

Part 1: Real Estate Investment Trusts (“UK REITs”)

Overview

1. This Part sets out the rules applicable to Real Estate Investment Trusts (“UK REITs”).

2. The UK REIT regime was introduced by sections 103 to 145 of, and Schedules 16 and 17 to, FA 2006 and came into force in respect of accounting periods beginning on or after 1 January 2007. It has subsequently been amended by section 52 of, and Schedule 17 to, FA 2007. The following sets of regulations have also been made under the regulation making powers in the UK REIT legislation:

- The Real Estate Investment Trusts (Breach of Conditions) Regulations 2006 (SI 2006/2864);
- The Real Estate Investment Trusts (Financial Statements of Group Real Estate Investment Trusts) Regulations 2006 (SI 2006/2865);
- The Real Estate Investment Trusts (Joint Ventures) Regulations 2006 (SI 2006/2866);
- The Real Estate Investment Trusts (Assessment and Recovery of Tax) Regulations 2006 (SI 2006/2867);
- The Real Estate Investment Trusts (Joint Venture Groups) Regulations 2007 (SI 2007/3425);
- The Real Estate Investment Trusts (Financial Statements of Group Real Estate Investment Trusts) (Amendment) Regulations 2007 (SI 2007/3536); and
- The Real Estate Investment Trusts (Breach of Conditions) (Amendment) Regulations 2007 (SI 2007/3540).

3. A UK REIT is a group of companies (a “group UK REIT”) or a single company (a “company UK REIT”) which gives a notice under clause 5 and has not ceased to be a UK REIT in accordance with clause 54, 55 or 61.

4. Provided that a UK REIT meets certain conditions (see Chapter 2 of this Part and clauses 19 (entry charge), 29 (distributions) and regulations made under section 973 of ITA (SI 2006/2867)), there is no charge to corporation tax (or income tax in the case of certain non-UK companies) on profits or gains arising in respect of “property rental business” (or “UK property rental business” in the case of non-UK companies). “Property

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rental business” is defined in clause 2(1), “UK property rental business” is defined in clause 3 and “non-UK company” is defined in clause 80(2).

5. Though the source legislation is recent a number of fundamental changes have been made as part of the process of rewriting it to make it even more accessible.

6. Distributions made by the principal company of a group UK REIT or company UK REIT in respect of profits and gains of property rental business are subject to deduction of tax at source under regulations made under section 973 of ITA (SI 2006/2867). In the hands of a shareholder, the distribution is treated as if it is UK property business income and is taxed accordingly with a credit for tax which has already been deducted at source.

7. As most UK REITs operate as groups of companies, the rewritten legislation makes the position of group UK REITs more prominent than in the source legislation.

Q1. We welcome comments on the refocusing of the legislation, making the position of group UK REITs more prominent and clearer .

8. As part of this refocusing, the clauses also incorporate paragraph 32 of Schedule 17 to FA 2006 (which deals with non-UK companies) into the rewritten legislation. As a consequence of this incorporation it will no longer be necessary to cross-refer to modified legislation.

Q2. We welcome comments on the proposal to incorporate legislation on non-UK companies directly into the legislation dealing with group companies.

9. The rewritten legislation has also been made more user-friendly by the enactment of certain regulations which modify the primary legislation through layers of cross-references. In particular it is proposed to enact the regulations dealing with joint venture companies (SI 2006/2866) and breach of conditions (SI 2006/2864 and SI 2007/3540), except for regulation 11 of SI 2006/2864 which will be relocated into SI 2006/2867 (recovery and assessment).

10. It is also proposed that the regulations on joint venture groups (SI 2007/3425) be enacted, although this has not yet been done. We will consult on the incorporation of SI 2007/3425 in due course. See *Changes 662* and *663* in Annex 1.

Q3. We welcome comments on the proposal to enact and revoke SI 2006/2864 (except for regulation 11), SI 2006/2866, SI 2007/3425 and SI 2007/3540.

11. The legislation has also been reorganised so that the exemptions from tax (Chapter 3) are more prominent. Most of the breach of conditions legislation (which incorporates SI 2006/2864 and SI 2007/3540) has been placed in Chapters 8 and 9. The rewritten joint venture legislation (which currently incorporates SI 2006/2866 but in due course will also include SI 2007/3425) has been placed towards the end of the Part in Chapter 10 and a number of definitions are at the end of the Part in Chapter 11.

Q4. We welcome comments on the organisation of the rewritten legislation.

12. Finally, the legislation has been rewritten without the use of the labels found in section 105 of, and paragraph 2 of Schedule 17 to, FA 2006. As part of the simplification of the legislation, the references to “C (tax-exempt)” and “G (property rental business)” have been replaced with references to a company or group so far as it carries on property rental business. Further, references to “tax-exempt business” have been replaced with references to property rental business as defined in clause 2. See *Change 660* in Annex 1.

Q5. We welcome comments on the proposal to replace the labels “C (tax-exempt)”, “G (property rental business)” and “tax-exempt business”.

Chapter 1: Introduction

Clause 1: Overview of Part

13. This clause provides an overview of the Part. It is new.

14. *Subsection (1)* sets out the “bargain” which is entered into by a group of companies on becoming a UK REIT. Where the group meets certain conditions it benefits from an exemption from corporation tax (and, through the operation of clause 3(3), an exemption from income tax for non-UK companies) in respect of profits and gains arising or accruing in respect of property rental business. This benefit comes with the following liabilities:

- an entry charge (clause 19),
- a requirement that the principal company of a group deducts sums representing income tax in respect of distributions made to shareholders (section 973 of ITA and SI 2006/2867), and
- the treatment of such distributions as profits of a UK property business rather than dividend income in the hands of shareholders (clause 29).

15. *Subsection (2)* makes similar provision in respect of companies which enter the UK REIT regime other than as part of a group.

16. *Subsections (3) to (8)* provide signposts to the remaining Chapters of the Part.

Clause 2: Meaning of “property rental business”

17. This clause defines “property rental business” for the purposes of the Part. It is based on section 104(1) and (2) of, and paragraph 32(2) of Schedule 17 to, FA 2006.

18. *Subsection (1)* defines “property rental business”. It is based on section 104(1) of FA 2006. As the definition of “Schedule A” (section 832 of ICTA) is being rewritten in Bill 5, reference is made to the definitions in [clauses 197[j050102] and 198[j050113] of Bill 5] rather than section 832 of ICTA.

19. [Clause 197[j050102] of Bill 5] provides:

A company’s UK property business consists of-

- (a) every business which the company carries on for generating income from land in the United Kingdom, and
- (b) every transaction which the company enters into for that purpose otherwise than in the course of such a business.

20. [Clause 198[j050113] of Bill 5] provides:

A company’s overseas property business consists of-

- (a) every business which the company carries on for generating income from land outside the United Kingdom, and
- (b) every transaction which the company enters into for that purpose otherwise than in the course of such a business.

21. *Subsection (3)* provides that, for non-UK companies, business is “property rental business” if it would be property rental business if carried on by a UK company. See clause 80 for the definitions of UK company and non-UK company. This provision ensures that the worldwide property rental business of a non-UK company is treated as property rental business for the purposes of the Part.

22. The definition of “tax-exempt business” in section 107(2) of FA 2006 has not been rewritten. Instead reference is made to “property rental business” throughout the rewritten legislation. The reason for not rewriting the reference to “tax-exempt business” is that the definition is slightly confusing as it suggests that the company must carry on a “tax-exempt business” to be within the regime. However, regulations 5 and 6 of SI 2006/2864 allow a company to breach the tax-exempt conditions set out in section 107 of FA 2006 and remain within the regime. It is clear from the rewritten legislation,

however, that the conditions in clause 10 must be met for a group or a company to remain within the UK REIT regime.

23. As “property rental business” and “UK property rental business” are the operative definitions, it is these which are defined and used throughout the rewritten legislation. See Q5 in the Overview commentary and *Change 660* in Annex 1.

Q6. We welcome comments on the proposal not to include a definition of “tax-exempt business” in the rewritten legislation.

Clause 3: “UK property rental business” of non-UK companies

24. This clause defines “UK property rental business” for the purposes of non-UK companies and treats profits of such business, which would ordinarily be charged to income tax, as chargeable to corporation tax. It is based on paragraph 32(1), (3) and (5) of Schedule 17 to FA 2006.

25. *Subsections (2) and (3)* provide that profits of UK property rental business of non-UK companies (including non-UK joint venture companies) which are subject to income tax under Chapter 3 of Part 3 of ITTOIA, are to be treated as being subject to corporation tax (and not income tax).

26. Subsections (2) and (3)(a) are needed to bring UK property rental business of non-UK companies within the charge to corporation tax so that provisions such as clauses 15 (tax treatment of profits) and 22 (ring-fencing) will apply to all non-UK companies.

27. As the source legislation (paragraph 32(3) of Schedule 17 to FA 2006) does not specify whether it is profits and/or gains of UK property rental business which are to be made subject to corporation tax, the legislation is drafted so that only *profits* of UK property rental business, which are not already subject to corporation tax, are caught by this section. This approach ensures that gains of non-UK companies with no permanent establishment in the UK are not brought within the charge to tax in the UK. See *Change 659* in Annex 1.

Q7. We welcome comments on the proposal to rewrite paragraph 32(3) of Schedule 17 to FA 2006 so that it only applies to *profits* of UK property rental business.

28. Subsections (2) and (3)(b) (based on paragraph 32(5) of Schedule 17 to FA 2006) are needed to ensure that non-UK companies will not be subject to either income tax or corporation tax in respect of profits of UK property rental business. Section 6 of ICTA (which is rewritten in [clause 3[j9106] of Bill 5]) provides that where amounts are charged to corporation tax and the company operates through a permanent establishment,

those amounts are not also subject to income tax. Consequently, non-UK companies which do not operate through a permanent establishment are, but for clause 3(3)(b), subject to both corporation tax and income tax in respect of profits of UK property rental business.

Clause 4: Meaning of “residual business”

29. This clause defines “residual business” for the purposes of the Part. It is based on section 105(3)(c) of, and paragraph 2(c) of Schedule 17 to, FA 2006.

30. The reason for the definition of residual business is two-fold. Firstly, it is needed to identify the profits and gains which are charged to corporation tax at the main rate under clauses 15(3) and 16(6). Secondly, it is needed to identify items to be included in the financial statements in accordance with clause 13(2)(c).

31. For non-UK companies the definition of residual business has been aligned with the definition used for other members of a group. It is based on paragraph 2(c) of Schedule 17 to FA 2006 which provides that residual business is all business other than property rental business.

32. Paragraph 32 of Schedule 17 to FA 2006 (non-UK companies) provides no specific modification to the general definition in paragraph 2(c). So the definition in paragraph 2(c) applies for the purposes of the preparation of financial statements (paragraph 31 of Schedule 17 to FA 2006) and for references to *profits* of residual business.

33. However, paragraph 32(6)(c) of Schedule 17 to FA 2006 has the effect that references to *gains* of residual business are to any *UK business* which is not *UK property rental business*.

34. Rather than have two definitions of residual business for non-UK companies (one for profits, the other for gains) the definition is aligned for the purposes of residual gains by expanding it to include *worldwide business*, and contracting it to exclude *all property rental business*.

35. The alignment of the definition of residual business has no effect on the amount of tax payable by non-UK companies in respect of gains. This is because non-UK companies are not liable to tax on overseas gains.

<p>Q8. We welcome comments on the proposal to simplify the definition of residual business for the purposes of non-UK companies so that it is the same for the purpose of all members of a group UK REIT.</p>
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Chapter 2: Requirements for being a UK REIT

Clause 5: Becoming a UK REIT: notice

36. This clause provides that, in order to be a “group UK REIT” (or a “company UK REIT”), the principal company of the group (or the company) must give notice of entering the UK REIT regime. It is based on sections 106(1), (3) and (4), 109(1) and 134(1) of, and paragraphs 5(1) and 8(1) of Schedule 17 to, FA 2006.

37. *Subsections (1) and (2)* provide that a group of companies can give notice for the UK REIT regime to apply from the beginning of a specified accounting period of the principal company. Where a group notice is given, all 75% subsidiaries of the group (as defined in clause 79) are included in the UK REIT regime.

38. Subsection (2) is drafted by reference to the accounting period of the principal company as it is likely that this was what was intended in paragraph 8(1) of Schedule 17 to FA 2006.

Q9. We welcome comments on the proposal to clarify that the notice must specify an accounting period of the principal company.

39. *Subsections (3) and (4)* make similar provision for a company (other than as a member of a group) to give notice to enter the UK REIT regime.

40. It is possible for a company with a 75% subsidiary to give notice under subsection (3) on its own, in which case none of its 75% subsidiaries is included in the UK REIT regime.

41. If a company UK REIT gives notice under subsection (3) and subsequently wants an existing 75% subsidiary to be brought within the regime, a group notice under clause subsection (1) needs to be given. The new notice must comply with all the requirements of clause 6. For example, the new notice must specify the accounting period of the principal company from which the notice is to take effect and it must be given before the accounting period from which it is to take effect.

42. If a company UK REIT gives notice under clause 67(2) for a joint venture company to be treated as forming a group UK REIT with the company UK REIT, the notice does not cause any 75% subsidiaries of the company UK REIT to be brought within the regime.

43. *Subsection (5)* provides that the principal company of a group, or a company, can only give notice if it is a “UK company” as defined in clause 80 and if it is not an open ended investment company.

44. It is unclear from the source legislation (in particular sections 106(2), 107(1) and 108(1) of FA 2006) whether a group or a company becomes a UK REIT from the date specified in a section 109 of FA 2006 notice or when the various conditions set out in sections 106(2), 107(1) and 108(1) of FA 2006 are satisfied. *Subsection (6)* addresses this by making it clear that a group or a company becomes a UK REIT from the beginning of the accounting period specified in the notice given under clause 5.

Q10. We welcome comments on the proposal to clarify that a group or company becomes a UK REIT from the beginning of the accounting period specified in the notice of entry to the regime.

45. *Subsection (7)(c)* defines “UK REIT” as meaning either a “group UK REIT” or a “company UK REIT”. *Subsections (7)(a)* and *(7)(b)* define “group UK REIT” and “company UK REIT” respectively as being a group or a company which has given notice under clause 5. These new labels are used throughout the legislation for ease of reference.

46. Section 103(3) of FA 2006, which provides that “a company or group to which this Part applies may be referred to as a Real Estate Investment Trust”, is not rewritten as this expression is not used elsewhere in the legislation.

Q11. We welcome comments on the new label “UK REIT” and on the proposal not to rewrite section 103(3) of FA 2006.

Clause 6: Supplementary provision about notices under section 5

47. This clause makes supplemental provision about the notice given under clause 5. It is based on sections 109(2) to (5) and 134(1) of, and paragraph 8(2) of Schedule 17 to, FA 2006.

48. *Subsection (1)* lists what the principal company of a group or a single company must provide in order to give a valid notice under clause 5.

49. *Subsection (1)(a)* requires the notice to be given in writing to “an officer of Revenue and Customs” rather than to “the Commissioners for Her Majesty’s Revenue and Customs” (section 109(2)(a) of FA 2006). This is because in practice it is an officer who is given the notice. See *Change 601* in Annex 1.

Q12. We welcome comments on the proposal to replace “the Commissioners of Her Majesty’s Revenue and Customs” with a reference to “an officer of Revenue and Customs”.

Clause 7: Duration of status as UK REIT

50. This clause provides that once a group or single company becomes a UK REIT, it continues to be a UK REIT until the regime ceases in accordance with clause 54, 55 or 61. It is based on section 110 and 134(1) of, and paragraph 4 of Schedule 17 to, FA 2006.

Clause 8: Being a UK REIT in relation to an accounting period

51. This clause makes it clear that once a notice under clause 5 has been given, the principal company of a group, or the company, must meet the conditions set out in the remainder of this Chapter in relation to all accounting periods. It is based on sections 106(1) and (2), 107(1) and (2), 108(1) and 134(1) of, and paragraph 4, 5(1) and (2) and 6(1) of Schedule 17 to, FA 2006.

52. *Subsection (2)(e)* provides that the principal company must prepare and submit financial statements to “an officer of Revenue and Customs” rather than to “the Commissioners for Her Majesty’s Revenue and Customs” (see paragraph 5(2) of Schedule 17 to FA 2006). This is because in practice it is an officer who receives and examines the financial statements provided under clause 13, not the Commissioners. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

Clause 9: Conditions for company

53. This clause sets out the conditions which the principal company of a group or, in the non-group case, the company, must meet throughout each accounting period. It is based on section 106(3) to (9) of, and paragraph 3(1) of Schedule 17 to, FA 2006.

Clause 10: Conditions as to property rental business

54. This clause sets out the conditions which need to be satisfied by a group or company in respect of its property rental business. It is based on sections 107(1), (3), (4) and (6), of, and paragraph 6(1) of Schedule 17 to, FA 2006.

55. *Subsections (1) and (2)* provide that the “property rental business” (defined in clause 2) must comprise at least three properties with no single property accounting for more than 40% of the total value of the properties involved in the business.

56. *Subsection (3)* provides that, for the purposes of this clause, the property rental business of a group is treated as single business.

57. For the purposes of the conditions in subsections (1) and (2), all worldwide properties of non-UK companies are taken into account. This is because paragraph 6(1) of Schedule 17 to FA 2006 provides that “for the purposes of section 107(1) the property rental businesses of the members of the group shall be treated as a single business”.

58. Since paragraph 32(2) of Schedule 17 to FA 2006 provides that “business carried on by a non-UK resident company is property rental business for the purposes of this Part if the business would be property rental business within the meaning given by section 104 [of FA 2006] if it were carried on by a UK resident company”, the property rental business includes the worldwide property rental business of non-UK companies. By including the worldwide property rental business of non-UK companies, condition A in clause 10 is easier to satisfy. However, condition B in clause 10 may, depending on the circumstances, be more difficult to satisfy, for example where a non-UK company has an overseas property worth more than 40% of the total value of the properties involved in the property rental business.

Q13. We welcome comments on the proposal to provide that the worldwide property of non-UK companies is taken into account when working out whether the conditions in clause 10 are satisfied.

59. This clause is drafted on the basis that there is no percentage reduction where property is held by a subsidiary which is not wholly owned by the group UK REIT.

Q14. We welcome comments on the proposal to take into account of 100% of all properties, rather than only the relevant percentage.

60. It is unclear from the source legislation whether properties owned by joint venture companies should be taken into account in this clause. Section 138 of FA 2006 provides that regulations may be made for the Part to apply. As regulations have been made it is considered that the Part, including section 107 of FA 2006, applies to joint venture companies unless there is something to the contrary in SI 2006/2866.

Q15. We welcome comments on the proposal to include properties owned by joint venture companies for the purposes of satisfying the property rental business conditions.

Clause 11: Condition as to distribution of profits

61. This clause sets out the distribution condition which needs to be satisfied by the principal company of a group or, in the non-group case, by a company. It is based on section 107(8) and (9) of, and paragraphs 6(4) and (5) and 32(8) of Schedule 17 to, FA 2006.

62. *Subsection (1)* provides that, in relation to an accounting period of the principal company, the principal company must distribute at least 90% of the group’s “UK profits”.

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63. *Subsection (2)* defines “UK profits” as the sum of the profits shown in the financial statements under clause 13(2)(b). Clause 13(3) provides that this is the sum of the profits arising from the property rental business of the UK members of the group together with the profits arising from UK property rental business carried on by non-UK companies. Clause 14(3) confirms that where a non-member of the group holds a percentage of the beneficial interest in a member of a group, that percentage is excluded from the financial statements and therefore also from the calculation of profits which this clause requires to be distributed.

64. *Subsection (4)* provides that, in relation to an accounting period of a company, the company must distribute at least 90% of profits of the group’s property rental business.

65. The distribution requirement in this clause also applies to the relevant proportion of profits generated by joint venture companies (regulations 6(1) and 10(3) of SI 2006/2866). See clause 67(1) which treats a joint venture company as a member of the group UK REIT and clause 67(2) which treats a company UK REIT and a joint venture company as forming a group UK REIT.

66. The requirement to distribute at least 90% of the group’s “UK profits”, or “profits” in the case of a company UK REIT, does not extend to chargeable gains. This contrasts with section 121 of FA 2006, rewritten in clause 29 (distribution treated as UK property business income in hands of shareholder) and section 973 of ITA (deduction of sums representing income tax at source) which apply to profits *and gains* of property rental business (or UK property rental business in the case of non-UK companies).

67. For the purposes of non-UK companies, the source legislation (paragraph 32(8)(a) of Schedule 17 to FA 2006, as modified by paragraph 6 of Schedule 17 to FA 2006) is ambiguous about whether it requires profits *and gains* of UK property rental business to be distributed. However, as section 107(8) does not refer to gains, it is considered that paragraph 32(8)(a) is not meant to catch gains.

<p>Q16. We welcome comments on the proposal to rewrite the distribution requirement to make it clear that for non-UK companies it only applies to profits.</p>

Clause 12: Conditions as to balance of business

68. This clause sets out the balance of business conditions which need to be satisfied by a group or company. It is based on sections 108(2) and (3) and 134(1) of, and paragraphs 4, 7 of Schedule 17 to, FA 2006.

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69. *Subsection (1)* provides that at least 75% of the “total profits” of the group or company must relate to property rental business. “Total profits” is defined in *subsection (2)* for groups and *subsection (3)* for companies.

70. Subsections (1) and (2) refer to “profits” (as does section 108 FA 2006) despite the fact that paragraph 7 of Schedule 17 to FA 2006, which modifies section 108, refers to “*income* accruing from tax-exempt business”. As there are no references to “income” in section 108 it is considered that the reference in paragraph 7 should be to “profits”.

Q17. We welcome comments on the proposal to refer to profits rather than income in subsections (1) and (2).

71. The amount to be included as “profits” is provided by section 108(2)(b) of FA 2006. This provision appears to apply for the purposes of both a group UK REIT and a company UK REIT. However, paragraph 7(a) of Schedule 17 to FA 2006 provides a different definition of profits for the purposes of a group UK REIT (assuming that the reference in paragraph 7(a) to “*income* accruing from tax-exempt business” refers to “*profits* accruing from the tax-exempt business”).

72. The legislation has therefore been rewritten so that subsection (2) (based on paragraph 7(a) and (b) of Schedule 17 to FA 2006) applies to a group UK REIT and *subsection (4)* (based on section 108(2)(b) of FA 2006) only applies to a company UK REIT.

Q18. We welcome comments on the proposal to rewrite section 108(2)(b) of FA 2006 so that it only applies to company UK REITs.

73. This clause refers to the group’s or company’s “property rental business” rather than “tax-exempt business” (used in section 108 of FA 2006) or “G (property rental business)” (used in paragraph 7 of Schedule 17 to FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

74. It is not clear from the source legislation whether the balance of business tests should include the worldwide profits and assets of non-UK companies. There is nothing in paragraph 32 of Schedule 17 to FA 2006 dealing specifically with the application of section 108 of FA 2006 to non-UK companies.

75. However, since section 108 of FA 2006, as modified by paragraph 7 of Schedule 17 to FA 2006, provides that profits and assets of G (property rental business) are treated as income and assets of tax-exempt business it is likely that it is intended that the worldwide profits and assets of non-UK companies should be included for the purposes of the balance of business tests.

Q19. We welcome comments on the proposal to include the worldwide profits and assets of property rental business of non-UK companies for the purpose of satisfying the balance of business tests.

76. The balance of business test in this clause includes the relevant proportion of property rental business of a joint venture company. See clause 67(1) which treats a joint venture company as a member of a group UK REIT and clause 67(2) which treats a company UK REIT and a joint venture company as forming a group UK REIT. (It should be noted that a separate balance of business test must be satisfied by each joint venture company. See clause 67(4)(b).)

Clause 13: Financial statements for group UK REITs

77. This clause sets out the requirements which need to be satisfied for the purposes of clause 8(2)(e) in respect of group financial statements. It is based on paragraphs 3(3), 31(2) and 32(8) of Schedule 17 to FA 2006.

78. *Subsection (2)* refers to the “group’s property rental business” rather than “G (property rental business)”. See Q5 in the Overview commentary and *Change 660* in Annex 1.

79. Subsection (2)(a) provides that the principal company must prepare financial statements for the group’s property rental business. It is based on paragraph 31(2)(a) of Schedule 17 to FA 2006. Further, paragraph 32(2) of Schedule 17 to FA 2006 states that “business carried on by a non-UK resident company is property rental business for the purposes of the Part if the business would be property rental business ... if it were carried on by a UK resident company”. (However, paragraph 32(8)(d) of Schedule 17 to FA 2006 provides that only profits and gains of UK property rental business are treated as profits and gains of a UK resident member for the purposes of a financial statement for G (property rental business).) The rewritten legislation is drafted on the basis that it is intended that such financial statements should include the worldwide property rental business of the group. This includes a non-UK company’s worldwide property rental business (see paragraph 2(b) of Schedule 17 to FA 2006).

Q20. We welcome comments on the proposal to draft subsection (2)(a) so that it includes worldwide property rental business of non-UK companies.

80. Subsection (2)(b) provides that the principal company must prepare financial statements for the group’s property rental business in the United Kingdom. *Subsection (3)* defines the group’s property rental business in the United Kingdom as property rental business carried on by UK companies and UK property rental business of non-UK companies. For non-UK companies, this provision is based on paragraph 32(8)(d) of Schedule 17 to FA 2006 which provides that only profits and gains of UK property rental

business are treated as profits and gains of a UK resident member for the purposes of a financial statement for G (property rental business).

81. Subsection (2)(c) provides that the principal company must prepare financial statements for the group's residual business. Financial statements under subsection (2)(c) relate to all business which is not property rental business. For non-UK companies the legislation has been drafted on the basis that the financial statements must include *worldwide* business which is not property rental business. This follows paragraph 2(c) of Schedule 17 to FA 2006.

Q21. We welcome comments on the proposal to draft subsection (2)(c) so that it includes worldwide business which is not property rental business in the case of non-UK companies.

82. The requirement to prepare financial statements under subsection (2)(a) and (b) also applies to venturing companies and venturing groups (defined in clause 68) and the relevant percentage of profits of property rental business of the joint venture company (regulations 5 and 12 of SI 2006/2866). See clause 67(1) which treats a joint venture company as a member of the group UK REIT and clause 67(2) which treats a company UK REIT and a joint venture company as forming a group UK REIT.

83. Financial statements under this clause exclude any “non-member percentage” (that is, any percentage of the beneficial interest in a member of the group held by a non-member), see clause 14(3).

Clause 14: Financial statements: further provision

84. This clause sets out further requirements in respect of the preparation of financial statements under clause 13 and also provides a regulation making power. It is based on paragraphs 31(3) to (7) and 32(8) of Schedule 17 to FA 2006.

85. *Subsection (3)* cross refers to clause 13(2) which refers to a “group's property rental business” rather than “G (property rental business)”. See Q5 in the Overview commentary and *Change 660* in Annex 1.

86. *Subsection (5)(c)* provides that the Commissioners may make regulations specifying the deadline for submitting a financial statement to an officer of Revenue and Customs. The clause refers to an “an officer of Revenue and Customs” in subsection (5)(c) rather than “the Commissioners” (see paragraph 31(7)(c) of Schedule 17 to FA 2006). This is because in practice the financial statements are submitted to an officer, rather than to the Commissioners. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

Chapter 3: Tax treatment of profits and gains of UK REITs

Clause 15: Profits

87. This clause sets out the tax treatment of profits of property rental business and residual business. It is based on sections 119 and 134(1) of, and paragraphs 17 and 32(4) of Schedule 17 to, FA 2006.

88. *Subsection (1)* provides that profits of property rental business of a UK company (including a UK joint venture company) which is, or is a member of, a UK REIT are not charged to corporation tax. It is based on section 119(1) of, and paragraph 17(1) of Schedule 17 to, FA 2006.

89. The source legislation provides that profits arising from the business of C (tax-exempt)/G (property rental business) shall not be charged to corporation tax. The references to C (tax-exempt)/G (property rental business) are replaced in subsection (1) with a reference to “property rental business”. See Q5 in the Overview commentary and *Change 660* in Annex 1.

90. *Subsection (2)* provides that profits of UK property rental business of a non-UK member of a group UK REIT (including a non-UK joint venture company) are not charged to corporation tax. It is based on paragraph 32(4) of Schedule 17 to FA 2006. This subsection applies to all profits of UK property rental business, since clause 3(2) and (3)(a) (based on paragraph 32(3) of Schedule 17 to FA 2006) provides that profits of UK property rental business which are chargeable to income tax under Chapter 3 of Part 3 of ITTOIA are instead be chargeable to corporation tax.

91. *Subsection (3)* provides that profits of residual business of a UK company which are charged to corporation tax are charged at a rate determined without reference to the small companies’ rate in section 13 of ICTA (ie they will be charged at the main corporation tax rate). This subsection is based on section 119(2) of, and paragraph 17(1)(b) of Schedule 17 to, FA 2006.

92. It is debatable whether subsection (3)(b) (based on section 119(2) of FA 2006) is necessary since all profits of UK companies are subject to corporation tax. By retaining subsection (3)(b) it is clear that subsection (3) is not a charging provision. However, it may be seen as misleading as it could suggest that some profits of UK companies may not be subject to corporation tax.

Q22. We welcome comments on the proposal to retain subsection (3)(b).
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93. Subsection (3) does not apply to non-UK companies (including non-UK joint venture companies). This is because section 134(1) of FA 2006 provides that the provisions of the Part apply to group members unless there is something to the contrary in

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Schedule 17 to FA 2006. Paragraph 17(1) of Schedule 17 to FA 2006 provides that section 119 of FA 2006 only applies to UK companies. Since paragraph 32 of Schedule 17 to FA 2006 only modifies section 119(1) for the purposes of non-UK companies and does not mention section 119(2) of FA 2006, it is considered that section 119(2) does not apply to non-UK companies. So subsection (3) does not apply to non-UK companies.

Q23. We welcome comments on the proposal that subsection (3) should not apply to non-UK companies.

94. For non-UK companies subject to income tax, the normal tax rule is that they are charged to income tax at the basic rate under Chapter 2 of Part 2 of ITA on profits of residual business.

95. *Subsection (4)* expands what is treated as profits of residual business for the purposes of corporation tax (and therefore subject to corporation tax at the main rate) to include the non-member percentage of profits which are excluded from the financial statements under clause 14(3). It is based on paragraph 17(2) of Schedule 17 to FA 2006.

96. The source legislation provides that where profits are excluded from the financial statements in accordance with paragraph 31(5) of Schedule 17 to FA 2006, the excluded percentage shall be treated as profits arising from the residual business of G (property rental business). The reference to G (property rental business) is replaced in subsection (4) with a reference to “property rental business of a member of a group”. See Q5 in the Overview commentary and *Change 660* in Annex 1.

97. Subsection (4) also applies to non-UK companies because paragraph 17(2) of Schedule 17 to FA 2006 is not restricted to UK companies. However, since subsection (3) (which charges profits of residual business to tax at the main rate of corporation tax) does not apply to non-UK companies, it is unclear what effect subsection (4) has on non-UK companies.

Q24. We welcome comments on the proposal to apply subsection (4) to non-UK companies.

98. Subsection (4) also applies to joint venture companies (including non-UK joint venture companies). This is because section 138 of FA 2006 provides that regulations can be made for the Part to apply to joint venture companies. Regulations have been made in SI 2006/2866. It is considered that paragraph 17(2) of Schedule 17 to FA 2006 applies to joint venture companies since there is nothing to the contrary in the regulations. This means that where a percentage of profits of property rental business is attributable to a non-member of a joint venture company, it is subject to tax at the main rate of

corporation tax if subsection (3) applies. In this respect, subsection (3) applies to the non-member percentage of property rental business of UK joint venture companies. This is because section 138 of FA 2006 provides that regulations can be made in relation to “property rental business”. It is considered that section 119(2) applies to all UK joint venture companies as there is nothing in SI 2006/2866 disapplying the application of section 119(2). (See regulation 7(5) and 13(1) of SI 2006/2866.)

Q25. We welcome comments on the proposal to apply subsection (3) to the non-member percentage of profits of property rental business carried on by UK joint venture companies and for subsection (4) to joint venture companies.

Clause 16: Gains

99. This clause sets out how gains arising in respect of property rental business and residual business are taxed. It is based on section 124, 127 and 134(1) of, and paragraphs 21 and 32(6) of Schedule 17 to, FA 2006.

100. *Subsections (1) to (3) and (8)* provide that gains made by a company (including a joint venture company) which is, or is a member of, a UK REIT in respect of property rental business (or UK property rental business in the case of a non-UK company) are not chargeable gains. For non-UK companies (including non-UK joint venture companies), gains made in respect of overseas assets are not subject to tax in the UK so there is no need to provide an exemption for non-UK companies in respect of gains on such overseas assets.

101. *Subsections (4), (5) and (8)* provide that where an asset is used partly for the purposes of property rental business (or UK property rental business in the case of a non-UK company), the gain attributable to the property rental business/UK property rental business is not a chargeable gain. These subsections also apply to joint venture companies.

102. *Subsection (6)* (which rewrites section 124(3) of, and paragraphs 21(1) and 32(6)(c) of Schedule 17 to, FA 2006) provides that gains of residual business which are subject to corporation tax are charged at the main corporation tax rate.

103. Section 124(3) of FA 2006 provides that:

Corporation tax shall be charged in respect of gains accruing to C (residual) at a rate determined without reference to section 13 of ICTA (small companies' rate).

104. It is not clear whether section 124(3) was meant to be a charging provision such that *all* gains of residual business are charged to the main rate of corporation tax.

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105. If this provision were to be interpreted as a charging provision it would mean that, when read in conjunction with paragraph 32(6)(c) of Schedule 17 to FA 2006, all United Kingdom gains of residual business accruing to non-UK companies would be subject to corporation tax at the main rate. However, if the non-UK company does not have a permanent establishment in the United Kingdom it is not subject to tax (either corporation tax or capital gains tax) on United Kingdom gains. Only gains relating to United Kingdom assets used for a trade or permanent establishment are subject to corporation tax under section 10B of TCGA.

106. It is unlikely that section 124(3) of FA 2006 is intended to bring into charge United Kingdom gains accruing to non-UK companies (which are not already within the charge by virtue of section 10B of TCGA), gains of residual business are only subject to the main rate of corporation tax where the gain is already subject to corporation tax. This means that, for non-UK companies, only gains of residual business caught by section 10B of TCGA are subject to this provision. See *Change 659* in Annex 1.

Q26. We welcome comments on the proposal that non-UK companies caught by section 10B of TCGA are subject to corporation tax at the main rate and that other non-UK companies are not subject to corporation tax on gains of residual business.

107. Subsection (6) also applies to the non-member percentage of gains arising in respect of property rental business of joint venture companies. This is because section 138 of FA 2006 provides that regulations can be made in relation to “property rental business”. It is considered that section 124(3) applies to all joint venture companies as there is nothing in SI 2006/2866 disapplying section 124(3). (See regulations 7(6), 8, 13(6) and 15 of SI 2006/2866.)

Q27. We welcome comments on the proposal to apply subsection (6) to the non-member percentage of gains accruing to property rental business carried on by joint venture companies.

108. *Subsection (7)* expands what is treated as gains of residual business (and therefore potentially subject to corporation tax at the main rate) to include the non-member percentage of gains which are excluded from the financial statements under clause 14(3). *Subsection (7)* applies to both UK and non-UK companies because paragraph 21(2) of Schedule 17 to FA 2006 is not restricted to UK companies.

109. *Subsection (7)* also applies to joint venture companies (including non-UK joint venture companies). This is because section 138 of FA 2006 provides that regulations can be made for the Part to apply to property rental business carried on by joint venture companies. Regulations have been made in SI 2006/2866. The rewritten legislation is

drafted on the basis that paragraph 21(2) of Schedule 17 to FA 2006 applies to joint venture companies since there is nothing to the contrary in the regulations. This means that where a percentage of gains accruing to property rental business is attributable to a non-member of a joint venture company, it is subject to tax at the main rate of corporation tax if subsection (6) applies.

Q28. We welcome comments on the proposal to apply subsection (7) to joint venture companies.

110. *Subsection (9)* provides that this clause is to be read as if it were contained in TCGA. It is drafted on the same basis as the source legislation (section 127 of FA 2006). It is unclear why this subsection does not also apply to sections 111 and 131 of, and paragraph 34 of Schedule 17 to, FA 2006. Consideration is being given to extending subsection (9) to apply to these provisions.

Q29. We welcome comments on the proposal to apply section 127 of FA 2006 to sections 111 and 131 of, and paragraph 34 of Schedule 17 to, FA 2006.

111. This clause refers to “property rental business” rather than “C (tax exempt)”/“G (property rental business)” (see section 124 of, and paragraph 21 of Schedule 17 to, FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

Chapter 4: Entering the UK REIT regime

Clause 17: Effects of entry: corporation tax

112. This clause provides that, for corporation tax purposes, when a company (including a joint venture company) enters the UK REIT regime its property rental business ceases and recommences and it is deemed to sell and reacquire the assets involved in that business. This clause is based on sections 111(1) to (3), (5) and (7) and 134(1) of, and paragraphs 9, 10 and 33 of Schedule 17 to, FA 2006.

113. *Subsections (1) and (7)* provide that property rental business (or UK property rental business of non-UK companies) carried on before entry to the UK REIT regime is treated as ceasing at entry for the purposes of corporation tax. As clause 3(3) provides that profits of UK property rental business of non-UK companies are treated as liable to corporation tax, this clause applies to all companies whether or not UK resident. See *Change 659* in Annex 1.

Q30. We welcome comments on the proposal to apply subsection (1) to all non-UK companies.

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114. *Subsections (2) to (4) and (7)* provide that, for the purposes of corporation tax, assets involved in property rental business (or UK property rental business of non-UK companies) immediately before entry to the UK REIT regime are treated as being sold and reacquired at market value on entry. Any resulting gain is not chargeable to corporation tax. For non-UK companies, only gains caught by section 10B of TCGA (gains arising in respect of a trade or permanent establishment in the United Kingdom) are caught by this clause. (United Kingdom gains of non-UK companies with no permanent establishment in the United Kingdom are not subject to tax in the UK.) See *Change 659* in Annex 1.

Q31. We welcome comments on the proposal to apply subsections (2) to (4) to gains of non-UK companies arising in respect of a trade or permanent establishment in the UK.

115. In subsection (2) the source legislation refers to the property being acquired by “C (tax-exempt)” (section 111(2) of FA 2006) and “G (property rental business)” (paragraph 9(2) of Schedule 17 to FA 2006). These references are replaced with a reference to the “company so far as it carries on property rental business”. See Q5 in the Overview commentary and *Change 660* in Annex 1.

116. *Subsection (5)* provides that if a percentage of the assets of a member of a group UK REIT is excluded from the financial statements because that percentage is attributable to a non-member, the percentage is ignored for the purposes of subsection (2). The source legislation (paragraphs 9(4) and 10(2) of Schedule 17 to FA 2006) cross-refers to G (property rental business). These references are replaced with a cross-reference to the “group’s property rental business”. See Q5 in the Overview commentary and *Change 660* in Annex 1.

117. *Subsection (6)* provides that, for corporation tax purposes, an accounting period ends and begins again on entry to the regime. As paragraph 32(3) of Schedule 17 to FA 2006 (rewritten in clause 3(3)) provides that the profits of property rental business of non-UK companies are treated as subject to corporation tax, this subsection also applies to non-UK companies for the purposes of corporation tax. See *Change 659* in Annex 1.

Q32. We welcome comments on the proposal to apply subsection (6) to non-UK companies which are treated as liable to corporation tax.

Clause 18: Effects of entry: CAA 2001

118. This clause is supplementary to clause 17 and modifies how CAA operates when a company (including a joint venture company) enters the UK REIT regime. It is based on sections 111(4) and 134(1) of, and paragraphs 9(2), 10(1) and 33 of Schedule 17 to, FA 2006.

119. This clause applies to non-UK companies (including non-UK joint venture companies) which are subject to corporation tax on gains caught by section 10B of TCGA (gains arising in respect of assets involved in a trade or permanent establishment in the UK). See *Change 659* in Annex 1.

Q33. We welcome comments on the proposal to apply this clause to non-UK companies which are liable to corporation tax.

120. *Subsection (4)* provides that anything done by or to the company prior to entry to the UK REIT regime is deemed to have been done by or to the “company so far as it carries on property rental business”. The source legislation refers to things being done by or to “C (tax-exempt)” (section 111(4)(c) of FA 2006) or “G (property rental business)” (paragraph 9(2) of Schedule 17 to FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

Clause 19: Entry charge

121. This clause provides for an amount of notional income (calculated in accordance with clause 20) to be chargeable to tax on each company on entry to the UK REIT regime. It is based on sections 112(1), (2) and (4) and 134(1) of, and paragraphs 11 and 33 of Schedule 17 to, FA 2006.

122. *Subsection (2)* provides that the notional amount is treated as arising in relation to the company’s residual business. This provision ensures that the amount is not treated as arising in respect of the company’s property rental business and therefore subject to clause 15(1) or (2) (ie not chargeable to tax).

123. *Subsection (3)* provides that UK companies (including UK joint venture companies), are chargeable to corporation tax under Schedule D Case VI on the notional amount at the rate mentioned in clause 15(3) (ie at the main rate of corporation tax). The reference to Schedule D Case VI will be replaced with a simple charge to corporation tax as part of the removal of the references to the Schedule D Case VI charges by Bill 5. For UK joint venture companies the legislation is clarified so that such companies are treated in the same way as other UK companies. See *Change 661* in Annex 1.

Q34. We welcome comments on the proposal to treat UK joint venture companies in the same way as other UK companies.

124. *Subsection (4)* provides that non-UK companies (including non-UK joint venture companies), are chargeable to income tax on the notional amount at the basic rate under section 11 of ITA. For non-UK companies the legislation is clarified so that the applicable rate is the basic rate rather than the rate on “the highest part of the company’s income”. See *Change 661* in Annex 1.

Q35. We welcome comments on the proposal that basic rate tax should be chargeable on the notional income for non-UK companies.

125. As subsection (4) is an income tax provision strictly it should be inserted into ITTOIA and a cross-reference inserted from this clause to ITTOIA. However, it is unlikely to be user-friendly to relocate subsection (4) into ITTOIA.

Q36. We welcome comments on the proposal not to insert subsection (4) into ITTOIA.

126. For non-UK companies trading through a permanent establishment in the United Kingdom it may be preferable for the company to pay the entry charge as corporation tax rather than income tax. In the light of this, consideration is being given to drafting the rewritten legislation along these lines. If this were done it would be a change in the law as the source legislation (paragraph 11(1)(d) of Schedule 17 to FA 2006) clearly states that non-UK companies are subject to income tax on the notional income. Such a change would not affect the amount of the entry charge.

Q37. We welcome comments on the proposal the non-UK companies, operating through a permanent establishment in the United Kingdom, are treated in the same way as UK companies for the purposes of the entry charge.

Clause 20: Calculation of notional income

127. This clause sets out how to calculate the amount of notional income for the purposes of clause 19. It is based on sections 112(3) and 134(1) of, and paragraphs 9(4), 10(2) and 11(1) of Schedule 17 to, FA 2006.

128. *Subsection (3)* defines “MV” as the total market value of assets which are involved in property rental business of the company (or UK property rental business in the case of non-UK companies) immediately before entry to the UK REIT regime. The source legislation (section 112(3)(a) of FA 2006) refers to assets being reacquired under section 111(2) of FA 2006 (ie by “C (tax-exempt)” or by “G (property rental business)” (paragraphs 9(2) and 10(4) of Schedule 17 to FA 2006)). See Q5 in the Overview commentary and *Change 660* in Annex 1.

129. *Subsection (4)* provides that if a percentage of the assets is excluded from the financial statements because it is attributable to a non-member, that percentage is ignored for the purposes of “MV”. The source legislation (paragraphs 9(4) and 10(2) of Schedule 17 to FA 2006) cross-refers to “G (property rental business)”. These references are replaced with a cross-reference to the “group’s property rental business”. See Q5 in the Overview commentary and *Change 660* in Annex 1.

130. *Subsection (5)(a)* defines “TR” for UK companies (including UK joint venture companies) as the rate mentioned in clause 15(3) (ie the main rate of corporation tax). For UK joint venture companies the legislation has been clarified so that such companies are treated in the same way as other UK companies. See *Change 661* in Annex 1.

Q38. We welcome comments on the proposal to treat UK joint venture companies in the same way as other UK companies.

131. *Subsection (5)(b)* defines “TR” for non-UK companies (including non-UK joint venture companies) as the basic rate of income tax. For non-UK companies the legislation has been clarified so that the applicable rate is the basic rate rather than the rate on “the highest part of the company’s income”. See *Change 661* in Annex 1.

Q39. We welcome comments on the proposal that “TR” should be defined as basic rate income tax for non-UK companies.

Clause 21: Election to treat notional income as arising in instalments

132. This clause provides that a company (including a joint venture company) may elect to pay the entry charge in instalments. It is based on sections 112(5) to (7) and 134(1) of, and paragraph 11(1) of Schedule 17 to, FA 2006.

133. *Subsection (3)* refers to an “officer of Revenue and Customs” rather than “the Commissioners for Her Majesty’s Revenue and Customs” (see section 112(6)(a) of FA 2006). This is because in practice the notice of election is submitted to an officer, not the Commissioners. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

Chapter 5: Assets etc

Clause 22: Ring-fencing of property rental business

134. This clause provides that, for corporation tax purposes, property rental business (or UK property rental business in the case of non-UK companies) is treated as a separate business from any other business carried on by a group UK REIT or by a company UK REIT. Also, to the extent that the UK REIT carries on property rental business (or UK property rental business in the case of non-UK companies), it is treated as a separate group or company from the rest of the group or company. This clause is based on sections 113(1) to (4) and 134(1) of, and paragraphs 12 and 32(3) of Schedule 17 to, FA 2006.

135. *Subsections (1)* and *(8)* provide that this clause applies to a group UK REIT, each member of the group (including a non-UK company) and a company UK REIT. It is unclear from the source legislation whether section 113(1) to (4) of FA 2006 applies to each non-UK company individually. This is because paragraph 12(2) of Schedule 17 to FA 2006 does not apply to non-UK companies. See *Change 659* in Annex 1.

Q40. We welcome comments on the proposal to apply this clause to non-UK companies.

136. *Subsections (2) to (4)* refer to property rental business of the group or company rather than “C (tax-exempt)” or “G (property rental business)” (section 113 of, and paragraph 12 of Schedule 17 to, FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

137. This clause applies to joint venture companies (including non-UK joint venture companies which are subject to corporation tax), although there is nothing specific in SI 2006/2866 about section 113 of FA 2006. The reason for including joint venture companies is that section 138(1) of FA 2006 provides that “the Treasury may by regulations provide for this Part to apply in relation to property rental business (“the joint venture”) ...” As regulations have been enacted under section 138, it is considered that the Part, including section 113, applies to joint venture companies as there is nothing in SI 2006/2866 to disapply section 113.

Q41. We welcome comments on the proposal to apply this clause to joint venture companies.

138. *Subsection (7)* provides that if a percentage of the profits of property rental business are excluded from the financial statements because they are attributable to a non-member, that percentage is treated as profits of residual business. The source legislation (paragraph 12(3) of Schedule 17 to FA 2006) refers to “G (property rental business)”. This reference is replaced with a cross-reference to the “property rental business of a member of a group”. See Q5 in the Overview commentary and *Change 660* in Annex 1.

Clause 23: Disapplication of certain provisions

139. This clause applies to UK companies and allows losses from overseas property rental business to be used against other property rental business income and disapplies the exemption for small and medium sized enterprises in respect of the transfer pricing rules. It is based on sections 113(5) and (6) and 134(1) of, and paragraph 12(2) of Schedule 17 to, FA 2006.

140. *Subsection (1)* provides that section 392B of ICTA (ring-fencing of losses from overseas property rental business) does not apply to property rental business of a UK company (including a UK joint venture company). It is based on section 113(5) of FA 2006 as modified by paragraph 12(2) of Schedule 17 to FA 2006. Paragraph 12(2) states section 113(5) only applies to UK companies, not non-UK ones. This is because non-UK companies are not subject to United Kingdom tax in respect of overseas property rental business.

141. Subsection (1) applies to UK resident joint venture companies, although there is nothing specific in SI 2006/2866 about section 113(5) of FA 2006. The reason for including joint venture companies is that section 138(1) of FA 2006 provides that “the Treasury may by regulations provide for this Part to apply in relation to property rental business (“the joint venture”) ...” As regulations have been enacted under section 138, it is considered that the Part, including section 113(5), applies to joint venture companies as there is nothing in SI 2006/2866 to disapply section 113(5).

Q42. We welcome comments on the proposal to apply this subsection to UK resident joint venture companies.

142. *Subsection (2)* provides that paragraphs 5B and 5C of Schedule 28AA to ICTA (transfer pricing: exemption for small and medium sized enterprises) do not apply to a UK company. This means that all UK companies regardless of size, which are subject to this Part, are subject to the transfer pricing rules.

143. Subsection (2) applies to UK resident joint venture companies, although there is nothing specific in SI 2006/2866 about section 113(6) of FA 2006. The reason for including joint venture companies is that section 138(1) of FA 2006 provides that “the Treasury may by regulations provide for this Part to apply in relation to property rental business (“the joint venture”) ...” As regulations have been enacted under section 138, it is considered that the Part, including section 113(6) applies to joint venture companies as there is nothing in SI 2006/2866 to disapply section 113(6).

Q43. We welcome comments on the proposal to apply this subsection to UK resident joint venture companies.

144. Subsections (1) and (2) replace the references to “G (property rental business)” and “C (tax-exempt)” (section 113 of, and paragraph 12 of Schedule 17 to, FA 2006) with a single reference to property rental business of the company. See Q5 in the Overview commentary and *Change 660* in Annex 1.

Clause 24: Profit: financing-cost ratio

145. This clause provides that if the result of the sum specified in subsection (2) is less than 1.25, “the excess” calculated in accordance with subsection (3) is charged to corporation tax. It is based on sections 115(1) to (3) and 134(1) of, and paragraph 4 of Schedule 17 to, FA 2006 and regulations 12 and 13 of SI 2006/2864.

146. This clause enacts regulations 12 and 13 of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

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147. The regulation-making power in section 115(1) of FA 2006 is not rewritten as the regulations which have been made under the power are enacted in this Bill. See Q3 in the Overview commentary and *Change 662* in Annex 1.

148. *Subsection (2)* sets out the formula to calculate “the excess” for the purposes of subsection (1). The definitions of “PP” and “PFC” refer to “property profits” and “property financing costs” and are defined further in clause 25.

149. This clause applies to the relevant proportion of a joint venture company’s property profits and property financing costs in the same way as for any other member of a group UK REIT. See *Change 663* in Annex 1.

Q44. We welcome comments on the proposal to treat all joint venture companies in the same way as members of a group UK REIT for the purposes of the financing-cost ratio.

150. *Subsection (3)* provides that the difference between the actual property financing costs of the UK REIT and the amount that would cause the sum specified in subsection (2) to be 1.25 (“the excess”), is charged to corporation tax under Schedule D Case VI. The reference to Schedule D Case VI will be replaced with a simple charge to corporation tax as part of the removal of the references to Schedule D Case VI charges by Bill 5.

151. *Subsections (4)* and *(5)* provide that the excess amount is treated as if it were profits of residual business of the principal company of a group UK REIT or a company UK REIT. This means that the rate of tax is the main rate of corporation tax as mentioned in clause 15(3).

152. Subsection (4) refers to the excess being treated as “*profits* of residual business”, rather than “*income* of C (residual)” (regulation 12(2) of SI 2006/2864) or “*income* of the residual part ...” (regulation 13(2) of SI 2006/2864). This change is made in order to maintain consistency throughout the legislation.

Q45. We welcome comments on the proposal to use “profits” in subsection (4) rather than “income”.

Clause 25: Meaning of “property profits” and “property financing costs”

153. This clause defines “property profits” and “property financing costs” for the purposes of clause 24. It is based on sections 115(2) and (4) and 134(1) of, and paragraph 14 of Schedule 17 to, FA 2006.

154. *Subsections (1) and (3)* define “property profits” and “property financing costs” respectively for the purposes of clause 24. These subsections refer to “property rental business” of the member of the group UK REIT or of the company UK REIT rather than “G (property rental business)” (paragraph 14 of Schedule 17 to FA 2006) or “C (tax-exempt)” (section 115 of FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

Clause 26: Notice to cancel tax advantage

155. This clause provides that an officer of Revenue and Customs can counteract a tax advantage obtained by a company which is, or is a member of, a UK REIT (including a joint venture company) if the officer thinks that the company has tried to obtain a tax advantage. It is based on sections 117(1) to (5) and 134(1) of, and paragraph 15(1) of Schedule 17 to, FA 2006.

156. *Subsections (1), (4) and (6)* refer to “an officer of Revenue and Customs” rather than “the Commissioners for Her Majesty’s Revenue and Customs” (see section 117(1) to (3) and (5) of FA 2006). This is because in practice the notice is given by an officer, not the Commissioners. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

157. *Subsection (3)* sets out how a tax advantage can be counteracted. Subsection (3)(a) provides that an assessment can be made on the company. For non-UK companies, such an assessment may be to income tax or corporation tax.

158. *Subsection (4)* provides that an officer of Revenue and Customs can assess (in addition to the assessment mentioned in subsection (3)(a)) a UK REIT to an *additional* amount of *corporation tax* to cancel out the tax advantage. The subsection is based on section 117(3)(b) of FA 2006.

159. However, if the adjustment under subsection (3) is by way of assessment to income tax, any assessment to corporation tax under subsection (4) is not additional to the assessment under subsection (3). It is therefore proposed either to remove the reference to “additional” from the second line of subsection (4) or to allow for the additional assessment under subsection (4) to be made to either income tax or corporation tax.

<p>Q46. We welcome comments on whether we should remove the word “additional” from the second line of subsection (4), or whether subsection (4) should be extended to allow for an assessment to be made to either income tax or corporation tax.</p>
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160. The reference to Schedule D Case VI in subsection (4) will be replaced with a simple charge to corporation tax as part of the removal of Schedule D Case VI charges by Bill 5.

Clause 27: Appeal against notice under section 26

161. This clause provides that a company which is, or is a member of, a UK REIT (including a joint venture company) may appeal to the Special Commissioners against a notice given under clause 26. It is based on section 117(6) to (8) and 134(1) of, and paragraph 15(2) of Schedule 17 to, FA 2006.

162. *Subsection (2)* refers to “an officer of Revenue and Customs” rather than “the Commissioners for Her Majesty’s Revenue and Customs” (see section 117(7) of FA 2006). This is because in practice the notice of appeal is made to an officer, not the Commissioners. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

Clause 28: Funds awaiting reinvestment

163. This clause provides how cash proceeds from the sale of assets used for property rental business are treated. It is based on sections 118 and 134(1) of, and paragraph 16 of Schedule 17 to, FA 2006.

164. *Subsection (1)* provides that the clause applies where a company which is, or is a member of, a UK REIT disposes of an asset used wholly and exclusively for the purposes of property rental business and holds the proceeds in cash. It is based on section 118(1) of FA 2006 as modified by paragraph 16 of Schedule 17 to FA 2006.

165. For the purposes of a group UK REIT this clause also refers to companies which are members of the group, although paragraph 16 does not specifically mention such members. This is because it is the individual companies which dispose of assets rather than the group.

<p>Q47. We welcome comments on the proposal that this clause applies also to individual members of a group UK REIT.</p>
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166. Subsections (1) and (3)(a) refer to “property rental business” rather than “tax-exempt business” (see section 118(1)(a) of FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

167. A similar point arises in *subsection (5)* which provides that this clause also applies to a reasonable proportion of the proceeds of the disposal of an asset used partly for the purposes of “property rental business of the company”. It refers to “property rental business” rather than “C (tax-exempt)” or “G (property rental business)” (see

section 118(5) of, and paragraph 16 of Schedule 17 to, FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

168. This clause also applies to the worldwide property rental business of non-UK companies (see section 134(1) of FA 2006 which provides that the Part applies to all members of a group unless Schedule 17 to FA 2006 provides the contrary).

Q48. We welcome comments on the proposal that this clause applies to the worldwide property rental business of non-UK companies.

169. This clause also applies to joint venture companies (including non-UK joint venture companies). Section 138 of FA 2006 provides that regulations can be made for the Part to apply to property rental business of joint venture companies. As there is nothing in SI 2006/2866 disapplying or varying the operation of section 118 of FA 2006, this clause is drafted on the basis that section 118 applies to joint venture companies.

Q49. We welcome comments on the proposal that this clause also applies to joint venture companies including non-UK ones.

Chapter 6: Distributions

Clause 29: Distributions: liability to tax

170. This clause provides that distributions made by the principal company of a group UK REIT in respect of profits and gains of the group's property rental business in the United Kingdom are treated as income of a UK property business rather than as dividend income in the hands of the shareholder. This clause also applies to distributions made by a company UK REIT in respect of profits and gains of property rental business. It is based on sections 121(1), (2) and (8) and 134(1) of, and paragraphs 18(1) and (3) and 32(8) of Schedule 17 to, FA 2006.

171. *Subsections (1) and (3)* provide that the section applies to a "distribution in respect of profits and gains". This is consistent with section 121(8)(b) of, and paragraphs 18(1)(b) and 32(8) of Schedule 17 to, FA 2006.

172. It should be noted, however, that the 90% distribution test in section 107(8) of FA 2006 (as modified by paragraphs 6(4) and 32(8) of Schedule 17 to FA 2006) only requires 90% of the *profits* of the property rental business to be distributed. There is no requirement for the 90% distribution test to include gains.

173. Subsections (1) and (3) refer to "property rental business" of the UK REIT rather than to "C (tax exempt)"/"G (property rental business)" (see section 121 of, and paragraph 18(1) of Schedule 17 to, FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

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174. *Subsection (5)* (which is based on section 121(1)(a) of FA 2006) provides that if the shareholder is within the charge to corporation tax, the distribution is treated as profits of a “UK property business (within the meaning of [clause 197[j050102] of Bill 5)”. That clause rewrites section 15(1) of ICTA (Schedule A) and provides that:

A company’s UK property business consists of-

- (a) every business which the company carries on for generating income from land in the United Kingdom, and
- (b) every transaction which the company enters into for that purpose otherwise than in the course of such a business.

175. *Subsection (5)* does not include a reference to gains of a UK property business despite the fact that section 121(8)(b) of FA 2006 says that profits includes gains as research indicates that this was the original intention.

176. Section 121(2)(a) of FA 2006 provides that if the shareholder is a non-resident company within the charge to corporation tax, the distribution “shall be chargeable to tax as profits of Schedule A”. Although section 121(2)(a) is phrased in a subtly different way from section 121(1)(a) (it refers to the distribution being chargeable to tax rather than being treated as profits of a Schedule A business), it does not appear to add anything to section 121(1)(a). Section 121(2)(a) is therefore not rewritten in subsection (5).

<p>Q50. We welcome comments on the proposal not to rewrite section 121(2)(a) of FA 2006.</p>

177. *Subsection (6)* (which is based on section 121(1)(b) of FA 2006) provides that if the shareholder is not within the charge to corporation tax, the distribution is treated as profits of a “UK property business (within the meaning of section 264 of ITTOIA 2005)”.

178. *Subsection (6)* does not include a reference to gains of a UK property business despite the fact that section 121(8)(b) of FA 2006 says that profits includes gains as research indicates that this was the original intention.

179. Section 121(2)(b) of FA 2006 provides that if the shareholder is a non-resident not within the charge to corporation tax, the distribution “shall be chargeable to tax as profits of UK property business (within the meaning of section 264 ITTOIA)”. Although section 121(2)(b) is phrased in a subtly different way from section 121(1)(b), (it refers to the distribution being chargeable to tax rather than being treated as profits of a UK property rental business), it does not appear to add anything to section 121(1)(b). Section 121(2)(b) is therefore not rewritten in subsection (6).

Q51. We welcome comments on the proposal not to rewrite section 121(2)(b) of FA 2006.

180. Subsection (6), refers to a shareholder “not within the charge to corporation tax” rather than to “a shareholder within the charge to income tax”. This makes it clear that all shareholders (including non-resident shareholders) are caught, either by subsection (5) or by subsection (6).

Q52. We welcome comments on the proposal to refer to a shareholder “not within the charge to corporation tax”.

181. In order to retain the corporation tax/income tax split of the legislation, subsection (5) should strictly be placed in Bill 5 and subsection (6) in Chapter 3 Part 3 of ITTOIA. However moving these provisions out of this Part would not be obviously helpful to users.

Q53. We welcome comments on the proposal to keep subsections (5) and (6) in clause 29.

182. *Subsection (7)* provides that in the case of a non-UK resident shareholder, a distribution is not subject to a duty to deduct at source in accordance with regulations made under section 971 of ITA. Consideration has been given as to whether this subsection should be rewritten in section 971 or 972 of ITA. However it is unlikely to be helpful to users to remove subsection (7) from this clause. It is therefore proposed that subsection (7) remain in this clause and section 972(6) of ITA is amended so that it refers to this subsection.

Q54. We welcome comments on the proposal to amend section 972(6) of ITA so that it refers to clause 29(7).

183. Subsection (7) is based on section 121(2)(c) of FA 2006. Section 121(2)(c) could be taken to apply to *all distributions* rather than just those relating to profits and gains of property rental business. It is likely that section 121(2) should not apply to all distributions. So subsection (7) only applies to distributions caught by this clause.

Q55. We welcome comments on the proposal that subsection (7) should refer only to distributions in respect of profits and gains of property rental business.

184. *Subsection (8)* provides a cross-reference to the deduction provisions in sections 973 and 974 of ITA.

Clause 30: Distributions: further provision

185. This clause makes further provision in respect of clause 29. It is based on sections 121(3) to (7) and 134(1) of, and paragraphs 18(1) and (2) and 32(8) of Schedule 17 to, FA 2006.

186. *Subsection (1)* provides that clause 29 does not apply to certain types of shareholders. Subsection (1)(d)(i) refers to a “premiums trust fund” within the meaning of section 222 of FA 1994 (see section 121(3)(d)(i) of FA 2006). However, there is no definition of premiums trust fund in section 230(1) of FA 1994, only a definition of “premium trust fund”. Consideration is being given to whether subsection (1)(d)(i) should refer to premium trust fund.

Q56. We welcome comments on the proposal to refer to “premium trust fund” in subsection (1)(d)(i).

187. *Subsection (3)* (together with *subsection (4)*) provides that sections 231 of ICTA and 397 of ITTOIA (tax credits in respect of qualifying distributions) do not apply to distributions made by the principal company of a group UK REIT or by a company UK REIT in respect of profits and *gains* of property rental business. It is based on section 121(5) of FA 2006.

188. However, on a strict reading of section 121(5) of FA 2006, subsection (4) (for the purposes of subsection (3)) should only refer to distributions in respect of “profits”. This is because section 121(8)(b) of FA 2006 only applies to section 121(1) of FA 2006. It does not apply to section 121(5).

Q57. We welcome comments on the proposal that subsection (3) applies to gains (as well as profits) of property rental business.

189. For the purposes of subsection (3), subsection (4) defines “relevant distribution” by reference to “property rental business” rather than “C (tax-exempt)”. See Q5 in the Overview commentary and *Change 660* in Annex 1.

190. For the purposes of a distribution made by a principal company of a group UK REIT, it is assumed that the reference to “C (tax-exempt)” in section 121(5) should have been modified by paragraph 18 of Schedule 17 to FA 2006 to refer to “G (property rental business)”.

191. *Subsection (5)* (based on section 121(6) of FA 2006) provides that relevant distributions (as defined in subsection (4)) are treated as profits of a single business separate from the businesses mentioned in *subsection (6)*. Subsection (6)(a) and (c) refer to “UK property business (within the meaning of [clause 197[j050102] of Bill 5])” and

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“overseas property business (within the meaning of [clause 198[j050113] Bill 5])” respectively. [Clause 197[j050102]] rewrites section 15(1) of ICTA (Schedule A) and provides that:

A company’s UK property business consists of-

(a) every business which the company carries on for generating income from land in the United Kingdom, and

(b) every transaction which the company enters into for that purpose otherwise than in the course of such a business.

192. [Clause 198[j050113] rewrites section 70A(4) of ICTA (overseas property business) and provides that:

A company’s overseas property business consists of-

(a) every business which the company carries on for generating income from land outside the United Kingdom, and

(b) every transaction which the company enters into for that purpose otherwise than in the course of such a business.

Clause 31: Dividends representing profits of UK property rental business

193. This clause provides that if a non-UK company pays a dividend in respect of profits of its UK property rental business to a United Kingdom member of the UK REIT group, that dividend is treated as being made by a UK company. This clause is based on paragraph 32(7) of Schedule 17 to FA 2006.

194. This clause only deals with distributions in respect of *profits* of UK property rental business. It does not deal with distributions in respect of *gains* of UK property rental business. Consideration is being give to applying this clause to gains as well as profits of UK property rental business.

<p>Q58. We welcome comments on the proposal to apply this clause to profits and gains of UK property rental business.</p>
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Clause 32: Attribution of distributions

195. This clause sets out how distributions are attributed between the property rental business of a UK REIT and any other business. It is based on sections 123 and 134(1) of, and paragraph 20 of Schedule 17 to, FA 2006.

196. Subsection (3) refers to “property rental business” of a member of the group or of a company rather than to “G (property rental business)” (paragraph 20(b) of Schedule 17

to FA 2006) or “C (tax-exempt)” (section 123(d) of FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

Clause 33: Tax consequences of distribution to holder of excessive rights

197. This clause sets out the tax consequences of a distribution made to a “holder of excessive rights” (defined in clause 35) where the distributing company has not taken steps to prevent it. It is based on section 114 of, and paragraph 13 of Schedule 17 to, FA 2006 and regulations 1(3) and 10(1), 10(3) to 10(5) of SI 2006/2864.

198. This clause is based on regulation 10 of SI 2006/2864 which is to be enacted in this clause and revoked. See Q3 in the Overview commentary and *Change 662* in Annex 1.

199. *Subsections (1) to (3)* provide that when a distribution is made to a holder of excessive rights and the distributing company has not taken reasonable steps to prevent its being made, the distributing company is treated as receiving an amount of income calculated in accordance with clause 34.

200. *Subsections (4) to (6)* provide that the amount is charged to corporation tax under Schedule D Case VI as if it were profits of residual business of the distributing company. Accordingly the rate of tax is the main rate of corporation tax, as residual profits are charged without reference to the small companies’ rate in section 13 of ICTA (see clause 15(3)). The reference to Schedule D Case VI will be replaced with a simple charge to corporation tax as part of the removal of reference to Schedule D Case VI charges by Bill 5.

Clause 34: “The section 34 amount”

201. This clause sets out how the “section 34 amount” is calculated for the purposes of clause 33. It is based on section 114(2) of, and paragraphs 2 and 13 of Schedule 17 to, FA 2006 and regulations 1(2) and 10(1) and 10(2) of SI 2006/2864.

202. This clause is based on regulation 10 of SI 2006/2864 which is to be enacted in this clause and revoked. See Q3 in the Overview commentary and *Change 662* in Annex 1.

203. *Subsections (2) and (3)* define “DO” (distribution in respect of ordinary shares) and “DP” (distribution in respect of preference shares) for a group UK REIT by reference to the group’s “UK profits” (as defined in clause 11(2)) rather than by reference to “profits of C (tax-exempt)” (regulation 10(2) SI 2006/2864). For a company UK REIT, “DO” and “DP” are defined by reference to the “profits of property rental business of the company” rather than “profits of C (tax-exempt)”. See Q5 in the Overview commentary and *Change 660* in Annex 1.

Clause 35: Meaning of “holder of excessive rights”

204. This clause defines “holder of excessive rights”. It is based on section 114(1) and 134(1) of, and paragraph 13 of Schedule 17 to, FA 2006 and regulation 1(2) of SI 2006/2864.

205. This clause is, to a large extent, based on regulation 1(2) of SI 2006/2864 which is to be enacted and revoked. See Q3 in the Overview commentary and *Change 662* in Annex 1.

Clause 36: Regulations: distributions to holders of excessive rights

206. This clause allows the Treasury to make regulations dealing with distributions made to holders of excessive rights. It is based on section 114 of, and paragraph 13 of Schedule 17 to, FA 2006.

207. The clause does not reproduce the general regulation making power in sections 114(1) nor the specific power in section 114(2)(a) of FA 2006. See *Change 664* in Annex 1.

Q59. We welcome comments on the proposal to provide a restricted regulation-making power as set out in clause 36 and also to relocate regulation 11 of SI 2006/2864 into SI 2006/2867.

Chapter 7: Gains etc

Clause 37: Movement of assets out of ring-fence

208. This clause sets out how gains made on of the disposal of an asset used in property rental business (or UK property rental business of non-UK companies) are treated. It also makes provision for repayment of a proportion of the entry charge in certain circumstances. It is based on sections 125(1) to (3) and (5) to (8) and 134(1) of, and paragraphs 21, 22 and 32(6) of Schedule 17 to, FA 2006.

209. *Subsections (1) to (3) and (9)* provide that where an asset which has been used wholly and exclusively for the purposes of property rental business (or UK property rental business in the case of non-UK companies) begins to be used for the purposes of residual business, the asset is deemed to be sold by the company in so far as it carries on property rental business (or UK property rental business if the company is a non-UK company) and reacquired at market value by the company in so far as it carries on residual business at market value. In accordance with clause 16(1) any resulting gain is not a chargeable gain.

210. *Subsections (4) to (6) and (9)* provide that where an asset which has been used wholly and exclusively for the purposes of the property rental business (or UK property rental business in the case of non-UK companies) is disposed of in the course of a trade,

the deemed disposal and reacquisition under clause 17(2) is ignored. Instead the asset is treated as disposed of in the course of the company's residual business. In accordance with clause 16(6) any resulting gain which is subject to corporation tax it is taxed at the main rate of corporation tax.

211. Subsections (1), (2) and (4) refer to property rental business of a company rather than to "C (tax-exempt)" (see section 125 of FA 2006) or "G (property rental business)" (see paragraph 21(1) of Schedule 17 to FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

212. *Subsection (8)* provides that if a percentage of the gains of property rental business is excluded from the financial statements because the gains are attributable to a non-member, that percentage of the gains is treated as gains of residual business. The source legislation (paragraph 21(2) of Schedule 17 to FA 2006) refers to "G (property rental business)". This reference is replaced with a cross-reference to the "group's property rental business". See Q5 in the Overview commentary and *Change 660* in Annex 1.

213. This clause also applies to joint venture companies, including non-UK resident joint venture companies (regulations 7(6), 8, 13(7) and 15 of SI 2006/2866).

Clause 38: Movement of assets out of ring-fence: CAA 2001

214. This clause provides that any sale and reacquisition under clause 37(2) is automatically at tax written down value for the purposes of CAA. It is based on section 125(4) and 134(1) of, and paragraphs 21(1) and 32(6) of Schedule 17 to, FA 2006.

215. This clause refers to the company so far as it carries on property rental business rather than to "C (tax-exempt)" (see section 125 of FA 2006) or to "G (property rental business)" (see paragraph 21(1) of Schedule 17 to FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

216. This clause also applies to joint venture companies, including non-UK resident joint venture companies (regulations 7(6), 8, 13(7) and 15 SI 2006/2866).

Clause 39: Movement of assets into ring-fence

217. This clause provides that if an asset used by the residual business of a company (including a non-UK company) begins to be used by the company for the purposes of property rental business (or UK property rental business, in the case of a non-UK company), it is treated as disposed of and reacquired at market value. It also provides that, for the purposes of CAA, the transfer of the asset is treated as made at the tax

written-down value. It is based on sections 126 and 134(1) of, and paragraphs 21 and 32(6) of Schedule 17 to, FA 2006.

218. In accordance with clause 16(6), if a gain arises under this clause and the gain is subject to corporation tax, it is charged at the main rate.

219. The wording of subsection (2) is aligned with that of clause 37(2) by including the words “at that time” at the end of the first line of subsection (2).

Q60. We welcome comments on the alignment of subsection (2) with clause 37(2).

220. Subsections (1) and (2) refer to “the company so far as it carries on property rental business” rather than to “C (tax-exempt)” (see section 126 of FA 2006) or to “G (property rental business)” (see paragraph 21(1) of Schedule 17 to FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

221. *Subsection (5)* provides that if a percentage of the gains of property rental business is excluded from the financial statements because that percentage of the gains is attributable to a non-member, those gains are treated as gains of a residual business. The source legislation (paragraph 21(2) of Schedule 17 to FA 2006) refers to “G (property rental business)”. This reference is replaced with a cross-reference to the “group’s property rental business”. See Q5 in the Overview commentary and *Change 660* in Annex 1.

222. This clause also applies to joint venture companies, including non-UK resident joint venture companies (regulations 7(6), 8, 13(7) and 15 SI 2006/2866).

Clause 40: Demergers: disposal of assets

223. This clause makes provision for a company UK REIT to dispose of an asset to a 75% subsidiary which subsequently becomes a member of a group UK REIT. It is based on section 126A of FA 2006.

224. In this clause reference is made to “property rental business” rather than “C (tax-exempt)”. See Q5 in the Overview commentary and *Change 660* in Annex 1.

Clause 41: Demergers: company leaving group UK REIT

225. This clause makes provision for a company to cease to be a member of a group UK REIT but to continue within the UK REIT regime. It is based on paragraph 34 of Schedule 17 to FA 2006.

Clause 42: Interpretation of Chapter

226. This clause provides that the Chapter (apart from clause 41) is to be read as if it were contained in TCGA. It is based on sections 127 of FA 2006.

227. It is unclear why the source legislation does not also refer to section 111 of FA 2006 (clause 17 effects of entry), paragraph 34 of Schedule 17 to FA 2006 (clause 41 demergers) and section 131 of FA 2006 (clause 62 effects of cessation). Consideration is being given to applying clause 42 to clauses 17, 41 and 62 .

Q61. We welcome comments on the proposal to apply clause 42 to clauses 17, 41 and 62.

Chapter 8: Breach of conditions in Chapter 2

Clause 43: Breach of relevant Chapter 2 conditions

228. This clause provides that where certain conditions in Chapter 2 are not met, the Treasury may make regulations about the application of the Part. It is based on sections 116(1) and (3) to (4) and 134(1) of, and paragraph 4 of Schedule 17 to, FA 2006.

229. The following regulations have been made under section 116 of FA 2006:

- Regulation 1 of SI 2006/2864 (general);
- Regulation 2 of SI 2006/2864 (breach of conditions for company – take-overs and demergers);
- Regulation 3 of SI 2006/2864 (breach of conditions for company – actions of others);
- Regulation 4 of SI 2006/2864 (breach of conditions for company – other);
- Regulation 5 of SI 2006/2864 (breach of requirements as to properties);
- Regulation 6 of SI 2006/2864 (breach of distribution condition);
- Regulation 7 of SI 2006/2864 (inserted by SI 2007/3540) (initial breach of Condition 2 in section 108(3) – balance of business condition);
- Regulation 7A of SI 2006/2864 (inserted by SI 2007/3540) (tax charge for specified accounting period – balance of business condition);
- Regulation 7B of SI 2006/2864 (inserted by SI 2007/3540) (breach of balance of business conditions);

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- Regulation 8 of SI 2006/2864 (amended by regulation 6 of SI 2007/3540) (multiple breaches of separate conditions); and
- Regulation 9 of SI 2006/2864 (breach of condition – information requirements).

230. As is proposed to enact these regulations (and also SI 2006/2866 and SI 2007/3425 dealing with joint venture companies) and consideration is being given to the need for the regulation-making power in section 116.

Clause 44: UK REIT to give notice of breach of relevant Chapter 2 condition

231. This clause provides that where certain conditions in Chapter 2 are not met, the principal company of a group UK REIT or a company UK REIT must notify an officer of Revenue and Customs of the breach. It is based on sections 116(1) and (2) and 134(1) of FA 2006 and regulation 9 of SI 2006/2864.

232. *Subsections (1) and (2)* refer to an “officer of Revenue and Customs” rather than to the “Commissioners for Her Majesty’s Revenue and Customs”. This is because in practice it will be the officer who is notified of the breach of the Part. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

233. *Subsection (4)* enacts the information requirements provided in regulation 9 of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

Clause 45: Breach of certain conditions for company

234. This clause makes provision about breaches of conditions C or D in clause 9. It is based on sections 116(1) and (3) and 134(1) of, and paragraph 4 of Schedule 17 to, FA 2006 and regulations 1(3) and 2 to 4 of SI 2006/2864.

235. This clause enacts regulations 1 to 4 of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

236. *Subsection (2)* provides that if a principal company of a group UK REIT or a company UK REIT becomes a member of a pre-existing group UK REIT, and by doing so fails to satisfy condition C (shares are listed) and condition D (not a close company) in clause 9, the breaches are ignored. It is based on regulation 2 of SI 2006/2864.

237. This means that subsection (2) applies when a UK REIT is taken over by a group UK REIT. However, if this is correct, it is difficult to see why subsection (2) is needed. If a UK REIT is taken over by a group UK REIT it is automatically treated as a member of the take-over group. Therefore it will no longer need to satisfy conditions C and D in clause 9 as these conditions only have to be satisfied by the principal company of the take-over group.

238. It is unlikely that regulation 2 of SI 2006/2864 intended to deal with the situation where a UK REIT takes over another UK REIT and, as a consequence, becomes the principal company of a group. In particular, for a company UK REIT, this would require a new group notice under section 109 of FA 2006 to be given.

239. Subsection (2) does not apply to demerger situations (ie when a member of a group UK REIT is taken over by another UK REIT). This is because regulation 1(3) of SI 2006/2864 modifies regulation 2 of SI 2006/2864 for the purposes of groups so that regulation 2 only applies to the principal company of a group UK REIT or to a company UK REIT.

240. In the light of these points, consideration is being given as to whether subsection (2) is needed. A similar point also arises in respect of regulation 8(3)(a) of SI 2006/2864 which is rewritten in clause 60(7)(a).

241. As indicated in clause 52, this clause is subject to clause 55 which allows an officer of Revenue and Customs to issue a notice of termination of the UK REIT regime if the company has relied on a provision mentioned in clause 60(5)(a) more than four times in a ten year period.

Clause 46: Breach of condition as to property rental business

242. This clause provides that conditions A or B of clause 10 can be breached without causing the UK REIT regime to terminate. It is based on section 116(1) and (3) of FA 2006 and regulations 1(3) and 5(1) and (2) of SI 2006/2864.

243. This clause enacts regulation 5(1) and (2) of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

244. As indicated in clause 52, this clause is subject to clause 55, which allows an officer of Revenue and Customs to issue a notice of termination of the UK REIT regime if clause 57 (serious breach), clause 58 (more than two breaches of property rental conditions) or clause 60 (more than four breaches of certain Chapter 2 conditions) applies.

Clause 47: Breach of condition as to distribution of profits

245. This clause sets out how the distribution condition in clause 11 can be breached without causing the UK REIT regime to terminate. It is based on section 116(1) and (3) of FA 2006 and regulations 1(3) and 6(1) to (3) and (5) to (8) of SI 2006/2864.

246. This clause enacts regulation 6(1) to (3) and (5) to (8) of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

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247. *Subsection (2)* provides that the breach is ignored if the company does not meet the distribution condition in clause 11, but an amount calculated under clause 48 is charged to corporation tax. The amount is charged to corporation tax under Schedule D Case VI as if it were profits of residual business of the distributing company. Accordingly the rate of tax is the main rate of corporation tax as residual profits are charged without reference to the small companies' rate in section 13 of ICTA (see clause 15(3)). The reference to Schedule D Case VI will be replaced with a simple charge to corporation tax in line with the removal of references to Schedule D Case VI charges by Bill 5.

248. As indicated in clause 52, this clause is subject to clause 55 which allow an officer of Revenue and Customs to issue a notice of termination of the UK REIT regime if clause 57 (serious breach) or clause 60 (more than four breaches of certain Chapter 2 conditions) applies.

Clause 48: “The section 48 amount”

249. This clause sets out how to calculate “the section 48 amount” for the purposes of clause 47. It is based on section 116(1) and (3) of FA 2006 and regulations 1(3) and 6(4) of SI 2006/2864.

250. This clause enacts regulation 6(4) of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

251. This clause provides that an “officer of Revenue and Customs” rather than “the Commissioners” can specify a later date in order to calculate “D”, the gross amount of profits distributed. This is because in practice it is an officer, not the Commissioners, who specifies a later date. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

Clause 49: Initial breach of condition B in section 12

252. This clause sets out how condition B in clause 12 (balance of business: assets involved in property rental business) can be breached in the first accounting period of a UK REIT without causing the UK REIT regime to terminate. It is based on section 116(1) and (3) of FA 2006 and regulations 1(3), 7(1) and (2) and 7A(1) to (3) and (8) of SI 2006/2864.

253. This clause enacts regulations 7(1) and (2) and 7A(1) to (3) and (8) of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

254. This clause provides that if the balance of business assets test in clause 12(5) is not met in the first accounting period, the breach is ignored, but an amount calculated in accordance with clause 50 is charged to corporation tax. The amount is charged to corporation tax under Schedule D Case VI as if it were profits of residual business of the

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principal company of the group UK REIT or company UK REIT. Accordingly the rate of tax is the main rate of corporation tax as profits of residual business are charged without reference to the small companies' rate in section 13 of ICTA (see clause 15(3)). The reference to Schedule D Case VI will be replaced with a simple charge to corporation tax as part of the removal of references to Schedule D Case VI charges.

255. The clause does not rewrite regulation 7(3) of SI 2006/2864 because it is considered unnecessary. Regulation 7(3) provides that if a breach of the balance of business assets test is ignored in the initial accounting period, it is also ignored for the purposes of regulation 7B(4) and (5) of SI 2006/2864. However, since regulation 7B(6) of SI 2006/2864 provides that the first accounting period is not to be taken into account for the purposes of regulation 7B(4) and (5), it is clear that breaches caught by regulation 7 (in the initial accounting period) are not taken into account for the purposes of regulation 7B. Consequently, regulation 7(3) is not necessary.

<p>Q62. We welcome comments on the proposal not to rewrite regulation 7(3) of SI 2006/2864.</p>
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256. As indicated in clause 52, this clause is subject to clause 55 which allows an officer of Revenue and Customs to issue a notice of termination of the UK REIT regime if clause 57 (serious breach), clause 59 (more than two breaches of balance of business conditions) or clause 60 (more than four breaches of certain Chapter 2 conditions) applies.

Clause 50: Meaning of “the notional amount”

257. This clause sets out how to calculate “the notional amount” for the purposes of clause 49. It is based on section 116(1) and (3) of FA 2006 and regulation 7A(4) to (7) of SI 2006/2864.

258. This clause enacts regulation 7A(4) to (7) of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

259. *Subsection (3)* refers to property rental business of the company rather than to “C (tax-exempt)”/“G (property rental business)” (see regulation 7A(5) of SI 2006/2864). See Q5 in the Overview commentary and *Change 660* in Annex 1.

260. The definition of “TMV” in subsection (3) is based on regulation 7A(5) of SI 2006/2864. Regulation 7A(5) provides that this is the aggregate market value of assets involved in the UK property rental business of “C (tax-exempt)” or “G (property rental business)”. However, there is no exclusion for assets attributable to any percentage of the assets held by a non-member of the group, as in clause 20(4). Consideration is being given to providing such an exclusion.

Q63. We welcome comments on the proposal to exclude the non-member percentage of assets from the definition of “TMV”.

261. The definitions of “TMV” (subsection (3)) and “entry charge notional income” (subsection (7)) include, respectively, the relevant proportion of assets and notional income attributable to a joint venture company (see regulation 7A(5)(c) of SI 2006/2864). See clause 69(2) which provides that references to a group UK REIT include references to a deemed UK REIT (defined in clause 68) and clause 69(4) which provide that, for the purposes of a group UK REIT, references to a member of a group include references to a joint venture company. It is proposed to include regulation 7A(5)(d) of SI 2006/2864 (joint venture groups) in due course.

Clause 51: Breaches of balance of business conditions after initial period

262. This clause provides how the balance of business conditions in clause 12 can be breached in the accounting periods following the first accounting period of the UK REIT without causing the UK REIT regime to terminate. It is based on section 116(1) and (3) of FA 2006 and regulations 1(3) and 7B(1) to (3) of SI 2006/2864.

263. This clause enacts regulation 7B(1) to (3) of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

264. In this clause reference is made to “property rental business” rather than “tax-exempt business” (see regulation 7B(2) and (3) of SI 2006/2864). See Q5 in the Overview commentary and *Change 660* in Annex 1.

265. As indicated in clause 52, this clause is subject to clause 55 which allows an officer of Revenue and Customs to issue a notice of termination of the UK REIT regime if clause 57 (serious breach), clause 59 (more than two breaches of balance of business conditions) or clause 60 (more than four breaches of certain Chapter 2 conditions) applies.

Clause 52: Chapter subject to section 55

266. This clause provides that this Chapter is subject to clause 55 (termination of UK REIT regime by officer of Revenue and Customs). It is based on section 116(4) of FA 2006.

Chapter 9: Leaving the UK REIT regime

Clause 53: Overview of Chapter

267. This clause provides an overview of the Chapter. It is new.

Clause 54: Termination by notice: group or company

268. This clause provides that the principal company of a group UK REIT or a company UK REIT can give notice to an officer of Revenue and Customs for the UK REIT regime to cease in respect of the group or company. It is based on sections 128 and 134(1) of, and paragraph 23 of Schedule 17 to, FA 2006.

269. *Subsection (3)* requires the notice to be given to an “officer of Revenue and Customs” rather than “the Commissioners of Her Majesty’s Revenue and Customs” (see section 128(2) of FA 2006). This is because in practice the notice of termination is given to an officer, not the Commissioners. *Subsection (4)* requires that the date on the notice must be after the date the “officer” receives the notice. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

Clause 55: Termination by notice: officer of Revenue and Customs

270. This clause provides that, in certain circumstances, an officer of Revenue and Customs can give a notice to the principal company of a group UK REIT or a company UK REIT that the group or company will cease to be within the UK REIT regime. It also provides a right of appeal to the Special Commissioners. It is based on sections 129 and 134(1) of, and paragraphs 23 and 24 of Schedule 17 to, FA 2006.

271. *Subsections (1), (2) and (4)* require the notice to be given by an “officer of Revenue and Customs” rather than “the Commissioners for Her Majesty’s Revenue and Customs” (see section 129(1), (2) and (5) of FA 2006). This is because in practice the notice of termination is given by an officer, not the Commissioners. *Subsection (5)* provides that an appeal can be made by the UK REIT by giving notice in writing to an “officer of Revenue of Customs” rather than “the Commissioners for Her Majesty’s Revenue and Customs” (see section 129(7) of FA 2006). Again, this is because the notice is given to an officer, not the Commissioners. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

Clause 56: Notice under section 55: tax advantage

272. This clause provides that if, during a ten year period, two notices have been given under clause 26 (cancellation of tax advantage), an officer of Revenue and Customs may give a notice under clause 55 terminating the UK REIT regime. It is based on sections 129(2) and 134(1) of FA 2006 and regulation 14 of SI 2006/2864.

273. *Subsection (1)* requires the notice to be given by an “officer of Revenue and Customs” rather than “the Commissioners for Her Majesty’s Revenue and Customs” (see section 129(2) of FA 2006). This is because in practice the notice of termination is given by an officer, not the Commissioners. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

274. *Subsections (2) to (4)* enact regulation 14 of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

Clause 57: Notice under section 55: serious breach

275. This clause provides that if an officer of Revenue and Customs thinks a breach of a condition in clauses 10 to 12 is so serious that the UK REIT regime should be terminated, the officer can issue a notice under clause 55 terminating the regime. It is based on sections 116(1) and (3), 129(2) and 134(1) of FA 2006 and regulations 1(3) and 7(4) and (5) of SI 2006/2864.

276. *Subsection (1)* requires the notice to be given by an “officer of Revenue and Customs” rather than “the Commissioners for Her Majesty’s Revenue and Customs” (see section 129(2) of FA 2006). This is because in practice the notice of termination is given by an officer, not the Commissioners. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

277. *Subsections (2) and (3)* enact regulation 7(4) and (5) of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

Clause 58: Notice under section 55: breach of conditions as to property rental business

278. This clause provides the circumstances when an officer of Revenue and Customs may issue a notice under clause 55 to terminate the UK REIT if there has been a breach of either condition A or B in clause 10. It is based on sections 116(1) and (3), 129(2) and 134(1) of FA 2006 and regulations 1(3) and 5(2) to (5) of SI 2006/2864.

279. *Subsection (1)* requires the notice to be given by an “officer of Revenue and Customs” rather than “the Commissioners for Her Majesty’s Revenue and Customs” (see section 129(2) of FA 2006). This is because in practice the notice of termination is given by an officer, not the Commissioners. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

280. This clause enacts regulation 5(2) to (5) of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

Clause 59: Notice under section 55: breach of conditions as to balance of business

281. This clause provides the circumstances when an officer of Revenue and Customs may issue a notice under clause 55 to terminate the UK REIT if there has been a breach of either condition A or B in clause 12. It is based on sections 116(1) and (3), 129(2) and 134(1) of FA 2006 and regulations 1(3) and 7B(4) to (7) of SI 2006/2864.

282. *Subsection (1)* requires the notice to be given by an “officer of Revenue and Customs” rather than “the Commissioners for Her Majesty’s Revenue and Customs” (see section 129(2) of FA 2006). This is because in practice the notice of termination will be given by an officer, not the Commissioners. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

283. This clause enacts regulation 7B(4) to (7) of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

Clause 60: Notice under section 55: multiple breaches of conditions in Chapter 2

284. This clause provides that if there are multiple breaches of certain Chapter 2 conditions, an officer may issue a notice under clause 55 to terminate the UK REIT. It is based on sections 129(2) and (3) and 134(1) of FA 2006 and regulations 1(3) and 8 of SI 2006/2864.

285. *Subsection (1)* requires the notice to be given by an “officer of Revenue and Customs” rather than “the Commissioners for Her Majesty’s Revenue and Customs” (see section 129(2) of FA 2006). This is because in practice the notice of termination will be made by an officer, not the Commissioners. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

286. This clause enacts regulation 8 of SI 2006/2864. See Q3 in the Overview commentary and *Change 662* in Annex 1.

287. *Subsection (7)(a)* provides that if a member of a group UK REIT or a company UK REIT becomes a member of a pre-existing group UK REIT, and by doing so fails to satisfy condition C (shares are listed) and condition D (not a close company) in clause 9, the breaches are ignored. It is based on regulation 8(3)(a) of SI 2006/2864.

288. This means that subsection (7)(a) applies when a member of a group UK REIT or a company UK REIT is taken over by another group UK REIT. However, if this is correct, it is difficult to see why subsection (7)(a) is needed. If a member of a group UK REIT or a company UK REIT is taken over by another group UK REIT it is automatically treated as a member of the take-over group. Therefore it will no longer need to satisfy conditions C and D in clause 9 as these conditions only have to be satisfied by the principal company of the take-over group.

289. It is unlikely that regulation 8(3)(a) of SI 2006/2864 deals with the situation where a UK REIT takes over another UK REIT and, as a consequence, becomes the principal company of a group. In particular, for a company UK REIT, this would require a new group notice under section 109 of FA 2006 to be made.

290. In the light of these points, consideration is being given as to the need for subsection (7)(a). A similar point also arises in respect of regulation 2 of SI 2006/2864 rewritten in clause 45(2).

Clause 61: Automatic termination for breach of certain conditions in section 9

291. This clause provides that the UK REIT regime automatically terminates if any of conditions A, B, E or F in clause 9 is breached and that the company which gave notice under clause 5 must notify an officer of Revenue and Customs of the breach. The clause is based on sections 130 and 134(1) of, and paragraphs 4 and 23 of Schedule 17 to, FA 2006.

292. *Subsection (3)* requires the notice to be given to an “officer of Revenue and Customs” rather than “the Commissioners for Her Majesty’s Revenue and Customs” (see section 130(2) of FA 2006). This is because in practice the notice of termination will be given to an officer, not the Commissioners. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

Clause 62: Effects of cessation

293. This clause sets out what happens, for corporation tax purposes, when a group UK REIT, a member of a group UK REIT (including a joint venture company) or a company UK REIT ceases to be within the UK REIT regime. It is based on sections 131(1) to (3) and (5) and 134(1) of, and paragraphs 25, 26 and 33 of Schedule 17 to, FA 2006.

294. This clause also applies to non-UK companies (including non-UK joint venture companies). See *Change 659* in Annex 1.

<p>Q64. We welcome comments on the proposal to apply this clause to non-UK companies.</p>
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295. *Subsections (2)* and *(7)* provide that property rental business (or UK property rental business in the case of a non-UK company) of an exiting company is treated for corporation tax purposes as ceasing immediately before cessation of the UK REIT regime.

296. *Subsections (2)* and *(3)* refer to “property rental business of an exiting company” rather than “C (tax-exempt)” (see section 131(1) of FA 2006) or “G (property rental business)” (see paragraph 25(1) of Schedule 17 to FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

297. *Subsections (3)* and *(7)* provide that assets “involved” in the property rental business (or UK property rental business in the case of a non-UK company) immediately before cessation are treated as being sold immediately before cessation by the company

so far as it carries on property rental business and reacquired immediately afterwards. See clause 82(3) for the definition of an asset “involved” in property rental business.

Clause 63: Effects of cessation: CAA 2001

298. This clause is supplementary to clause 62 and modifies how CAA operates when a company (including a joint venture company) ceases to be in the UK REIT regime. It is based on sections 131(4) and 134(1) of, and paragraphs 25(1), 26(1) and 33 of Schedule 17 to, FA 2006.

299. This clause applies to non-UK companies (including non-UK joint venture companies). See Q64 in the commentary on clause 62 and *Change 659* in Annex 1.

300. *Subsection (5)* refers to anything done prior to cessation by or to “the company so far as it carries on property rental business”. The source legislation refers to things being done by or to “C (tax-exempt)” (see section 131(4)(c) of FA 2006) or “G (property rental business)” (see paragraph 25(1) of Schedule 17 to FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

Clause 64: Early exit by notice

301. This clause provides what happens, for the purposes of corporation tax, when a UK REIT or a member of a group UK REIT (including a joint venture company), which was within the UK REIT regime for less than ten years, disposes of an asset within two years of giving notice to leave the UK REIT regime. It is based on sections 132 and 134(1) of, and paragraphs 4, 27 and 28 of Schedule 17 to, FA 2006.

302. This clause applies to UK property rental business of non-UK companies (including non-UK joint venture companies) and subsection (7) applies to non-UK companies. See Q64 and *Change 659* in Annex 1.

303. *Subsection (4)* provides that one of the conditions for subsection (6) to apply is that assets “involved” in the property rental business (or UK property rental business in the case of a non-UK company) are disposed of within two years of cessation of the UK REIT regime. See clause 82(3) for the definition of an asset “involved” in property rental business.

304. *Subsection (4)* refers to “property rental business of the relevant company” rather than “C (tax-exempt)” (see section 132(3) of FA 2006) or “G (property rental business)” (see paragraph 27 of Schedule 17 to FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

Clause 65: Early exit

305. This clause provides that the Commissioners can make certain directions if a group UK REIT or company UK REIT ceases to be a UK REIT within ten years of entering the regime as a result of clause 55 (termination by officer) or clause 61 (automatic termination). It is based on sections 133 and 134(1) of, and paragraph 4 and 29 of Schedule 17 to, FA 2006.

Chapter 10: Joint ventures

Overview

306. This Chapter enacts SI 2006/2866 for joint ventures. See Q3 in the Overview commentary and *Change 663* in Annex 1.

307. It is considered that the whole of Part 4 of FA 2006 applies to a joint venture company unless there is provision to the contrary in SI 2006/2866 (although this interpretation is not explicit in the regulations).

308. Further, we have concluded that the regulations do not deal with taxation of non-property rental business of joint venture companies. This is because section 138(1) of FA 2006 only provides that regulations may be made in respect of “property rental business”. However, we have also concluded that the regulations do apply to the percentage of property rental business carried on by a joint venture company which is attributable to non-UK REIT members.

<p>Q65. We welcome comments on the proposal to apply the whole of Part 4 of FA 2006 to joint venture companies in so far as they carry on property rental business.</p>
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309. SI 2007/3425 has not yet been incorporated into the draft clauses. However, we intend to do this in due course.

310. The clauses simplify the way the joint venture company legislation operates by:

- in the case where the participating UK REIT is a member of a group, treating the joint venture company (in so far as it carries on property rental business) as if it were a member of the UK REIT group (see clause 67(1)); and
- in the case where the participating UK REIT is a company, wherever possible, treating the joint venture company (in so far as it carries on property rental business) and the company UK REIT as if they formed a group UK REIT (see clause 67(2)).

Q66. We welcome comments on the proposal to simplify the way joint venture companies are treated by treating them so far as possible as if they formed part of a group UK REIT.

Clause 66: Overview of Chapter

311. This clause provides an overview of the Chapter. It is new.

Clause 67: Notice for Part to apply

312. This clause provides that a group UK REIT or a company UK REIT can bring a joint venture company (including a non-UK joint venture company) into the regime if certain conditions are met. It is based on section 138(1) and (3) of FA 2006 and regulations 2, 3(1), 9 and 10(1) of SI 2006/2866.

313. This clause enacts regulations 2, 3(1), 9 and 10(1) of SI 2006/2866. See Q3 in the Overview commentary and *Change 663* in Annex 1.

314. *Subsection (1)* provides that, for the purposes of the Part, the principal company of a group UK REIT may give notice for a joint venture company (in so far as it carries on property rental business) to be treated as a member of the group UK REIT. *Subsection (2)* provides that, for the purposes of the Part, a company UK REIT may give notice to be treated as a group UK REIT together with a joint venture company (in so far as it carries on property rental business).

Q67. We welcome comments on the proposal to treat a joint venture company as a member of a group UK REIT for the purposes of the Part.

315. Giving a notice under subsection (2) does not mean that the company UK REIT will be treated as giving a group notice under clause 5(1), and will, as a result, be required to bring all other subsidiaries into the UK REIT regime.

316. *Subsection (3)(b)* provides that the notice must be given to an “officer of Revenue and Customs” rather than “the Commissioners for Her Majesty’s Revenue and Customs” (see regulations 2(2) and 9(3) of SI 2006/2866). This is because in practice the notice will be given to an officer, not the Commissioners. See Q12 in the commentary on clause 6 and *Change 601* in Annex 1.

317. *Subsection (4)(b)* provides that each joint venture company must also satisfy the balance of business tests in clause 12. It is based on condition 7 in regulations 3(1) and 10(1) of SI 2006/2866. When looking at whether the balance of business tests are satisfied, all profits and assets of the joint venture company are taken into account.

Clause 68: Expressions used in Chapter

318. This clause provides definitions of “deemed UK REIT”, “joint venture company”, “venturing company” and “venturing group” for the purposes of the Chapter. It is based on section 138(1) and (2) of FA 2006 and regulations 1(3), 2(1), 3(1), 9(1) and 10(1) of SI 2006/2866.

319. This clause enacts regulations 1(3), 2(1), 3(1), 9(1) and 10(1) of SI 2006/2866. See Q3 in the Overview commentary and *Change 663* in Annex 1.

Clause 69: General modifications of Part

320. This clause provides general modifications to the Part to take into account joint venture companies. It is based on section 138(1) and (2) of, and paragraph 3(1) of Schedule 17 to, FA 2006 and regulations 5 to 8, 10(3), 12, 13 and 15 of SI 2006/2866.

321. This clause enacts regulations 5 to 8, 10(3), 12, 13 and 15 of SI 2006/2866. See Q3 in the Overview commentary and *Change 663* in Annex 1.

322. *Subsection (5)(a)* provides that a reference to a “UK company” which is a member of a UK REIT includes a joint venture company which is UK resident and is not resident in any other place for tax purposes. *Subsection (5)(b)* provides that a reference to a non-UK company includes a joint venture company which is not within subsection (5)(a). Since regulations have been made under section 138(1) of FA 2006 the clauses apply the provisions of paragraph 3(1) of Schedule 17 to FA 2006 to joint venture companies.

Q68. We welcome comments on the proposal to apply paragraph 3(1) of Schedule 17 to FA 2006 to joint venture companies.

Clause 70: Specific modifications of Part

323. This clause provides specific modifications to the Part to take into account joint venture companies. It is based on sections 138(1) and (2) of FA 2006 and various regulations of SI 2006/2866.

324. This clause enacts regulations 2(1), 9(1) and 14 of SI 2006/2866. See Q3 in the Overview commentary and *Change 663* in Annex 1.

325. *Subsections (4) to (8)* provide that a further amount of notional income will be charged to tax under clause 19 if either:

- a venturing company becomes a principal company of a group UK REIT and it increases its holding in a joint venture company; or

- a venturing group increases its holding in a joint venture company to more than 75%.

326. These subsections are based on regulation 14(2) to (7) of SI 2006/2864. As part of the rewrite process, the provisions have been simplified and regulation 14(4)(b) of SI 2006/2866 has not been rewritten because it is not considered to be necessary. If more than 75% of the shares of the joint venture company are held by the company, the joint venture company is treated as a subsidiary and is covered by the clause 5(1) notice. It is not possible to give a further notice under clause 67.

Q69. We welcome comments on the simplification of regulation 14(2) to (7) of SI 2006/2864 and the proposal not to rewrite regulation 14(4)(b) of SI 2006/2866.

Clause 71: Duration of UK REIT status in joint venture cases

327. This clause provides that if the 40% tests in clause 67 are not satisfied, the joint venture company is no longer treated as a member of a group UK REIT or deemed UK REIT. It is based on section 138(1) and (2) of FA 2006 and regulations 4 and 11 of SI 2006/2886.

328. This clause enacts regulations 4 and 11 of SI 2006/2866. See Q3 in the Overview commentary and *Change 663* in Annex 1.

Clause 72: Regulations: joint ventures

329. This clause provides that the Treasury may make regulations in relation to joint ventures. It is based on sections 138 and 134(1) of FA 2006.

330. *Subsection (1)(b)* provides that regulations may be made in relation to joint ventures carried on by a person in which a member of a group UK REIT or a company UK REIT has an interest. Consideration is being given to the need for retaining such a regulation-making power once SI 2006/2866 (joint venture companies) and SI 2007/3425 (joint venture groups) are rewritten; and also to whether the power should allow amendments by regulation to Chapter 10.

Chapter 11: Miscellaneous provision and interpretation

Clause 73: Calculation of profits

331. This clause provides for the calculation of profits for the purposes of certain provisions in the Part. It is based on section 120 of, and paragraph 31(4) of Schedule 17 to, FA 2006.

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332. This clause applies to non-UK companies (paragraphs 31(4) and 32(8) of Schedule 17 to FA 2006) and joint venture companies (including non-UK ones) (regulations 7(5), 8, 13(1) and 15 of SI 2006/2864).

333. *Subsections (4), (5) and (8)* refers to “property rental business” rather than “tax-exempt business” (see section 120(3), (4) and (6) of FA 2006). See Q5 in the Overview commentary and *Change 660* in Annex 1.

334. *Subsection (5)(c) and (d)* is based on section 120(4)(c) of FA 2006. Section 120(4)(c) of FA 2006 refers to “paragraph 2(3) of Schedule 26 to FA 2002”. This provision was replaced by SI 2006/3269 and no longer exists. This is apparently a missed consequential. However the problem is not only the reference to paragraph 2(3) but also the term “host contract” in section 120(3)(c) of FA 2006.

335. It is likely that the correct substitution for “paragraph 2(3) of Schedule 26 to FA 2002” is “paragraphs 2A and 2B of Schedule 26 to FA 2002”. This is based on the fact that article 25(3) of SI 2006/3269 itself substituted this wording for a reference to paragraph 2(3) in paragraph 45L(1A) of Schedule 26.

336. For “host contract” these clauses refer to both a “non-financial host contract” (defined in paragraph 2A of Schedule 26) and a “host contract” (defined in paragraph 2B). As paragraph 2A is rewritten in [clause 558[j72602A] of Bill 5] and paragraph 2B in [clause 559[j72602B] of Bill 5] (Chapter 2 of Part 8) it is proposed to substitute the new Bill 5 references into this clause in due course.

Q70. We welcome comments on the proposals to replace the reference to paragraph 2(3) of Schedule 26 to FA 2002 with references to [clauses 558[j72602A] and 559[j722602B] of Bill 5], which rewrite paragraphs 2A and 2B of Schedule 26 to FA 2002, and to refer to a “non-financial host contract” as well as a “host contract”.

337. *Subsection (8)* requires income and expenditure to be “apportioned on a just and reasonable basis”. It is based on section 120(6) of FA 2006 which states that income and expenditure be “apportioned reasonably”. See *Change 604* in Annex 1.

Q71. We welcome comments on the proposal to require income and expenditure to be apportioned on a just and reasonable basis.

Clause 74: Availability of group reliefs

338. This clause provides that a group UK REIT which carries on property rental business is treated as a separate group from other business carried on by the group for the purposes of various group-related provisions. It is based on section 136 of FA 2006.

339. The source legislation (section 136(1) of FA 2006) refers to “G (property rental business)”. But it does not provide a definition for the purposes of section 136 of FA 2006. The definition is the same as in paragraph 2(b) of Schedule 17 of FA 2006. So the clause refers to the “group so far as it carries on property rental business” rather than “G (property rental business)”. See Q5 in the Overview commentary and *Change 660* in Annex 1.

Clause 75: Effect of deemed disposal and reacquisition

340. This clause provides that a deemed disposal and reacquisition of an asset under this Part has effect for any future disposal. It is based on section 141 of FA 2006.

Clause 76: Regulations

341. This clause provides that regulations made under the Part can also make provision for various other purposes. It is based on section 144 of FA 2006.

342. This clause is drafted in line with other general regulation-making provisions and includes a specific reference to the making of “supplemental” provision.

Clause 77: Property rental business: excluded business

343. This clause provides a list of classes of businesses which are not property rental business. It is based on section 104(2) of, and paragraphs 1 to 5 and 14 of Schedule 16 to, FA 2006.

344. *Subsection (2)* provides a list of classes of business which are not property rental business.

345. Class 4 of subsection (2) refers to “UK property business (as defined by [clause 197[j050102] of Bill 5])”. That clause provides that:

A company’s UK property business consists of-

- (a) every business which the company carries on for generating income from land in the United Kingdom, and
- (b) every transaction which the company enters into for that purpose otherwise than in the course of such a business.

Clause 78: Property rental business: excluded income

346. This clause provides that business is not property rental business in so far as it gives rise to certain income. It is based on section 104(2) of, and paragraphs 6 to 14 of Schedule 16 to, FA 2006.

347. *Subsection (1)* provides that business is not property rental business in so far as it gives rise to income of a class referred to in subsection (2). The source legislation (section 104(2)(b) of FA 2006) refers to “income *or profits...*”. It is unclear what the reference to “profits” is intended to catch. It is therefore proposed to omit the reference to profits in this clause.

Q72. We welcome comments on the proposal to omit the reference to profits in clause 78.

Clause 79: Groups

348. This clause sets out which companies are treated as part of a group for the purposes of the Part. It is based on section 134(2) to (6) of FA 2006.

349. *Subsection (3)* provides that a company cannot be a member of more than one group. However, this does not include joint venture companies which can be members of more than one group UK REIT. See *subsection (4)*.

Clause 80: Meaning of “UK company” and “non-UK company”

350. This clause defines “UK company” and “non-UK company” for the purposes of the Part. It is based on section 106(3) of, and paragraph 3(1) of Schedule 17 to, FA 2006.

351. *Subsection (1)* defines “UK company” for the purposes of the Part as a company which is UK resident and is not resident in any other place for the purpose of taxation. The reason for this new defined term is that the definition of UK company is not the same as “UK resident” (which is defined in [clause 1242 of Bill 5]).

Q73. We welcome comments on the proposal to adopt the new label “UK company”.

352. This clause also applies to joint venture companies as section 138(1) FA 2006 provides that if regulations have been made the UK REIT regime applies subject to modifications in regulations.

Clause 81: Meaning of “entry” and “cessation”

353. This clause defines “entry” and “cessation”. It is based on sections 105(1) and (2) and 134(1) of, and paragraph 4 of Schedule 17 to, FA 2006.

Clause 82: References to assets

354. This clause provides what is meant by a reference to an asset and when that asset is “involved” in a property rental business. It is based on sections 108(3), 111(6), 131(6), 132(3) and 142 of FA 2006.

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Clause 83: Definitions

355. This clause provides a list of definitions for this Part. It is based on section 142 of FA 2006.

356. Our present intention is that the definitions in this clause will be relocated into the index of definitions in Schedule 4 to Bill 6.

ANNEX 1: MINOR CHANGES TO THE LAW MADE BY THE BILL

Change 601: References to “officer of Revenue and Customs”: clauses 6, 8, 14, 21, 26, 27, 44, 48, 54 to 61 and 67

This change replaces references to the “Commissioners” in the source legislation with references to “an officer of Revenue and Customs”.

The provisions affected by this change will in future authorise or require things to be done by or in relation to an officer of Revenue and Customs rather than by or in relation to the Commissioners. This reflects the way in which Her Majesty’s Revenue and Customs is organised and operates in practice. Section 13 of CRCA allows nearly all functions conferred on the Commissioners to be exercised by any officer. All of the functions affected by this change, which are in the main concerned with administrative processes, are in fact exercised by officers of the Commissioners, and the Commissioners themselves are not personally involved in their exercise.

Each provision affected by the conversion of references to the Commissioners will be identified in the Table of Origins by a cross-reference to this change.

This change has no implications for the amount of tax due, who pays it or when. It affects (in principle and in practice) only administrative matters.

Change 604: Requiring an apportionment to be just and reasonable: clause 73

This change requires any apportionment that is not required by the source legislation to be made on a just and reasonable basis to be made on such a basis.

In some cases where there is an apportionment under legislation rewritten in this Act, the apportionment is required by the source legislation to be made on a just and reasonable basis. In other cases, it is required to be made only on a just basis or only on a reasonable basis, or there are no requirements. In new tax legislation it is now the practice to require an apportionment to be just and reasonable. For example, before it was replaced by ITEPA, section 140B(4) of ICTA (inserted by FA 1998) required a just and reasonable apportionment to be made of any consideration given partly in respect of one thing and partly in respect of another. There is no reason why an apportionment should not be on a just and reasonable basis. And it is desirable that all apportionments should be made on the same basis.

Section 120(6) of FA 2006 requires the apportionment to be made reasonably. As rewritten in clause 73(8), it requires the apportionment to be made on a just and reasonable basis.

The same change was made in ITTOIA to provide a uniform expression of the basis on which apportionments are to be made.

This change makes minor amendments to a number of existing rules, but is expected to have no practical effect as it is in line with generally accepted practice.

Change 659: Non-UK companies: clauses 3, 16, 17, 18, 22 and 62 to 64

This change clarifies the basis on which non-UK companies which are members of a group UK REIT are charged to tax. The change, which affects a number of provisions, is linked to the way in which profits arising from, and chargeable gains accruing on assets used by, a trade carried on through a permanent establishment in the UK are subject to corporation tax (section 11 of ICTA and section 10B of TCGA).

The aspects of this change have been grouped together and are set out below and should be considered together as a single change.

Clause 3: paragraph 32(3) of Schedule 17 to FA 2006

Paragraph 32(3) of Schedule 17 to FA 2006 provides that:

The property rental business of the company in the United Kingdom shall be treated as if it were (subject to the application of this Part) chargeable to corporation tax.

Paragraph 32(3) does not specify whether it is profits and/or gains of property rental business in the United Kingdom which are to be made subject to corporation tax. Accordingly, on a strict reading of paragraph 32(3), both should be subject to corporation tax. This would mean that gains made by non-UK companies with no permanent establishment in the United Kingdom would be subject to corporation tax.

Ordinarily, however, gains made by non-UK companies are not subject to tax in the United Kingdom unless they are caught by section 10B of TCGA (ie gains that arise in respect of the disposal of United Kingdom assets used in connection with a United Kingdom permanent establishment).

It is unlikely that it was intended that such gains should be brought within the charge to corporation tax. Clause 3 is therefore drafted on the basis that it is only profits of non-UK companies, which are not already subject to corporation tax, which are caught by this provision (see clause 3(3)).

This aspect of the change is taxpayer-favourable. It ensures that only gains caught by section 10B of TCGA are subject to tax in the United Kingdom.

Clause 16: section 124(3) of FA 2006

Section 124(3) of FA 2006 provides that:

Corporation tax shall be charged in respect of gains accruing to C (residual) at a rate determined without reference to section 13 of ICTA (small companies rate).

This provision is the equivalent of section 119(2) of FA 2006 which makes similar provision in respect of profits. Section 119(2) of FA 2006 provides that:

Profits arising from the business of C (residual) which are charged to corporation tax shall be charged at a rate determined without reference to section 13 of ICTA (small companies rate).

Section 119(2) of FA 2006 is clearly not a charging provision as it refers to profits “which are charged to corporation tax”. However, it is unclear whether section 124(3) of FA 2006 is meant to be a charging provision or not; and if it is not meant to be a charging provision, why it is drafted on a different basis from section 119(2) of FA 2006.

If section 124(3) of FA 2006 is a charging provision, it means that all United Kingdom gains of non-UK companies will be subject to corporation tax if they relate to the non-UK company’s residual business. For non-UK companies which are caught by section 10B of TCGA (ie chargeable gains accruing on disposals of United Kingdom assets used for the purposes of the trade or permanent establishment) this would not be a change as such companies are already subject to corporation tax on such gains. However, for United Kingdom gains accruing to non-UK companies with no permanent establishment this would represent a new charge.

It is unlikely that section 124(3) of FA 2006 should seek to introduce a new charge to tax for non-UK companies. Clause 16 is therefore drafted on the basis that it only applies to companies already subject to corporation tax on gains.

This aspect of the change is taxpayer-favourable. It ensures that only gains caught by section 10B of TCGA will be subject to tax in the United Kingdom.

Clauses 17 and 18: section 111 of FA 2006

Sections 111 and 134(1) of, and paragraphs 9, 10 and 33 of Schedule 17 to, FA 2006 provide that for corporation tax purposes, when a UK company (including a joint venture company) enters the UK REIT regime its property rental business ceases and recommences and the UK company is deemed to sell and reacquire assets involved in that business.

There is nothing in paragraph 32 of Schedule 17 to FA 2006 which modifies this position for non-UK companies. Consequently, the provisions of section 111 of FA 2006 do not apply to non-UK companies.

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It is unclear why this is so when certain non-UK companies are also subject to corporation tax because of section 10B of TCGA (non-UK resident companies are charged to corporation tax on gains accruing on the disposal of assets used for the purposes of a trade or permanent establishment in the United Kingdom). Further, non-UK companies are deemed to be subject to corporation tax in respect of profits of UK property rental business under clause 3(3)(a) (based on paragraph 32(3) of Schedule 17 to FA 2006).

This aspect of the change makes clear that clauses 17 and 18 apply to UK and non-UK companies.

Overall, the effect of this aspect of the change is likely to be taxpayer-favourable. For non-UK companies operating through permanent establishments in the United Kingdom it provides an up-lift in the market value of assets brought into the UK REIT regime. However, this change also means that all property rental business carried on before entry to the regime is treated as ceasing and recommencing. And for corporation tax purposes this change also triggers a new accounting period.

Clause 22: section 113 of FA 2006

Sections 113(1) to (4) and 134(1) of, and paragraphs 12 and 32(3) of Schedule 17 to, FA 2006 provide that property rental business is treated as a separate business from any other business carried on by a group UK REIT or company UK REIT. Also, to the extent that the UK REIT carries on property rental business, it is treated as a separate group or company from the rest of the group or company.

However, it is unclear from the source legislation whether section 113(1) to (4) of FA 2006 applies to each non-UK company individually. This is because paragraph 12(2) of Schedule 17 to FA 2006 does not apply to non-UK companies. (It should be noted that paragraph 12(1) of Schedule 17 of FA 2006 applies to “G (property rental business)” which means that section 113(1) to (4) of FA 2006 does apply to non-UK companies in so far as they are members of a group UK REIT.)

It is difficult to see why section 113 of FA 2006 should not also apply to non-UK companies individually (and accordingly why paragraph 12(2) of Schedule 17 to FA 2006 does not also apply to non-UK companies). In particular it is difficult to see how sections 125 and 126 of FA 2006 apply to non-UK companies if section 113 does not also apply to them.

Clause 22 is therefore drafted so that it applies to all companies including non-UK companies. In particular, subsection (1) applies to a group UK REIT, each member of the group (including a non-UK company) and to a company UK REIT.

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As part of this, subsection (8) provides that this clause only applies to UK property rental business of non-UK companies since overseas property rental business of such companies is not subject to tax in the United Kingdom. Consequently, there is no point in ring-fencing it.

Overall, the effect of this aspect of the change is to clarify the intention of the legislation.

Clauses 62 and 63: section 131 of, and paragraphs 25 and 26 of Schedule 17 to, FA 2006

Sections 131 and 134(1) of, and paragraphs 25 and 26 of Schedule 17 to, FA 2006 provide what happens for corporation tax and capital allowances purposes when a group UK REIT, a UK company which is a member of a group UK REIT or a company UK REIT ceases to be within the UK REIT regime.

There is nothing in paragraph 32 of Schedule 17 to FA 2006 which modifies this position for non-UK companies. Consequently, the provisions of section 131 of FA 2006 do not apply to non-UK companies.

It is unclear why this is so when some non-UK companies are also subject to corporation tax. In particular, all non-UK companies are deemed to be subject to corporation tax in respect of profits of UK property rental business (see paragraph 32(3) of Schedule 17 to FA 2006, rewritten in clause 3(3)(a)) and non-UK companies are charged to corporation tax on gains accruing on the disposal of assets used for the purpose of a trade or permanent establishment in the United Kingdom. Clauses 62 and 63 are therefore drafted so that they apply to all companies including non-UK companies.

Overall, the effect of this aspect of the change is likely to be taxpayer-favourable. For non-UK companies operating through permanent establishments in the United Kingdom it provides an up-lift in the market value of assets sold and reacquired under clause 62(3). However, this change also means that all property rental business carried on by an exiting company is treated as ceasing and recommencing. And for corporation tax purposes this change also triggers a new accounting period.

Clause 64: section 132 of, and paragraphs 27 and 28 of Schedule 17 to, FA 2006

Section 132 of, and paragraphs 27 and 28 of Schedule 17 to, FA 2006 provide what happens when a group UK REIT, a UK company which is a member of a group UK REIT or a company UK REIT leaves the UK REIT regime within ten years of entering the regime and sells an asset within two years of leaving it.

Paragraph 28 of Schedule 17 to, FA 2006 provides that section 132(2) and (3) of FA 2006 only applies when a UK member of a group UK REIT leaves the regime. Further, there is

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nothing in paragraph 32 of Schedule 17 to FA 2006 which modifies this position for non-UK companies.

It is unclear why paragraph 28 of Schedule 17 to, FA 2006 only applies to UK members of a group UK REIT when the rest of section 132 of FA 2006 applies to non-UK companies. The effect of the source legislation is that the provisions of section 132 apply to an exiting company if it is UK resident but does not apply to an exiting company if it is non-UK resident.

Clause 64(7) (together with the rest of the clause) is drafted so that it applies to all companies leaving the regime including non-UK companies.

Subsection (9) restricts the application of this clause by providing that it only applies to UK property rental business of non-UK companies since overseas property rental business of such companies is not subject to tax in the United Kingdom. Consequently, this change will have no practical effect.

The overall effect of this aspect of the change is likely to be taxpayer-adverse. However its effect is limited to situations where a non-UK company, which is subject to corporation tax, leaves the regime.

This change is in principle and in practice adverse to some taxpayers and favourable to others.

Change 660: Tax-exempt business: clauses 12 to 18, 20, 22, 23, 25, 28 to 30, 32, 34, 37 to 40, 50, 51, 62 to 64, 73 and 74

This change replaces references in the source legislation to “C (tax-exempt)” and “G (property rental business)” with references to a company or group so far as it carries on property rental business. It also replaces the references to “tax-exempt business” with references to property rental business.

“C (tax-exempt)” and “G (property rental business)”

Section 105(3)(b) of FA 2006 defines “C (tax-exempt)” as meaning the company in so far as it carries on “tax-exempt business” (as defined in section 107(2) of FA 2006) while Part 4 of FA 2006 applies to it. A company carries on “tax-exempt business” if it satisfies conditions 1, 2 and 3 in section 107. This means that its property rental business must involve at least three properties; no single property may represent more than 40% of the total value of properties involved in property rental business; and at least 90% of the profits of property rental business must be distributed. In the case of a company UK

REIT, references in this note to the “tax-exempt conditions” are to the three conditions mentioned in this paragraph.

However “G (property rental business)” is defined in paragraph 2(b) of Schedule 17 to FA 2006 as meaning the group in so far as it carries on property rental business which satisfies conditions 1 and 2 in section 107 of FA 2006 while Part 4 of FA 2006 applies to it. This means that the property rental business must involve at least three properties; and no single property may represent more than 40% of the total value of properties involved in property rental business. Consequently, “G (property rental business)” does not include a reference to the 90% distribution requirement. In the case of a group UK REIT, references in this note to the “tax-exempt conditions” do not include a reference to the 90% distribution requirement. It is nonetheless clear that the distribution requirement must be satisfied by a group.

In order to align the position for a group UK REIT and a company UK REIT, the 90% distribution requirement is rewritten as a separate clause (clause 11) immediately after clause 10, which rewrites conditions 1 and 2 in section 107(2).

“Tax-exempt business”

Section 107(2) of FA 2006 provides that “property rental business” is “tax-exempt business” if at least three properties are involved in the property rental business, no single property is worth more than 40% of the total value of the properties involved in the property rental business and at least 90% of the profits of the property rental business are distributed by the principal company of a group UK REIT or by a company UK REIT.

If a UK REIT breaches any of conditions 1 to 3 in section 107, it does not have a “tax-exempt business”. This means that it cannot be treated as “C (tax-exempt)” or “G (property rental business)”, which in turn means that the provisions of the Part cannot apply to it. Clause 107(1) clarifies this point by stating that “in order to be a company to which the Part applies ... the company must throughout the accounting period have a property rental business in respect of which conditions 1 and 2 below [in section 107] are satisfied”. Consequently, on a strict reading of the legislation, if a group or company does not have a tax-exempt business, it should not be treated as a UK REIT.

However, since regulations 5 and 6 of SI 2006/2864 allow the conditions in section 107 FA 2006 to be breached without the UK REIT ceasing to be a UK REIT the clauses do not retain the references to “tax-exempt business”. Instead the tax-exempt conditions are requirements which need to be satisfied by the UK REIT in relation to each accounting period. It should be noted, however, these requirements are subject to the provisions set out in Chapters 8 (breach of conditions in Chapter 2) and 9 (leaving the UK REIT regime).

Affected clauses

This change affects the following clauses:

- *Clause 12:* The balance of business tests in section 108 of FA 2006 (as modified by paragraph 7 of Schedule 17 to FA 2006) provide that at least 75% of the profits must arise, and 75% of the assets must be involved in, “tax-exempt business”. However, if the group or company breaches the tax-exempt business conditions in section 107 of FA 2006 but remains in the UK REIT regime it cannot satisfy the balance of business conditions because it will not have any assets or profits which relate to “tax-exempt business”. Consequently, it automatically ceases to be a UK REIT. As it is unlikely that it is intended that a breach of section 107 of FA 2006 should automatically cause a breach of section 108 of FA 2006, the clauses are drafted on the basis that the balance of business conditions can be satisfied if at least 75% of the profits and 75% of the assets of the UK REIT relate to “property rental business” (rather than to “tax-exempt business”). This change also means that for the purposes of regulation 8 of SI 2006/2864 (multiple breaches) there is no longer an automatic breach of the balance of business tests when the tax-exempt conditions in section 107 are not met.
- *Clauses 13(2) and 14(3):* Paragraph 31 of Schedule 17 to FA 2006 provides that financial statements must be prepared for “G (property rental business)”. The references to G (property rental business) are replaced with references to “the group’s property rental business” because it is the group in so far as it carries on property rental business for which financial statements must be prepared. If the group fails to satisfy the tax-exempt conditions it is still required to prepare and submit financial statements as long as it remains within the UK REIT regime.
- *Clause 15(1):* Section 119(1) of, and paragraph 17(1)(a) of Schedule 17 to, FA 2006 provide that profits arising from the business of C (tax-exempt)/G (property rental business) shall not be charged to corporation tax. The references to C (tax-exempt)/G (property rental business) are replaced with references to “property rental business” because, even if the tax-exempt conditions set out in section 107(2) of FA 2006 are not met, the profits of property rental business should still not be subject to corporation tax as long as the group or company remains within the UK REIT regime.
- *Clause 15(4):* Paragraph 17(2) of Schedule 17 to FA 2006 provides that where a percentage of profits is excluded from the financial statements in accordance with paragraph 31(5) of Schedule 17 to FA 2006, the excluded percentage of profits shall be treated as profits arising from the residual business of G (property rental business). The reference to G (property rental business) is replaced with a reference to “property rental business of a member of a group” because, even if the tax-exempt conditions are not met, the profits of the property rental business

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should still be attributed to the residual business as long as the group remains within the UK REIT regime.

- *Clause 16(2) to (5)*: Section 124 of, and paragraph 21 of Schedule 17 to, FA 2006 provide that gains accruing to the business of C (tax-exempt)/G (property rental business) shall not be charged to corporation tax. The references to C (tax-exempt)/G (property rental business) are replaced with references to “property rental business” because, even if the tax-exempt conditions are not met, the gain accruing to the property rental business should still not be subject to corporation tax as long as the group or company remains within the UK REIT regime.
- *Clause 16(7)*: Paragraph 21(2) of Schedule 17 to FA 2006 provides that where a percentage of gains is excluded from the financial statements in accordance with paragraph 31(5) of Schedule 17 to FA 2006, the excluded percentage shall be treated as gains arising from the residual business of G (property rental business). The reference to G (property rental business) is replaced with a reference to “property rental business of a member of a group” because, even if the tax-exempt conditions are not met, the gains of property rental business should still be attributed to the residual business as long as the group remains within the UK REIT regime.
- *Clause 17(2)*: Section 111(2) of, and paragraph 9(2) of Schedule 17 to, FA 2006 provide that, for the purposes of corporation tax, assets involved in property rental business before entry to the UK REIT regime are treated as being sold and reacquired by C (tax-exempt)/G (property rental business). The references to C (tax-exempt)/G (property rental business) are replaced with references to “the company so far as it carries on property rental business” because, even if the tax-exempt conditions are not met, assets used in property rental business are treated as sold and reacquired as long as the group or company remains within the UK REIT regime.
- *Clause 17(5)*: Paragraphs 9(4) and 10(2) of Schedule 17 to, FA 2006 provide that, for the purposes of corporation tax, where a percentage of the assets of a member of G (property rental business) is excluded from the financial statements in accordance with paragraph 31(5) of Schedule 17 to FA 2006 (non-member percentage), that percentage of the assets is disregarded for the purposes of the sale and reacquisition provisions rewritten in this clause. The reference to G (property rental business) is replaced with a cross-reference to clause 14(3) and clause 13(2) which deal with the “group’s property rental business” because, even if the tax-exempt conditions are not met, the assets are still disregarded as long as the group remains within the UK REIT regime.

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- *Clause 18(4)*: Section 111(4) of, and paragraph 9(2) of Schedule 17 to, FA 2006 provide that, for the purposes of CAA, anything done by a company before entry to the UK REIT regime is deemed to have been done by or to C (tax-exempt)/G (property rental business). The references to C (tax-exempt)/G (property rental business) are replaced with references to the “company so far as it carries property rental business” because, even if the tax-exempt conditions are not met, the provisions rewritten in this clause still apply as long as the group or company remains within the UK REIT regime.
- *Clause 20(3)*: Section 112(3)(a) of, and paragraph 11(1) of Schedule 17 to, FA 2006 provide that market value is the sum of the market value of assets which are treated as sold and reacquired by C (tax-exempt)/G (property rental business). The references to C (tax-exempt)/G (property rental business) are replaced with references to “property rental business of the company” because, even if the tax-exempt conditions are not met, assets used in respect of property rental business are treated as sold and reacquired as long as the group or company remains within the UK REIT regime.
- *Clause 20(4)*: Paragraphs 9(4) and 10(2) of Schedule 17 to, FA 2006 provide that where a percentage of the assets of a member of G (property rental business) is excluded from the financial statements in accordance with paragraph 31(5) of Schedule 17 to FA 2006 (non-member percentage), that percentage of the assets is disregarded for the purposes of market value. The reference to G (property rental business) is replaced with a cross-reference to clause 14(3) and clause 13(2) which deal with the “group’s property rental business” because, even if the tax-exempt conditions are not met, the assets are still disregarded as long as the group remains within the UK REIT regime.
- *Clause 22(2) to (4)*: Section 113 of, and paragraph 12 of Schedule 17 to, FA 2006 provide that, for the purposes of corporation tax, the business of C (tax-exempt)/G (property rental business) is a separate and distinct business from any other business carried on by the company. Further, that to the extent that a UK REIT carries on property rental business, C (tax-exempt)/G (property rental business) are treated as a separate company or group. The references to C (tax-exempt)/G (property rental business) are replaced with references to “property rental business” of the group or company because it is the property rental business which is ring-fenced, not just property rental business which satisfies the tax-exempt conditions set out in section 107(2) of FA 2006. In particular, if the company breaches the requirements of section 107(2) but is still within the UK REIT regime, the property rental business is still ring-fenced notwithstanding that it is not “tax-exempt business” as defined in section 107(2) of FA 2006.

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- *Clause 22(7)*: Paragraph 12(3) of Schedule 17 to, FA 2006 provides that where a percentage of the profits of a member of G (property rental business) is excluded from the financial statements in accordance with paragraph 31(5) of Schedule 17 to FA 2006 (non-member percentage), the excluded percentage of the profits is treated as profits of residual business. The reference to G (property rental business) is replaced with a reference to the “property rental business of a member of a group” because, even if the tax-exempt conditions are not met, the profits are still treated as profits of residual business as long as the group remains within the UK REIT regime.
- *Clause 23*: Section 113(5) and (6) of, and paragraph 12(2) of Schedule 17 to, FA 2006 provide that UK companies can use losses from overseas property rental business against other property rental business income. It also disappplies the exemption for small and medium-sized enterprises in the transfer pricing rules. The references to C (tax-exempt)/G (property rental business) are replaced with references to “property rental business” of the group or company because it is the property rental business which is subject to this clause, not just property rental business which satisfies the tax-exempt conditions set out in section 107(2) of FA 2006. In particular, if the company breaches the requirements of section 107(2) but is still within the UK REIT regime, the property rental business is still subject to this clause notwithstanding that it is not “tax-exempt business” as defined in section 107(2) of FA 2006.
- *Clause 25*: “Property profits” and “property financing costs” are defined by reference to “property rental business” rather than by reference to “G (property rental business)” (paragraph 14 of Schedule 17 to FA 2006) or “C (tax-exempt)” (section 115 of FA 2006). This is because “property profits” include profits of the property rental business regardless of whether the company satisfies the tax-exempt conditions, as long as the company remains in the UK REIT regime. Similarly, “property financing costs” include the financing costs of property rental business regardless of whether the company satisfies the tax-exempt conditions.
- *Clause 28*: This clause provides that cash proceeds from the sale of assets used for property rental business are to be treated for the first year as assets held in connection with property rental business. This clause refers to “property rental business” rather than “tax-exempt business”, “C (tax-exempt)” or “G (property rental business)” (see section 118 of, and paragraph 16 of Schedule 17 to, FA 2006). This is because cash proceeds from assets used in property rental business should benefit from this clause regardless of whether the assets also meet the tax-exempt conditions, as long as the company remains in the UK REIT regime.

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- *Clause 29:* This clause provides that distributions by a principal company of a group UK REIT or by a company UK REIT in respect of profits and gains of property rental business are treated as profits of UK property business rather than as a dividend in the hands of the shareholder. Subsections (1) and (3) refer to “property rental business” of the UK REIT rather than “C (tax exempt)”/”G (property rental business)” (see section 121(1) of, and paragraph 18 of Schedule 17 to, FA 2006). This is because all distributions in respect of property rental business are treated as UK property income in the hands of a shareholder regardless of whether the company satisfies the tax-exempt conditions, as long as the company remains in the UK REIT regime.
- *Clause 30:* Subsections (3) and (4) provide that section 231 of ICTA and section 397 of ITTOIA do not apply to distributions made by a company in respect of profits and gains of property rental business. Subsection (4) refers to “property rental business” rather than “C (tax-exempt)” because section 121(5) of FA 2006 applies to all distributions in respect of the property rental business regardless of whether the company satisfies the tax-exempt conditions as long as the company remains in the UK REIT regime.
- *Clause 32(3):* This clause sets out how distributions are to be attributed between property rental business and any other business. Subsection (3) refers to “property rental business” of a member of a group or of a company rather than “C (tax-exempt)”/”G (property rental business)” (see section 123(d) of, and paragraph 20(b) of Schedule 17 to, FA 2006). This is because even if the company does not satisfy the tax-exempt conditions, the attribution of distributions provision applies, as long as the company remains in the UK REIT regime.
- *Clause 34(2) and (3):* “DO” (distribution in respect of ordinary shares) and “DP” (distribution in respect of preference shares) are defined by reference to a group’s “UK profits” (as defined in clause 11(2)) for a group UK REIT; and by reference to “profits of property rental business of the company” for a company UK REIT. The source legislation (regulation 10(2) of SI 2006/2864) defines them by reference to “C (tax-exempt)”. DO and DP should be calculated by reference to property rental business regardless of whether the property rental business is “tax-exempt” as defined in section 107(2) of FA 2006, as long as the company remains in the UK REIT regime. Further, for a group UK REIT, it is unclear what is meant by the reference to “C (tax-exempt)”.
- *Clause 37(1), (2) and (4):* This clause sets out how gains made on the disposal of an asset used in property rental business (or UK property rental business of non-UK companies) are treated. This clause refers to property rental business of a company rather than “C (tax-exempt)”/”G (property rental business)” (see section 125 of, and paragraph 21 of Schedule 17 to, FA 2006). This is because

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section 125 applies to all disposals of assets used for the purposes of property rental business, regardless of whether the company satisfies the tax-exempt conditions, as long as the company remains in the UK REIT regime.

- *Clause 37(8)*: Paragraph 21(2) of Schedule 17 to FA 2006 provides that where a percentage of the gains of a member of G (property rental business) is excluded from the financial statements in accordance with paragraph 31(5) of Schedule 17 to FA 2006 (non-member percentage), the excluded percentage of the gains is treated as gains of residual business. The reference to G (property rental business) is replaced with a cross-reference to clause 14(3) and clause 13(2) which deal with the “group’s property rental business” because, even if the tax-exempt conditions are not met, the gains are still treated as gains of residual business as long as the group UK REIT remains within the UK REIT regime.
- *Clause 38*: This clause provides that any sale and reacquisition under clause 37(2) is automatically at tax written-down value for the purposes of CAA. This clause refers to “the company so far as it carries on property rental business” rather than “C (tax-exempt)”/”G (property rental business)” (see section 125 of, and paragraph 21(1) of Schedule 17 to, FA 2006). This is because even if the company does not satisfy the tax-exempt conditions, this provision still applies, as long as the company remains in the UK REIT regime.
- *Clause 39(1) and (2)*: This clause provides that if an asset used for the purposes of residual business of a company begins to be used for the purposes of its property rental business, the asset is treated as having been disposed of and reacquired at market value. It also provides that for the purposes of the CAA the transfer of the asset is treated as being made at the tax-written down value. This clause refers to “the company so far as it carries on property rental business” rather than “C (tax-exempt)”/”G (property rental business)” (see section 126 of, and paragraph 21 of Schedule 17 to, FA 2006). This is because section 126 provides that the assets are deemed to be reacquired by the company so far as it carries on property rental business regardless of whether the company satisfies the tax-exempt conditions, as long as the company remains in the UK REIT regime.
- *Clause 39(5)*: Paragraph 21(2) of Schedule 17 to FA 2006 provides that where a percentage of the gains of a member of G (property rental business) is excluded from the financial statements in accordance with paragraph 31(5) of Schedule 17 to FA 2006 (non-member percentage), that percentage of the gains is treated as gains of residual business. The reference to G (property rental business) is replaced with a cross-reference to clause 14(3) and clause 13(2) which deal with the “group’s property rental business” because, even if the tax-exempt conditions are not met, the gains is still treated as gains of residual business as long as the group remains within the UK REIT regime.

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- *Clause 40:* This clause makes provision for a company UK REIT to dispose of an asset to a 75% subsidiary which subsequently becomes a member of a group UK REIT. This clause refers to “property rental business” rather than “C (tax-exempt)” (see section 126A of FA 2006). This is because section 126A provides that the demerger rules apply as long as the company is a UK REIT, regardless of whether it satisfies the tax-exempt conditions.
- *Clause 50:* This clause sets out how to calculate “the notional amount” for the purposes of clause 49. Subsection (3) refers to “property rental business of the company” rather than “C (tax-exempt)”/“G (property rental business)” (see regulation 7A(5) of SI 2006/2864). This is because the definition of “market value of assets” is calculated by reference to the aggregate market value of assets of property rental business regardless of whether the group or company satisfies the tax-exempt conditions, as long as the company remains in the UK REIT regime.
- *Clause 51:* This clause provides how the balance of business conditions in clause 12 can be breached in the accounting periods following the first accounting period of a UK REIT without causing the UK REIT regime to terminate. This clause refers to “property rental business” rather than “tax-exempt business” (see regulation 7B(2) and (3) of SI 2006/2864). This is because the conditions in section 108 of FA 2006 apply to profits of, or assets involved in, property rental business regardless of whether the company satisfies the tax-exempt conditions, as long as the company remains in the UK REIT regime.
- *Clause 62(2) and (3):* This clause provides what happens, for corporation tax purposes, when a group UK REIT, a member of a group UK REIT (including a joint venture company) or a company UK REIT ceases to be within the UK REIT regime. Subsection (2) refers to “property rental business of an exiting company” rather than “C (tax-exempt)”/“G (property rental business)”. This is because section 131(1) of FA 2006 (as modified by paragraphs 25 and 26 of Schedule 17 to FA 2006) provides that the business ceases and the assets are deemed to be sold and reacquired regardless of whether the group or company satisfies the tax-exempt conditions.
- *Clause 63(5):* This clause provides what happens for the purposes of CAA when a member of a group UK REIT (including a joint venture company) or a company UK REIT ceases to be within the UK REIT regime. Subsection (5) refers to the “company so far as it carries on property rental business” rather than “C (tax-exempt)”/“G (property rental business)”. This is because section 131(4) of FA 2006 (as modified by paragraphs 25 and 26 of Schedule 17 to FA 2006) provides that anything done prior to cessation by or to “C (tax-exempt)”/ “G (property rental business)” is treated as being done by or to the company after

cessation. But this provision applies regardless of whether the company satisfies the tax-exempt conditions.

- *Clause 64(4)*: This clause provides what happens, for corporation tax purposes, when a group UK REIT, a member of a group UK REIT (including a joint venture company) or a company UK REIT leaves the UK REIT regime within ten years of entry and sells an asset within two years of leaving the regime. Subsection (4) refers to “property rental business of the relevant company” rather than “C (tax-exempt)”/“G (property rental business)”. This is because section 132 of FA 2006 (as modified by paragraphs 27 and 28 of Schedule 17 to FA 2006) refers to the disposal of a “tax-exempt asset”, ie one involved in the business of “C (tax-exempt)”/“G (property rental business)”. But this provision applies regardless of whether the company satisfies the tax-exempt conditions.
- *Clause 73*: This clause provides for the calculation of profits for the purposes of certain provisions of the Part. The clause refers to “property rental business” rather than “tax-exempt business” (see section 120(3), (4) and (6) of FA 2006). This is because the calculation of profits applies to the “property rental business” of the UK REIT even if it fails to satisfy the tax-exempt conditions, as long as the group or company remains in the UK REIT regime.
- *Clause 74*: This clause provides that a group UK REIT which carries on property rental business is treated as a separate group from other business carried on by the group for the purposes of various group-related provisions. Subsection (1) refers to “the group so far as it carries on property rental business” rather than “G (property rental business)” (see section 136(1) of FA 2006). This is because the property rental business is treated as separate from other business even if the group fails to satisfy the tax-exempt conditions, as long as the group remains in the UK REIT regime.

This change has no implications for the amount of tax due, who pays it or when. It affects (in principle and in practice) only administrative matters.

Change 661: Entry charge: clauses 19 and 20

This change clarifies the way the entry charge is calculated for the purposes of non-UK companies and joint venture companies.

Sections 112(1), (2) and (4) and 134(1) of, and paragraphs 11 and 33 of Schedule 17 to, FA 2006 (rewritten in clause 19) provide for an amount of notional income (calculated in

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accordance with clause 20) to be chargeable to tax on each company on entry to the UK REIT regime.

Sections 112(3), 134(1) of, and paragraph 11(1) of Schedule 17 to, FA 2006 (rewritten in clause 20) set out how to calculate the amount of notional income.

Clauses 19(3) and 20(5)(a)

The amount of tax (the entry charge) actually paid by a company is 2% of the market value of the assets involved in the property rental business (or UK property rental business if the company is non-UK resident) immediately before entry. This is because the rate of tax used in the numerator (see clause 19) should be the same as the rate of tax used in the denominator of the tax calculation in clause 20(2) and the numerator and denominator tax rates should cancel each other out.

However, for UK joint venture companies, it is unclear what rate of tax applies for the purposes of the calculation in section 112(2) of FA 2006. This is because SI 2006/2866 does not specify the rate of tax applicable for the purposes of section 112 of FA 2006.

Clauses 19(3) and 20(5)(a) are drafted to make it clear that UK joint venture companies are treated in the same way as other UK companies and consequently the rate of tax used is the rate used in clause 15(3).

From a practical point of view, this has no effect as the entry charge remains 2% of the market value of assets involved in UK property rental business. This is because the rate of tax used in the numerator (see clause 19) is the same as the rate of tax used in the denominator of the tax calculation in clause 20(2) and the numerator and denominator tax rates cancel each other out.

Clauses 19(4) and 20(5)(b)

Paragraph 11(1)(d)(iii) of Schedule 17 to FA 2006 provides that:

[section 112 of FA 2006 shall apply to non-UK resident members] as if a reference to the rate at which the company pays tax on income were, where relevant, a reference to the rate at which the company would pay tax on the notional income if it were the highest part of the company's income.

It is unclear what is meant by the reference to the "highest part of the company's income". For non-UK companies (including non-UK joint venture companies) liable to income tax, section 11 of ITA provides that income tax is charged at the basic rate unless the amount relates to savings or dividend income. So clauses 19(4) and 20(5)(b) are drafted on the basis that the notional amount is subject to tax at the basic rate in the case of non-UK companies.

From a practical point of view, this has no effect as the entry charge remains 2% of the market value of assets involved in UK property rental business. This is because the rate of tax used in the numerator (see clause 19) is the same as the rate of tax used in the denominator of the tax calculation in clause 20(2) and the numerator and denominator tax rates cancel each other out.

This change has no implications for the amount of tax due, who pays it or when. It affects (in principle and in practice) only administrative matters.

Change 662: Enactment of the Real Estate Investment Trusts (Breach of Conditions) Regulations 2006 (SI 2006/2864) and the Real Estate Investment Trusts (Breach of Conditions) (Amendment) Regulations 2007 (SI 2007/3540): clauses: 24, 33 to 35, 44, to 51 and 56 to 60

This change enacts and revokes the provisions of regulations 1 to 10 and 12 to 14 of the Real Estate Investment Trusts (Breach of Conditions) Regulations 2006 (SI 2006/2864) and the whole of the Real Estate Investment Trusts (Breach of Conditions) (Amendment) Regulations 2007 (SI 2007/3540). It also relates to the proposed insertion of regulation 11 of SI 2006/2864 into the Real Estate Investment Trusts (Assessment and Recovery of Tax) Regulations 2006 (SI 2006/2867) and (following its insertion into SI 2006/2867) the revocation of that regulation.

Under sections 114 to 116 of FA 2006 and sections 973 and 974 of ITA the Treasury has power to make regulations dealing with breaches of conditions or requirements.

The regulations made in SI 2006/2864 (as amended by SI 2007/3540) provide circumstances when a breach can be made without the UK REIT regime terminating, the number of breaches which can be made before the regime terminates and whether any additional tax should be paid in consequence of the breach.

The regulation making power in section 115(1) and (3) of FA 2006 (profit: financing-cost ratio) is not rewritten. Instead it is proposed to enact the regulations made under these provisions (see clause 24 which enacts regulations 12 and 13 of SI 2006/2864).

The following is a list of where the regulations of SI 2006/2864 (as amended by SI 2007/3540) are rewritten:

- Regulation 1: various clauses

- Regulation 1(2): clause 34 (definition of MCT) and clause 35 (definition of holder of excessive rights)

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- Regulation 2: clause 45, mainly in subsection (2)
- Regulation 3: clause 45, mainly in subsections (3) and (4)
- Regulation 4: clause 45, mainly in subsection (5)
- Regulation 5(1) and (2): clause 46
- Regulation 5(2) to (5): clause 58
- Regulation 6(1) to (3) and (5) to (8): clause 47
- Regulation 6(4): clause 48
- Regulation 7(1) and (2): clause 49
- Regulation 7(3): not rewritten
- Regulation 7(4) and (5): clause 57
- Regulation 7A(1) to (3) and (8): clause 49
- Regulation 7A(4) to (7): clause 50
- Regulation 7B(1) to (3): clause 51
- Regulation 7B(4) to (7): clause 59
- Regulation 8: clause 60
- Regulation 9: clause 44
- Regulation 10: clauses 33, 34
- Regulation 11: to be relocated to SI 2006/2867
- Regulation 12: clause 24
- Regulation 13: clause 24
- Regulation 14: clause 56

As mentioned in Change 664, it is proposed to restrict the regulation-making power in section 114 of FA 2006 (holders of excessive rights). Also the regulation-making power in section 115 of FA 2006 (profit: financing-cost ratio) is not being rewritten. Finally there is consultation on whether the regulation-making power in section 116 of FA 2006 (minor or inadvertent breach) should be rewritten (see commentary on clause 43). As a result, the rewritten provisions are either no longer subject to regulation-making powers or are subject to restricted regulation-making powers.

This change has no implications for the amount of tax due, who pays it or when. It affects (in principle and in practice) only administrative matters.

Change 663: Enactment of the Real Estate Investment Trusts (Joint Ventures) Regulations 2006: clauses 24, 67 to 71

This change enacts and revokes the provisions of the Real Estate Investment Trusts (Joint Ventures) Regulations 2006 (SI 2006/2866).

SI 2006/2866 was made under the powers conferred on the Treasury by section 138 FA 2006. Section 138(1) of FA 2006 gives the Treasury power to make regulations providing that the UK REIT regime applies in relation to property rental business carried on either jointly by a UK REIT and another person or by a person in which a UK REIT has an interest. Under section 138(2)(b) of FA 2006 the Treasury has power to make regulations which modify or disapply a provision of the Part in its application to a UK REIT.

SI 2006/2866 provides that a modified version of the UK REIT regime applies to joint venture companies where a UK REIT has at least a 40% interest in the joint venture company. In order to make the legislation more user-friendly SI 2006/2866 has been incorporated in the main body of legislation dealing with UK REITs. In particular, Chapter 10 provides general and specific modifications of the Part for the purposes of joint venture companies.

SI 2006/2866 is enacted on the following basis:

- the whole of Part 4 of FA 2006 applies to joint venture companies unless there is provision to the contrary in SI 2006/2866 although this is not explicit in the regulations, and
- the regulations do not deal with taxation of residual business of joint venture companies. This is because section 138(1) of FA 2006 provides that regulations may be made in respect of “property rental business”.

In addition the way the joint venture company legislation operates has been simplified by:

- in the case of venturing groups, treating the joint venture company as if it were a member of the UK REIT group; and
- in the case of venturing companies, wherever possible, treating the joint venture company and venturing company as if they formed a group UK REIT.

In clause 24(2) the financing-cost ratio formula applies to joint venture companies in the same way as for other UK REITs (see regulation 6(4) of SI 2006/2866).

It is also proposed to enact (and revoke) the Real Estate Investment Trusts (Joint Venture Groups) Regulations 2007 (SI 2007/3425). However, these provisions are not yet included in the draft clauses.

As mentioned in the commentary on clause 72, consideration is being given to the need for the general regulation-making power which would enable clauses 67 to 71 to be amended.

This change has no implications for the amount of tax due, who pays it or when. It affects (in principle and in practice) only administrative matters.

Change 664: Section 114 of FA 2006: clause 36

This change rewrites the regulation-making power in section 114 of FA 2006.

Clause 36 allows the Treasury to make various regulations dealing with distributions made to holders of excessive rights (defined in clause 35). It is based on section 114 of, and paragraph 13 of Schedule 17 to, FA 2006.

The general regulation-making power in section 114(1) of FA 2006 and the provision in section 114(2)(a) of FA 2006 have not been rewritten because regulations 1(2) and 10 SI 2006/2864 (which were made under these powers) have been rewritten clauses 33 to 35. See also *Change 662* in this Annex.

The omission of the general regulation-making power means that it is no longer possible to amend clauses 33 to 35 by regulations.

Instead, there is a specific regulation-making power where a principal company of a group UK REIT or a company UK REIT makes a distribution to a holder of excessive rights.

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The restricted regulation-making power provides:

- a power to provide that a charge does not arise or is reduced if the company takes certain action. The reason for keeping this regulation-making power (which is based on section 114(2)(b) of FA 2006) is that no regulations have yet been made under this power; and
- a power to provide for the collection of information. This is a new provision. The reason for including it is that regulation 11 of SI 2006/2864 is not enacted in this Part. Instead it will be inserted into SI 2006/2867 (which deals with assessment and recovery). See Change 662 in Annex 1. This power will allow the continuation of regulation 11 of SI 2006/2864.

This change has no implications for the amount of tax due, who pays it or when. It affects (in principle and in practice) only administrative matters.