditor becoming a group member. The situation is such that neither section 361 nor section 362 CTA 2009 applies or would apply.

  In this case, the financial statements of the worldwide group are to be assumed to be prepared on the basis that the gain or loss on the derecognition of the loan is spread over the remainder of the term of the loan on a just and reasonable basis.

156. New Section 496 contains a power to allow HMRC to make regulations in respect of capital market arrangements to allow liabilities of a company to be transferred to another UK group company.

157. New Section 497 contains a power to allow HM Treasury to make regulations to revise the legislation as a result of changes in accounting standards.

158. New Section 498 governs the making of regulations under Part 10, by Statutory Instrument.

Part 2 of Schedule 1: New schedule 7A to TIOPA 2010

159. Part 2 of schedule 1 inserts a new Schedule 7A into TIOPA. This covers administrative provisions relevant to the interest restriction rules.

Part 1: The reporting company

160. Paragraph 1 of schedule 7A provides for the appointment of a "reporting company" for a period of account by a member of a worldwide group. The appointment is automatically rolled over for future periods (paragraph 1(3)), unless it is revoked under paragraph 2 or a replacement reporting company is appointed under paragraph 5.

161. The appointment must be made after the end of the period of account but no later than six months after the end of that period (paragraph 1(4)). The notice of appointment must be supported by a majority of eligible group members (paragraph 1(5)). The reporting company must be an "eligible company" (paragraph 1(8)).

162. Paragraph 2 provides that the appointment of a reporting company may be revoked by a member of a worldwide group with the support of a majority of eligible group members.

163. Paragraph 3 permits HMRC to make regulations in connection with the appointment of a reporting company and the revocation of an appointment.

164. Paragraph 4 permits HMRC to appoint an eligible company as the reporting company where the members of the worldwide group have not done so within the required time limit.

165. Paragraph 5 permits HMRC in certain circumstances to appoint a different reporting company, in place of the company appointed under paragraph 1 or paragraph 4.

166. Paragraph 6 requires that where a reporting company is appointed for a period of account, it must so notify each company that was a UK group company at any time during the period of account. It must also notify the ultimate parent, if that company would not otherwise be notified. A UK group company, defined in section 492, is a member of the group within the scope of UK corporation tax.

167. Paragraph 7 requires the reporting company to make an "interest restriction return". This return sets out the amounts of interest and other financing amounts that are to be disallowed or reactivated, and how they are allocated to companies in a group. The time limits for making the return are set out in paragraph 7(5) and 7(6).

168. Paragraph 8 permits the reporting company to submit a revised interest restriction return, and sets out circumstances where a reporting company must submit a revised interest restriction return.

169. Paragraph 9 permits a reporting company to submit a full interest restriction return within five years of the end of the period of account, where it had previously submitted an abbreviated return. Submission of full returns allows the group to access any available interest allowance in later periods.

170. Paragraph 10 sets out the meaning of a "consenting company" and a "non-consenting company". A "consenting company" is a company in a group that has agreed to accept the allocation of disallowed amounts made to it in the interest restriction return submitted by the reporting company. All other companies in the group are "non-consenting" companies.

171. Paragraph 11 provides that if a company is one which supported the appointment of a reporting company under paragraph 3 it is therefore deemed to be a consenting company, unless it expressly makes a statement to the contrary under paragraph 1(7) when the reporting company is appointed, or revokes its consent by giving a notice under paragraph 10(2)(b).

Part 2: Contents of interest restriction return

172. Paragraph 12 of schedule 7A sets out the elections that must be made in an interest restriction return.

173. Paragraph 13 permits the reporting company to elect on behalf of the group that the group ratio method should be used to compute the group's interest disallowance.

174. Paragraph 14 permits the reporting company to elect on behalf of the group that the group ratio method should be used to compute the group's interest disallowance, but subject to the "blended group ratio provisions" (see sections 401 to 404).

175. Paragraph 15 permits the reporting company to elect on behalf of the group that the group ratio method should be subject to the group-EBITDA (chargeable gains) election (see section 422).

176. Paragraph 16 permits the reporting company to elect on behalf of the group that the group ratio method should be used to compute the group's interest disallowance, but subject to the "alternative calculation provisions" (see sections 423 to 426). These provisions are also relevant for the calculation of adjusted net group-interest expense for the purposes of the fixed ratio debt cap.

177. Paragraph 17 permits the reporting company to elect on behalf of the group that the group ratio method should be used to compute the group's interest disallowance, but subject to the "non-consolidated investment provisions" (see sections 427 and 428). These provisions are also relevant for the calculation of adjusted net group-interest expense for the purposes of the fixed ratio debt cap.

178. Paragraph 18 permits the reporting company to elect on behalf of the group that the group ratio method should be used to compute the group's interest disallowance, but subject to the consolidated partnership provisions (see section 430). These provisions are also relevant for the calculation of adjusted net group-interest expense for the purposes of the fixed ratio debt cap.

179. Paragraph 19 permits the reporting company to elect to submit an abbreviated return if the worldwide group is not subject to interest restrictions (see paragraph 19(3)).

180. Paragraph 20 sets out what must be included in an interest restriction return. Paragraph 20(3) sets out the requirements of the full return. Paragraph 20(5) sets out

the requirements of an abbreviated return.

181. Paragraph 21 sets out the detail of the calculations that must be included in a full interest restriction return.

182. Paragraph 22 sets out the information that must be included in a statement of allocated interest restrictions. This statement sets out the amounts of interest restriction that will be applied to each company for the period. This statement must be included in the full return where there are amounts to be restricted for the period.

183. Paragraph 23 sets out the meaning of a "pro-rata share" of the total disallowed amount for a period of account. This sets the limit on the amounts of disallowance that can be allocated to "non-consenting" companies. It also forms the basis of the amounts to be restricted where no interest restriction return has been submitted. The pro-rata allocation is based on the proportion that a company's net tax-interest bears to the total of the net tax-interest expense amounts across the group for the period of account.

184. Paragraph 24 sets out how a company allocates a "pro-rata share" to its own accounting periods. The worldwide group's "period of account" used in computing the total disallowance and the allocated shares may not necessarily coincide with the corporation tax accounting period for every company in the group. Apportionment will therefore be necessary.

185. Paragraph 25 sets out what information must be included in a statement of allocated interest reactivations. An "interest reactivation" arises when an amount disallowed in one period of account could potentially be deductible in a later period of account because the group's tax-EBITDA in that later period is sufficient to permit a deduction greater than the interest arising in that period.

186. Paragraph 26 sets out how to calculate the amount available for reactivation by a company for a period of account of the group. Any reactivation will take effect in the "specified accounting period", which is the first accounting period that overlaps with the group's period of account in which the company was a part of the group.

187. The starting point ("A") is the total amount that has been disallowed under these rules by that company that is brought forward at the start of the specified accounting period. There are then four possible adjustments in relation to amounts that it must disallow in the current accounting period (amounts B to E). B and C deal with amounts disallowed and reactivated in the specified accounting period in respect of an earlier period of account of the worldwide group. D and E deal with amounts disallowed and reactivated in the specified accounting period in respect of a period of account of another worldwide group before the company joined the worldwide group that is the subject of the reactivation calculation.

188. Paragraph 27 permits the use of estimated amounts in the interest restriction return if necessary and requires disclosure of the amounts that are estimates.

189. Paragraph 28 permits HMRC to correct an interest restriction return. The correction must be made no later than nine months after the day on which the return was

submitted.

190. Paragraph 29 sets out a penalty for failure to deliver an interest restriction return.

191. Paragraph 30 sets out a penalty for the submission of an incorrect return.

192. Paragraph 31 sets out what is meant by the term "concealed" for the purposes of paragraph 30. It also extends the meaning of a careless or deliberate inaccuracy to encompass an inaccuracy that is not brought to the attention of an officer of HMRC.

193. Paragraph 32 provides for a penalty to be imposed on a company that provides inaccurate information to another company for the purposes of an interest restriction return submitted by that other company.

194. Paragraph 33 provides for any penalty to be reduced to reflect the level of disclosure. It also empowers HMRC to consider and apply special circumstances, which are to be set out in regulations made by HMRC.

195. Paragraph 34 sets out how a penalty is to be assessed, paid and enforced.

196. Paragraph 35 provides a right of appeal against a penalty.

197. Paragraph 36 sets out the procedure for appeals against penalties.

198. Paragraph 37 sets out the tax treatment of any payment made between companies in respect of penalties charged on the recipient of the payment. Such payments are to be ignored for tax purposes, up to the amount of the penalty.

Part 3: Duty to keep and preserve records

199. Paragraph 38 of schedule 7A requires a reporting company to keep and preserve certain records.

200. Paragraph 39 sets out the penalty for failure to comply with the requirements of paragraph 34.

Part 4: Enquiry into interest restriction return

201. Paragraph 40 of schedule 7A provides a power for HMRC to open an enquiry into an interest restriction return. The provisions are similar to those in Part 4 of schedule 18 to FA 1998, adapted for the purposes of interest restriction returns. In particular, an enquiry into an interest restriction return does not affect, and is not affected by, any enquiry into a company tax return of a member of the group. Paragraph 40(6) permits a company tax return to be amended in consequence of an enquiry into an interest restriction return, irrespective of the status of any enquiry into the company's tax return.

202. Paragraph 41 sets out the normal time limits within which an enquiry may be opened.

203. Paragraph 42 sets out certain extended time limits within which an enquiry may be opened. These time limits apply if the conditions set out in paragraph 42(1) are met.

204. Paragraph 43 sets out the scope of an enquiry into an interest restriction return. The

enquiry cannot consider any matters contained in a company tax return that affect the interest restriction return. That is, the accuracy of any amounts of tax-interest or other components of tax-EBITDA of a company are matters for an enquiry into that company's tax return, and not for an enquiry into the interest restriction return. However, it is possible for HMRC to enquire into how such an amount should be treated for the purposes of Part 10.

205. Paragraph 44 permits the scope of an enquiry to include the composition of the worldwide group and whether the period of account is correctly identified.

206. Paragraph 45 allows HMRC to amend a company's self-assessment during the course of an interest restriction enquiry, where it is considered that the tax payable is understated in the company's return. Paragraph 45(3) and (4) sets out appeal rights.

207. Paragraph 46 applies where a reporting company amends an interest restriction return during the course of an enquiry. The amendment may be taken into account in the enquiry, but is not given effect until completion of the enquiry.

208. Paragraph 47 sets out what steps HMRC must take on completion of an enquiry. A closure notice must be issued. Where relevant, that notice must state any change to the period of account (paragraph 47(3)) or the composition of the group (paragraph 47(4) to (6)).

209. Paragraph 48 enables the reporting company to apply to the tribunal to issue a direction to HMRC to issue a closure notice in relation to an enquiry.

210. Paragraph 49 sets out the required contents of a closure notice. Paragraph 49(2)(b) covers all revisions that may be required to a return, including those that may arise as a result of paragraph 49(4): where the return was for the wrong period of account; or paragraph 49(6): where the composition of the group was incorrect. The notice need not specify how amounts are to be allocated.

211. Paragraph 49(7) covers the situation where the group composition was incorrect because some companies that were not members of the worldwide group have been included in the return.

212. Paragraph 49(8) covers the situation where one or more companies have been excluded incorrectly from the original worldwide group identified in the interest restriction return under enquiry, and the ultimate parent of the group identified in the closure notice is not the ultimate parent of a worldwide group for which a reporting company has been appointed. Paragraph 51 covers the situation where the ultimate parent is already the ultimate parent of another such group.

213. Paragraph 50 requires the reporting company to submit an amended interest restriction return or new interest restriction returns, to give effect to the conclusions in the enquiry closure notice, including any consequential effects. If the company does not do so, within the time limit set out in paragraph 50(2), HMRC may make a determination under paragraph 58.

214. Paragraph 50(2) requires that a return under paragraph 49 only has effect if it is submitted to an officer of HMRC within three months of the day on which the closure

notice is given to the company.

215. Paragraph 51 applies where HMRC determines that the interest restriction return should have been submitted for a different group, where one or more entities was incorrectly excluded from the original group and where the ultimate parent is already the ultimate parent of another such group. HMRC must appoint a reporting company for the "new group", which must then undertake all the requirements regarding an interest restriction return. Any interest restriction return, notice of enquiry, and appeal in relation to the original group is treated as withdrawn.

216. Paragraph 52 provides a right of appeal against the conclusion stated in a closure notice under paragraph 49, or against a notice given under paragraph 51.

217. Paragraph 53 covers the situation where the worldwide group has a different composition to that for which the interest restriction return was originally submitted, and where the reporting company that submitted the original return is not a member of the revised group. HMRC may appoint a new reporting company. This may apply, for instance, if HMRC concludes that some of the members of a group for which a return was submitted are members of one or more different groups.

218. Paragraph 54 provides that where anything is to be done for the purposes of Part 10 of TIOPA on a just and reasonable basis, HMRC may, in setting out conclusions in relation to a closure notice, specify a different "just and reasonable" basis to that used initially by the reporting company in the interest restriction return. The basis specified may be questioned on the grounds that it is not just and reasonable (but not on any other grounds).

219. Paragraph 55 ensures full continuity of application of the provisions of schedule 7A where there is more than one reporting company for a period of account.

Part 5: Determinations by officers of Revenue and Customs

220. Paragraph 56 of schedule 7A provides HMRC with the power to make a determination where a reporting company has failed to make a compliant interest restriction return by the filing deadline and HMRC considers that a disallowance should be made. The disallowance is shared between UK group companies on a pro rata basis. HMRC must inform each company of its disallowance and notify the reporting company.

221. Paragraph 57 provides a time limit for the validity of an interest restriction return following a determination under paragraph 56 (but not after a determination under paragraph 58). Notwithstanding time limits that might otherwise apply, the return can have effect if submitted within 12 months of the issue of the notice of determination.

222. Paragraph 58 provides an officer of Revenue and Customs with a power to determine the pro-rata shares of the disallowed amounts where a closure notice given under paragraph 47 required the reporting company to make a return or returns, but the company has failed to do so within the time specified in paragraph 50(2). An officer may also make a determination if the return is considered not to comply with the

requirements of the closure notice. The relevant group company and the reporting company must be informed, and the company tax return of the relevant company is amended accordingly. HMRC must take action under this paragraph within 3 months of the end of the period for revision of the interest restriction return by the reporting company.

223. Paragraph 59 sets out a company's right to appeal against an HMRC determination made under paragraph 58. The only permitted ground of appeal is that the determination is inconsistent with the closure notice to which it relates.

Part 6: Information powers exercisable by members of group

224. Paragraph 60 of schedule 7A sets out what information must be provided by members of the group to the reporting company. It also requires the reporting company to send a copy of the interest restriction allocation to all relevant companies. A "relevant company" is a company that was a UK group company (defined in section 473) at any time in the group's period of account. In all cases the requirement is enforceable between the parties involved.

225. Paragraph 61 sets out what information may be required by a group company from other group companies, where a reporting company has not been appointed. Again, the requirement is enforceable between the parties involved.

Part 7: Information powers exercisable by officers of Revenue and Customs

226. Paragraphs 62 to 67 of schedule 7A deal with information powers similar to those in Schedule 35 to FA 2008 but designed to be applied in connection with an enquiry into an interest restriction return.

227. Paragraph 62 provides that HMRC may serve a notice on a member of a group requiring it to provide information or documents reasonably required for checking an interest restriction return.

228. Paragraph 63 provides for a third party information notice to be served in connection with checking an interest restriction return. A third party is defined as a party that is not a member of the group. The service of such a notice requires either the consent of a UK group company or the approval of the tribunal.

229. Paragraph 64 provides that where a group has submitted an interest restriction return, a notice under paragraph 62 or 63 can only be served if that return is under enquiry.

230. Paragraph 65 provides a right of appeal against a notice under paragraph 62; and a right of appeal against a notice under paragraph 63, but only where the tribunal has not approved the giving of the notice.

231. Paragraph 66 applies certain provisions of Schedule 36 to FA 2008 to the information powers exercisable under paragraph 60 or 61.

232. Paragraph 67 explains what is meant by "checking an interest restriction return".

Part 8: Company tax returns

233. Paragraph 68 of schedule 7A provides that certain elections affecting the amounts in a company's tax return for an accounting period must be made in the original or amended return to which the election relates.

234. Paragraph 69 makes further provision regarding the mechanics and time limits for elections, or their withdrawal, and consequential amendments to company tax returns under section 375, 377 and 380 and for amendments required under section 376.

235. Paragraph 70 provides that a company's tax return is treated as amended to take account of any changes to its profits or losses that arise from an interest restriction return. In particular, this will apply where the interest restriction return changes the amounts of disallowance or reactivation that are allocated to a particular company.

236. Paragraph 71 provides a regulation-making power in relation to amendments of a company tax return made in accordance with paragraph 70, or any other amendments of a company tax return in connection with the rules introduced by this schedule.

237. Paragraph 72 permits a company to make, amend or revoke certain claims following amendments to its company tax return that are consequent on an interest restriction return.

238. Paragraph 73 specifies that "company tax return" means a return under schedule 18 to FA 1998.

Part 9: Supplementary

239. Paragraph 74 of schedule 7A ensures that a person cannot be liable to a penalty under this schedule in addition to being convicted of an offence.

240. Paragraph 75 requires that a notice of appeal must specify the grounds of the appeal.

241. Paragraph 76 sets out when amounts included in an interest restriction return may be treated as conclusively determined. This is where the time limits for submitting revised returns have passed, or a return has been subject to an enquiry that has been concluded. This does not prevent HMRC from opening an enquiry under the extended time limits set out in paragraph 42, where an error is discovered, or from making a determination under paragraph 56 or 58.

Part 3 of Schedule 1: Consequential amendments

242. Paragraph 3 amends section 98 of the Taxes Management Act 1970

243. Paragraph 4 amends paragraph 88 of schedule 18 to FA 1998.

244. Paragraph 5 amends section A1 of CTA 2009.

245. Paragraphs 6 to 9 amend CTA 2010.

246. Paragraph 10 deals with the consequences of inserting a new Part 10 into TIOPA.

The existing Part 10 becomes Part 11, the existing sections 375 and 376 are repealed (subject to a saving provision), and the existing sections 372 to 374 and 377 to 382 are renumbered to follow on from the new Part 10.

247. Paragraph 11 repeals Part 7 of TIOPA (Tax Treatment of Financing Costs and Income, commonly referred to as the "Debt Cap"), which is superseded by the corporate interest restriction rules. The main rule is that the current Debt Cap legislation will cease to have effect for periods of account commencing on or after 1 April 2017. Certain related provisions are also repealed.

248. Paragraphs 12 to 20 make consequential amendments to TIOPA.

249. Paragraph 21 amends Chapter 3 of Part 9A of TIOPA. This amends section 371CE and inserts a new section 371CEA which defines a group treasury company for the purposes of determining the charge gateway in the Controlled Foreign Company (CFC) rules. This provision replaces the definition from the repealed Debt Cap rules.

250. Paragraph 22 amends Chapter 9 of Part 9A of TIOPA. This replaces section 371IE, the existing rule that provides relief under the CFC rules for "matched interest", with an equivalent provision following the repeal of the current Debt Cap rules.

251. Paragraph 23 amends Chapter 19 of Part 9A of TIOPA. This includes the introduction of a new section 371SLA which sets out certain assumptions to be made in applying the corporate interest restriction rules in the calculation of chargeable profits of a CFC.

252. Paragraph 24 introduces a new index of defined expressions as Part 7 of schedule 11 to TIOPA.

Part 4 of Schedule 1: Commencement and transitional provision

253. Paragraph 25 sets out the commencement rules, the main commencement provision being that the rules will have effect for periods of account commencing on or after 1 April 2017. Where the group draws up accounts (or is so treated as doing so) which straddle 1 April 2017, the rules apply as if accounts were drawn up for two separate periods, one ending 31 March 2017 and another starting on 1 April 2017.

254. Where it is just and reasonable to do so, groups may take accounts that have been prepared and apportion amounts to the respective notional periods; but if such an approach is not just or reasonable, the rules should have effect on the assumption that accounts had been prepared for the respective notional periods.

255. Paragraph 26 sets out specific commencement provisions relating to the repeal of Part 7 of TIOPA. This follows a similar approach to the commencement of the new rules.

256. Paragraph 27 extends the time limit for elections under section 484 and section 486 in the first year to 31 March 2018.

257. Paragraph 28 extends the time limits for the appointment of a reporting company and the revocation of such an appointment in the first year to 31 March 2018. It also extends the filing deadline in the first year to 30 June 2018.

258. Paragraph 29 makes transitional provision by excluding amounts that are being brought into account under the Change of Accounting Practice Regulations 2004 (S.I. 2004/3271) from the rules where the change of accounting policy occurred in a period that commenced before 1 April 2017. In particular, such amounts will be left out of account of both tax-interest and tax-EBITDA amounts.

259. Paragraph 30 makes transitional provision by excluding amounts that are being brought into account under the transitional rules as a result of the changes made to the loan relationship and derivative contract rules (Parts 5 and 7 of CTA 2009) made by Finance (No.2) Act 2015. In particular, such amounts will be left out of account of both tax-interest and tax-EBITDA amounts.

260. Paragraph 31 provides groups with an option to apply the corporate interest restriction rules on the assumption that companies had elected into regulations 7, 8 and 9 of the Disregards Regulations (S.I. 2004/3256). This therefore disregards the fair value movements on certain hedging derivative contracts from being included in the tax-interest and tax-EBITDA figures. Instead it brings these amounts into account in line with the hedged item. For this to have effect, all UK group companies as at 1 April 2017 must elect into this treatment. The election applies to all derivative contracts entered into before 1 April 2020.

261. Paragraph 32 provides for companies with accounting periods beginning on or before 1 April 2018, to make an election before that date under section 433 or section 444 to be treated as a qualifying infrastructure company within Chapter 8.

262. Paragraph 33 provides that a company may be a qualifying infrastructure company in an accounting period beginning before 1 April 2018, if it would meet the tests in section 432 in an accounting period including 1 April 2018 and being at least three months long. Amounts that would be exempted by sections 438, 440, 441 and 442 are reduced on a just and reasonable basis.

263. Paragraph 34 sets out a transitional rule relating to the anti-avoidance provision introduced as section 461.

264. Paragraph 35 provides that the Commissioners may make consequential amendments to secondary legislation which have effect under the same commencement rules.

265. Paragraph 36 sets out an interpretative rule for the preceding paragraphs.

Background note

266. This legislation has its origins in the G20/OECD project to tackle Base Erosion and Profit Shifting (BEPS) in relation to the taxation of international groups of companies. The BEPS project identified a number of key risks to be tackled. It was noted that BEPS risks in the area of interest payments may arise in three basic scenarios:

- Groups placing higher levels of third party debt in high tax countries.
- Groups using intragroup loans to generate interest deductions in excess of the group's actual third party interest expense.
- Groups using third party or intragroup financing to fund the generation of tax exempt income.

267. To address these risks, Action 4 of the OECD's Action Plan on Base Erosion and Profit Shifting, published in 2013, called for recommendations regarding best practices in the design of rules to prevent base erosion through the use of interest expense. Following several rounds of discussions and public consultation, the OECD published recommendations on preventing base erosion through the use of interest expense in October 2015. Following further work, the OECD published additional guidance in December 2016 on the design and operation of the group ratio rule, and approaches to deal with risks posed by the banking and insurance sectors.

268. The recommended approach is based on a fixed ratio rule which limits an entity's net deductions for interest and payments economically equivalent to interest to a percentage of its taxable earnings before interest, taxes, depreciation and amortisation (EBITDA).

269. Recognising that some groups are highly leveraged with third party debt for non-tax reasons, the recommended approach proposes a group ratio rule alongside the fixed ratio rule. This would allow an entity with net interest expense above a country's fixed ratio to deduct interest up to the level of the net interest to EBITDA ratio of its worldwide group.

270. The recommended approach also allows countries to supplement the fixed ratio rule and group ratio rule with other provisions that reduce the impact of the rules on entities or situations which pose a lower BEPS risk, such as:

- A *de minimis* threshold which carves out entities which have a low level of net interest expense. Where a group has more than one entity in a country, it is recommended that the threshold be applied to the total net interest expense of the local group.
- An exclusion for interest paid to third party lenders on loans used to fund public-benefit infrastructure, subject to conditions. In these circumstances, an entity may be highly leveraged but, due to the nature of the assets and the close link to the public sector, the BEPS risk is

reduced.

- The carry forward of disallowed interest expense and/or unused interest capacity (where an entity's actual net interest deductions are below the maximum permitted) for use in future years. This will reduce the impact of earnings volatility on the ability of an entity to deduct interest expense. The carry forward of disallowed interest expense will also help entities which incur interest expenses on long-term investments that are expected to generate taxable income only in later years, and will allow entities with losses to claim interest deductions when they return to profit.

271. This legislation looks to implement the OECD's recommendations as follows.

272. The rules will operate on a worldwide group basis for each period of account of the group's ultimate parent. This will allow groups to manage any restriction across their businesses. The rules will apply to the net interest expense within the charge to Corporation Tax, including other similar financing costs. Groups with less than £2 million of net interest expense within the scope of Corporation Tax per annum will not need to apply the rules. All groups will continue to be able to deduct current period net interest expenses and similar financing costs up to that amount.

273. The fixed ratio method will limit the amount of net interest expense that a worldwide group can deduct against its taxable profits to 30% of its taxable EBITDA. A modified debt cap within the new rules will ensure the net interest deduction does not exceed the total net interest expense of the worldwide group.

274. The group ratio method allows a "group ratio" to be substituted for the 30% figure. The group ratio is based on the net interest expense to EBITDA ratio for the worldwide group based on its consolidated accounts. Interest payable to shareholders and other related parties, and interest on instruments with equity-like features are not reflected in the group ratio.

275. Groups may make irrevocable "chargeable gains" and "alternative calculation" elections to make certain prescribed adjustments to the accounting figures more closely align them to how amounts of "interest" and "EBITDA" would be calculated under UK tax rules. This election has effect for both the operation of the modified debt cap rule and the group ratio method.

276. The public infrastructure rules provide rules which exclude from the scope of the main rules amounts of qualifying interest expense incurred by qualifying companies on funds invested in long-term infrastructure for the public benefit. These rules will not exclude interest payable to shareholders and other related parties (except in the case of some existing loans or where the other party is itself a qualifying company), nor where the lender has recourse to income or assets other than those connected with public benefit infrastructure that is fully within the scope of UK taxation.

277. There are rules to help address timing differences between interest expense and

EBITDA. Amounts of restricted interest are carried forward indefinitely. They are deducted in a later period to the extent there is sufficient interest allowance. Unused interest allowance can be carried forward for up to five years.

278. There are special rules to deal with particular issues, for example: derivatives, Double Taxation Relief, the Patent Box and other tax incentives, joint ventures, the definition of interest in a banking trade, the oil and gas tax regime, Real Estate Investment Trusts (REITs), investments held by insurance companies, members of Lloyd's, the tonnage tax regime, fair value accounting, co-operative and community benefit societies, payments to charities, leases, related parties, and securitisation companies.

279. There is a regime-wide anti-avoidance rule.

280. Legislation for this measure was originally included in the Finance (No.2) Bill 2017. That bill was taken forward on the basis of consensus with a number of clauses left out, including the corporate interest restriction.

281. The legislation is now included in this Finance Bill 2017 in line with the legislation from the previous bill. Some minor revisions to the legislation have been made as a result of points that have raised by external advisers and others, most of which simply clarify that the rules operate in the way intended. The legislation, including these revisions, takes effect from 1 April 2017, as announced in the business tax road map published in 2016 and reconfirmed at Spring Budget 2017.

282. The main revisions made to the legislation are follows:

- Section 382 is revised to treat amounts as tax-interest where those amounts are deductible under particular tax rules, amounts have previously been disallowed and those disallowed amounts would be included in tax-interest. For example, as a result of the hybrid rules at Part 6A of TIOPA 2010.
- Section 402 is revised to ensure that the blended net group-interest expense does not excessively limit the operation of the blended group ratio.
- Section 411 is revised to ensure that amounts in respect of pension schemes are not included in the group-interest figures.
- Section 417 is revised to ensure that the reference to capital expenditure includes capitalised interest and other financing amounts included in the carrying value of a relevant asset.
- Section 425 is revised to ensure that the provision has effect whenever an employee share acquisition arrangement falls to be treated under Parts 11 or 12 of the Corporation Tax Act 2009.
- Section 439 is revised to ensure that the grandfathering provision under

the public infrastructure rules operates correctly where a company has an interest in another company.

- Section 443 is revised to ensure that groups electing into public infrastructure rules which would obtain interest deduction below de minimis should get a de minimis deduction *instead* of the treatment under the public infrastructure rules.
- Section 448 is revised to ensure that decommissioning activities can fall to be qualifying infrastructure activities.
- Section 456 is revised to ensure that this rule operates as a practical alternative to fair value accounting for insurers. It also ensures that the reference to creditor relationships held by an insurer extends to include loans held in connection with the regulation of underwriting business carried on by members of Lloyd's.
- Sections 462 to 472 which sets out the related party definition has been revised. This ensures that the rules which exclude certain arrangements from being related parties have priority over the rules that bring additional arrangements into the related party rules. The revisions also ensure that the main definition is limited to equity interests in an entity, and that 'normal commercial loans' would not normally make the parties related for the purposes of these rules.
- The time limit for appointing a reporting company (paragraph 1 of Schedule 7A) and the filing deadline for an interest restriction return (paragraph 7 of Schedule 7A) have been extended in the first year so that those time limits cannot expire before 31 March 2018 and 30 June 2018 respectively.

283. If you have any questions about this measure, please contact the Corporate Interest Restriction team on email: interest-restriction.mailbox@hmrc.gsi.gov.uk.