October 29, 2021

New Tax Regime for UK Asset Holding Companies

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In a very exciting development for the UK funds industry, the UK Government has released its final policy paper for the new Asset Holding Companies regime, the cornerstone of its review of the UK funds system. This measure is the UK's bid to become the jurisdiction of choice for establishing European asset holding companies, by combining a tax regime competitive with Luxembourg and Ireland with the UK's financial infrastructure and extensive double tax treaty network. Since so many fund managers are themselves based in the UK, bringing the fund vehicles they manage and invest onshore would remove many convoluted constraints around decision making / board presence imposed by local tax "substance" requirements. However, the regime is not limited to UK managed funds and is likely to have wider appeal.

The regime is relevant for most kinds of unlisted investment fund, including credit funds, private equity funds and real estate funds (where it should combine with anticipated changes to the UK REITS regime next year) and for institutional investors investing in these asset classes. To be eligible for Qualifying Asset Holding Company (QAHC) status, broadly, funds must be at least 70% owned by diversely owned funds, charities, long-term insurance businesses, sovereign immune entities and certain pension schemes and public bodies, and must mainly carry out investment activity (with only insubstantial ancillary trading permitted). The Government intends the regime to be available for existing funds by election, and has included entry provisions for market value rebasing of certain assets and the creation of a new accounting period for new QAHCs. The entry charges are, however, expected to be subject to typical reliefs and exemptions such as the substantial shareholding exemption (SSE).

In return, QAHCs gain a wide suite of tax benefits consistent with the regime's self-declared aim: to recognise circumstances where intermediate holding companies are used to facilitate the flow of capital, income and gains between investors and underlying investments, so that investors do not suffer additional tax from participating in these structures and intermediate holding companies pay no more tax than is proportionate to their (limited) activities. Overall, the regime is very generous, with the main limits being drawn at the taxation of profits from trading activities, UK land and intangibles.

Key measures include:

1. **At the Asset Holding Company (AHC) level:**

   - exempting from gains on disposals of certain shares which are not in holding vehicles for UK land, and of overseas property (free from the usual conditions attached to the UK's participation exemption, the SSE)

   - exempting profits of an overseas property business, and associated loan relationships and derivatives profits, which are subject to overseas tax (reducing the administrative burden of claiming double tax relief)

2. **At the return to investor level:**

   - treating premiums paid on a repurchase of share capital from an individual to be treated as capital rather than income distributions

   - exempting repurchases from stamp duty and stamp duty reserve tax (SDRT)

   - disapplying UK withholding tax on payments of interest to investors

- allowing certain amounts paid to qualifying remittance basis users by a QAHC to be treated as non-UK source, reflecting the underlying mix of UK and overseas income and gains

3. **Of benefit to credit funds in particular, tackling tax asymmetry between a QAHC's interest receipts and payments by:**

   - allowing deductions for profit participating and limited recourse debt

   - switching off the late paid interest rules and deeply discounted securities rules in some situations, so that these can be relieved in the QAHC on the accruals basis

Since the proposals are based on sustained engagement with the asset management industry, the draft legislation is expected to adopt many suggested changes in response to concerns raised.

If you would like to discuss any aspect of the regime further please contact Brenda Coleman, Andy Howard, Chris Agnoli or your usual contact in the tax team.