

HMRC DT Treaty Passport Scheme

Frequently Asked Questions

Updated January 2012

Frequently Asked Questions 1 to 17 were published at the introduction of the Double Taxation Treaty Passport (DTTP) Scheme in 2010. We have added the supplementary FAQs 18 to 25 in response to questions asked since then.

1.

Q. Syndicated loans can lead to applications days before an interest payment is due so can a speeded up process be offered?

Can we have a concession for the first interest payment to be tax free?

A. The certified claim system requires a purchaser of a participation in a syndicated loan to make a certified claim for a relief-at-source Direction in respect of the first acquisition of debt-right, with all the time-lapse implications of foreign tax office certification and post delays. The Direction is couched to cover both the first and any subsequent purchases of debt-right from the UK borrower by that lender.

The DTTP scheme will drastically reduce the waiting time with the initial application: the UK borrower will communicate directly with HMRC in its notification of a new participation, and the Direction issued shortly thereafter. There will be no need to wait until HMRC receives a certified claim form via the overseas fiscal authorities.

One consequence of the establishment of a 'notification' relationship between the UK borrower and HMRC will be that taxpayer confidentiality considerations will no longer stop HMRC from keeping the borrower (and its agents) fully abreast of the progress towards issuing a Direction – as is the case where HMRC is dealing with the lender as a claimant.

HMRC is committed to issuing Directions as soon as is practicable and will attempt to assist if there is a particularly tight timescale, but until the new system is up and running and the take-up of passports is known, no specific commitment on turn around time can be made.

The Syndicated Loan Scheme ('SLS') for dealing with syndicated loans does not require individual applications by corporate lending members of a syndicate. Matters are dealt with entirely by the Syndicate Manager, which makes decisions on the withholding tax implications and consequences of changes in lending members and their shares in syndicate income.

The system is designed so that such a concession is not needed, and in any event HMRC is trying to move away from concessions.

2.

Q. Could HMRC offer an automatic clearance if the form is completed correctly?

A. At present we cannot offer this as we don't have the IT capability. As explained at the presentation we hope to increase on line filing capability in the future so we may be able to look again at this question once the technology is in place.

3.

Q. What are the transitional arrangements?

A. The certified claim procedure will remain appropriate for situations where the DTTP scheme may not, or cannot, be used – for example, non-corporate lenders.

4.

Q Is the Direction tied to the period of the passport?

A. Our present policy, which will remain unchanged, is to issue a Direction for no more than 5 years, with some flexibility on a case by case basis – for example, if the certain term of a loan is slightly longer than this. Our policy on the extension/renewal of a Direction is detailed in HMRC DT Guidance Note 8 (go to www.hmrc.gov.uk and enter **DT Guidance Note 8** in the *Search* facility).

This will be the case even when the passport reaches its expiry date prior to the Direction period running out. The only departure from this will be when the Direction is explicitly withdrawn by HMRC (see FAQs 5 & 6 below for further details).

5.

Q. What happens to the borrower if the lender has their passport withdrawn?

A. HMRC would ordinarily need to cancel a Direction to render it void; in making a decision to do so, HMRC would consider, on a case by case basis, the circumstances surrounding the withdrawal of the passport holder status and how that might impact on the right to treaty benefit in respect of the loan concerned.

It is possible that a passport may be withdrawn due to misuse of the passport system where the lending entity still has the general right to treaty benefits: it would be forced then to make claims on a certified basis only, but it may not be necessary to cancel existing Directions issued within the DTTP scheme.

The borrower can therefore rely on a Direction in the usual way unless informed otherwise by HMRC in a notice of cancellation. In this context, the loss of passport holder status by a lender will not **of itself** be viewed as a material change invalidating a Direction.

In a connected party lending situation the borrower may become liable to withholding tax if it knew or might reasonably have been expected to know that the passport holder did not qualify for relief, as this would undermine the good faith basis on which HMRC had acted in issuing the Direction.

6.

Q. It is possible that a loan will cease to qualify for treaty relief after a Direction has been issued by HMRC, for example, because the lender assigns the loan. Where does the onus lie on informing HMRC so they can withdraw the Direction?

A. The present Direction template (which will be maintained) contains the following standard conditions:

'1. The Direction will automatically cease to have effect, and you will need to start to deduct tax at the full rate, if:

- there is any change in the nature or description of the income*
- you learn of any change in the residence status or business details, including changes in name, address or ownership (by way of business sale, transfer or merger), of the recipient of the income*
- there are any changes in your own business details, including changes in name, address or ownership (by way of business sale, transfer or merger).*

If you are in any doubt about whether any of these conditions are triggered, or if you have any questions about their application, get in touch with HMRC Residency, as soon as possible, using our contact details shown in this Direction.

*2. If payments continue after the **expiry date** shown overleaf, you should follow the normal rules on tax deduction that apply at the time you make the payment. If you are in any doubt ask your Tax Office for advice.*

3. This Direction does not affect HMRC's right to make enquiries into your company's tax returns and affairs, to ensure that its self assessment is accurate. In particular, it does not preclude a subsequent challenge under Schedule 28AA Income and Corporation Taxes Act 1988 to the arm's length character of the payments which are the subject of this Direction, in connection with the computation of your company's corporation tax liability. Payments exceeding the arm's length amount cannot be deducted in arriving at the assessable profits or allowable losses of the borrower.'

Clearly, as with any Direction, there is an onus on the borrower to notify us of any material changes it becomes aware of them. HMRC DT Guidance Note 2 goes into some detail about issues surrounding material changes during the lifetime of a Direction (go to www.hmrc.gov.uk and enter **DT Guidance Note 2** in the Search facility).

To repeat what was said in the reply to the previous question: 'the loss of passport holder status by a lender will not **of itself** be viewed as a material change invalidating a Direction.'

In addition, of course, under clause 16 of the Terms & Conditions the passport holder is obliged to notify HMRC of any changes affecting its status as a passport holder.

7.

Q. Would revolving facilities be covered in their entirety or would a new application be needed for each draw down?

A. The underlying relationship between lender and borrower stays essentially the same over the term of a revolving loan facility; in the absence of any material changes over the period of the facility which call into question the basis on which the Direction was made, then the Direction will remain good, within our usual practice on time-limitation.

8.

Q. Could we grant passports for 10 years instead?

A. We have decided on five years initially, which is longer than originally requested in the consultation, where suggestions ranged between one and three years. We may make a policy decision to extend it in the future but that depends entirely on how well the system works.

9.

Q. Will both systems run side by side?

A. Passported loans can be made only from 1 September 2010; to that extent there is no transitional (or phasing-in) period. The certified claim process will continue as the 'default' method of obtaining relief.

10.

Q. Could we give passports automatically to the larger lenders?

A. We cannot discriminate in favour of one class of customers at the expense of all others.

11.

Q. What is the incentive for lenders?

A. The incentive will primarily be the time saved in omitting the certification stage; and the new DTTP notification relationship established between the UK borrower and HMRC (which will simplify communication between the two within taxpayer confidentiality rules) should ease and speed up the Direction process.

Lenders will not be forced by HMRC into applying for a passport, or into using it if they obtain one. The certified claim route to relief remains in place.

12.

Q. Can the database show who has applied for a passport to stop multiple applications from groups?

A. The database will show only those who have been granted passport holder status – that is its main function, to be available for perusal by borrowers in order to verify passport status.

A passport will be required for each corporate member of a group of companies that wish to use the system, just in the same way that certified claims are required from them in non-DTTP situations. There will be no 'group passport' that can be used by any and all members of a group.

13.

Q. Is there any plan to extend the DTTP scheme to applications under the EU Directive on Interest and Royalties?

A. The EU Directive (Council Directive 2003/49/EC) is covered by specific UK legislation dictating its operation and time limits. The DTTP scheme is a change of process within the existing legislation covering withholding tax on payments overseas that are relievable under double taxation arrangements. As such the two systems are and should remain separate – not least to avoid any need for legislative changes.

14.

Q. Why have HMRC restricted the use of an existing certification to one issued within the last 12 months?

A. The 12 month time limit is to ensure that the certification is suitably 'current' and can therefore be presumed to be accurate. 12 months is a convenient and reasonable cut-off.

15.

Q. Why is the onus on the passport holder to tell the borrower of the need to send a Form DTTP2 notification to HMRC?

A. The passport holder has 'signed up' to the terms and conditions of the DTTP scheme whereas the borrower may be unfamiliar with the system; this requirement is a safeguard to ensure that the passport holder alerts the borrower to the latter's obligations under the DTTP system.

16.

Q. What is the purpose of putting passport holder details on a publicly available database if there is a requirement for the passport holder to provide the borrower with relevant details?

A. The database is there so that the borrower can confirm that the lender has a current passport and provides comfort that it is appropriate for them to submit a form DTTP2.

17.

Q. What are the factors that may influence HMRC to decline an application for a passport?

A. The passport application form is designed primarily to confirm the existence and residency status of the prospective passport holder, with the presumption that the applicant will have established a successful and trouble-free DT claim history with HMRC. We anticipate that refusals will be rare, but cannot exclude the possibility that HMRC's previous dealings with the applicant might give us reservations about granting a treaty passport. The factors bearing on HMRC's decision will thus vary on a case by case basis.

Supplementary FAQs – July 2011

18.

Securitisations of contractual debt

Q. In what circumstances would HMRC accept the use of a treaty passport in the purchase or acquisition of this type of debt-right by a passport holder?

A. Large amounts of money can be involved in these acquisitions and the arrangements under which sales and transfers are effected can be complex. And nearly always the UK borrowers are individuals outside the 'UK corporate borrower' scope of the DTTP scheme as set out at paragraph 1 of the DTTP Terms and Conditions.

For such reasons as these the use of a treaty passport would not always be right or appropriate to such transactions.

That said, HMRC is willing to extend the use of the treaty passport facility in situations where

- the purchase or acquisition of the debt-right by the passport holder is effected in a single transaction
- interest payments are gathered in and paid on under a single asset management agreement
- a single UK corporate entity represents itself to be, and self-assessing itself as, liable to a duty to withhold tax under Section 874(2) Income Tax Act 2007 on payments transmitted to the passport holder

Particular regard should be had to paragraphs 13 and 14 of the DTTP Terms and Conditions, especially concerning beneficial ownership considerations (where pertinent to the availability of relief), by the parties to these sorts of transactions in judging whether the use of a passport is appropriate.

19.

Material date of the loan

Q. Can you confirm the material date of the passported loan for the purposes of triggering the deadline of **30 working days** for submitting a **form DTTP2** notification?

A. For most purposes this will be the date the loan is made, and the parties to it have established their lender/borrower status as it will from that date that any interest payments will need the cover of a Direction authorising DT treaty relief at source.

However, where there has been an assignment, sale or other transfer of the debt-right, then the material date will not be the date of the loan as such (which may have been in existence for some years), but the date when this new **loan relationship** between the lender (the treaty passport holder) and the UK borrower came into existence. That is the date when the new owner of the debt-right became entitled to receive interest in place of the original or previous lender.

The 'Loan details' section of the form DTTP2 is being modified to make this clear. For the time being, in such cases we recommend that this section of the form be completed by the borrower on the lines of:

'Date of original loan: dd/mm/yy

Date of loan relationship with treaty passport holder: dd/mm/yy.'

20.

Scope for late notifications on form DTTP2

Q. What scope is there for HMRC accepting late notifications on form DTTP2?

A. The time allowed to borrowers for making an effective notification on a DTTP2 is set out in paragraph 10 of the Terms and Conditions: it is **30 working days** after the loan relationship in question has come into being. Excluding weekends and UK public holidays, this will always allow a borrower over a month to submit the notification and we believe this is reasonable.

HMRC will **not** accept a DTTP2 submitted after the time allowed unless there is a reasonable excuse. Generally, a 'reasonable excuse' is an unusual event that is either unforeseeable or beyond your control which has prevented you from filing the DTTP2 on time. In the absence of a reasonable excuse the DTTP2 notification will, in accordance with the Terms and Conditions, be ineffective and the lender will need to make a full certified claim in the normal way in order to get relief on its interest payments.

21.

UK Guarantors

Q. What is the position of a UK guarantor to a debt with regard to the DTTP scheme?

A. Of its nature the exposure of a guarantor of a debt will be contingent on whether – if at all – it will be called on to act on that guarantee in the case of default by the principal debtor, and assume the responsibility for making interest payments. (Any payments not categorisable as interest do not of course come into any consideration of a DTTP context.)

In the case of such default, a new payer/payee relationship can then be said to exist between the guarantor and the overseas owner of the debt-right, which can then expose the guarantor to a withholding tax obligation. While the loan arrangements giving rise to the guarantee might have existed for some time, and was contracted with a UK borrower other than the guarantor, for the purposes of the DTTP scheme HMRC regards the date from which the guarantee is called upon (and the guarantor assumes liability for payments) as the beginning of a new loan relationship amenable to the use of a passport.

On this footing, and conditional on the guarantor being a UK corporate as provided for under paragraph 1 of the DTTP Terms and Conditions, and absent any resulting changes in the overseas owner of the debt-right, the latter may make use of its passport in substitution for a certified claim in the usual way.

This assumes too that there is no bar to the use of the passport found elsewhere in the DTTP Terms and Conditions.

22.

Changes in a loan and its ownership

Q. Can you clarify the circumstances in which a treaty passport may be used as a substitute for a new or fresh claim?

A. The main purpose of the DTTP scheme is to reduce claim paperwork and delays falling on overseas corporate lenders. It does this principally by replacing the traditional certified claim which requires certification by the taxation authorities of the lender's residence state with a shorter customer-driven notification process.

As a general rule, **and assuming that all relevant DTTP criteria are met**, if a claim form would have been necessary hitherto, then the DTTP passport can be used instead.

Specifically, this can cover

- Changes in material circumstances in the lifetime of a Direction – see DT Guidance Note numbers 2 and 8 (go to www.hmrc.gov.uk and enter **DT Guidance Note 2** or **DT Guidance Note 8** in the *Search* facility)
- Contractual extensions of a loan (being an instance of such a material circumstance)
- The sale or assignment of a loan
- 'UK-source' applications dealt with by DT Guidance Note 1 (go to www.hmrc.gov.uk and enter **DT Guidance Note 1** in the *Search* facility)
- and allowed for under the DTTP Terms and Conditions - (where the borrower believes that it would be liable to UK withholding tax on interest payments)

where the existing or new lender is a passport holder; a borrower may then submit a DTTP2 notification in place of a claim form (certified or otherwise) from the lender that would otherwise be required.

Please see the Guidance Notes mentioned above before you make any decision to take the DTTP route, as compliance with them (in all save the claim form procedures they detail) will still be incumbent to the parties to a loan.

So far as changes, extensions and transfers of debt-right are concerned intending users of a passport in these circumstances should be especially careful to judge whether the material changes involved are potentially of such a nature as would prudently merit a fresh claim or passport application (where, for example, the passport holder's name has changed). This would be a matter for the parties to the transaction to weigh up for themselves, having regard to factors like (but not limited to) the commercial terms of the new or extended loan relationship, and any cross-ownership or community of interest relationship between the parties to a deal.

23.

United States LLCs, S Corporations and the like – fiscal transparency considerations

Q. Can you explain how these sorts of US business forms interact with the DTTP scheme?

A. The possession and use of a passport involves a significant departure from the traditional certified claim procedure with its checks and verification procedures. With these considerations in mind, the intention of the scheme is to limit the granting of passports to independent foreign corporate entities and business forms treated in their country of residence as such, possessing in full corporate personality characteristics that allow HMRC to consider them wholly responsible and accountable for their actions.

Non-acceptance into the passport scheme does not mean that HMRC is denying a right to make claims for DT relief, but simply that it does not consider the applicant in question to meet the intentionally narrow criteria defining those for whom the scheme is intended. Hence, for example, HMRC will continue to take certified claims in the name of fiscally transparent US partnerships in the usual way, even though these are ineligible for passports.

A United States LLC which has elected under 'check the box' to be taxed on a simple corporate basis is eligible to apply for and use a passport, as it meets the criteria of both Article 3(1)(b) of the UK/USA Double Taxation Convention and paragraph 1 of the DTTP Terms and Conditions.

Conversely, an LLC which is taxed on a fiscally transparent (partnership) basis is not eligible for a passport.

Although US S Corporations are required to file separate US income tax returns they are (in broad terms) required to determine and allocate 'tax attributes' (linked to business profits) to their individual owners proportionate to their share ownership; these tax attributes are then brought into account in assessing that owner's overall tax exposure.

Given this essential look-through basis of S Corporations' tax treatment under US tax rules, they are not considered by HMRC to possess the necessary attributes of being treated and taxed in themselves as a corporation sufficient to meet the tests set out in Paragraph 1 of the DTTP Terms and Conditions. They are thus to be regarded as ineligible for treaty passports.

In more general terms, HMRC does not consider as suitable for a treaty passport any US business form that is taxed under US tax rules on a 'disregarded' or 'branch' basis – that is, one that is not treated as separate from its owner for US tax purposes. This remains the case even where the disregarded concern is in legal form a corporation, or has elected for corporate tax status – such as a single-owner LLC electing for corporate tax status but which is also then 'disregarded' and subsumed in the tax treatment of its parent. HMRC will continue to entertain claims – in the usual certified form – from such concerns.

24.

Q. Can a 'branch' or permanent establishment of a company doing business in a country other than that of its head office rely on the DTTP passport of that parent?

A. Yes.

Where, for DT treaty purposes, HMRC regards that branch as being indistinguishable from its head office, then the double taxation arrangements the UK has with the country of residence of that head office governs what relief from UK withholding tax might be available to interest paid to the branch.

That being the case, if a loan is suitable for DTTP treatment when made by the head office, then it can be considered as so eligible when made by a branch, subject, of course, to it meeting all other DTTP criteria for suitability and any tests (such as subject to tax in the head office residence country) laid out in the relevant double taxation treaty relied on to obtain relief.

25.

Syndicated Loans

Q. What are the options for the use of a treaty passport with syndicated loans?

A. A syndicate as such cannot be a treaty passport holder.

Where the syndicate has chosen to be treated as an entity under the Syndicated Loan Scheme (formerly the PTRS), it will be the Syndicate Manager which conducts the syndicate's dealings with HMRC. Possession of a passport by the overseas lender will help the Syndicate Manager to judge the availability of DT relief available to the syndicate as a whole.

If passport holders are lending members of a syndicate that is outside the SLS, then it is open to them to make use of their passport in substitution for a certified claim (assuming the satisfaction of all relevant DTTP conditions – for example, beneficial ownership where relevant). The UK borrower must then tell HMRC of that use within the required time frame with a DTTP2 notification, leading to the issue of a Direction enabling relief at source on the interest payments to that passport holder.

Overseas lending members of a non-SLS syndicate that do not possess a passport will need to make a certified claim in the normal way.

Where a UK borrower has a loan facility with multiple lenders, and frequent buying into or trading of debt-right, then HMRC recognises that individual DTTP2 notifications may place an undue compliance burden on that borrower.

As a consequence, HMRC is willing to consider entering into arrangements with that borrower whereby these individual notifications can be swept up into a monthly consolidated notification. This will still require a passport holder to follow the procedure with the borrower set out at paragraph 9 of the DTTP Terms and Conditions - for example, specifying the rate of DT relief it considers itself entitled to - but in a modified form appropriate to the borrower's circumstances.

UK borrowers wishing to enter into such arrangements with HMRC should contact **HM Revenue & Customs, LBS DT Treaty Team, Barkley House, Castle Meadow Road, Nottingham, NG2 1BA**, telephone **0115 974 0897**.