THE INVESTMENT ASSOCIATION

AREF

Response to consultation

The UK Property Rich Collective Investment Vehicles (Amendment of the Taxation of Chargeable Gains Act 1992) Regulations 2021

About the Investment Association

The Investment Association (IA) champions UK investment management, a world-leading industry which helps millions of households save for the future while supporting businesses and economic growth in the UK and abroad. Our 250 members range from smaller, specialist UK firms to European and global investment managers with a UK base. Collectively, they manage £8.5trillion for savers and institutions, such as pension schemes and insurance companies, in the UK and beyond. The UK asset management industry is the largest in Europe and the second largest globally.

About the Association of Real Estate Funds

The Association of Real Estate Funds (AREF) represents the UK real estate funds industry and has 67 member funds with a collective net asset value of more than £70 billion under management on behalf of their investors. The Association is committed to promoting transparency in performance measurement and fund reporting through the AREF Code of Practice, the MSCI/AREF UK Quarterly Property Funds Index and the MSCI/AREF Property Fund Vision Handbook.

Executive Summary

The IA and AREF warmly welcome the draft legislation introducing a portfolio exemption for non-resident Collective Investment Vehicles (CIVs) and offshore Life Insurance Companies from the UK Non-Resident Capital Gains (UK NRCG) rules.

Feedback from our members as well as the wider international fund industry has been universally positive and unequivocally supportive. We value the pragmatic and supportive approach that HMRC has taken in dealing with policy and practical issues that have arisen since the introduction of the NRCG rules in 2019.

The resulting amendments represent a collaborative effort with industry and helps build trust in a tax system that is seen as fair and even-handed, making good on the UK Government's recent commitment to building a modern tax administration system fit for the 21st century. Both AREF and the IA believe this approach reflects best practice through sustained dialogue with stakeholders to not only help craft policy, but follow through on commitments to further hone legislation after it has ascended to the statute book. Each iteration of these rules, through secondary legislation and updates to guidance, has resulted in improvements and provides a model for future policy making.

The introduction of the portfolio exemption for holdings less than 10% in UK Property Rich entities will remove the disproportionate administrative burden and consequential commercial barriers for incidental investment in UK real estate by foreign investors such as

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CIVs and Life Assurance companies, while protecting the UK's taxing rights on significant investments in the UK property sector by non-UK residents.

The 10% threshold will bring the UK tax rules in line with international norms and send a positive message to investors globally on the openness of the UK government to protect and enhance the competitiveness of the UK. We particularly also welcome the retrospective nature of the change which will ensure parity for all investors irrespective of the time that they invested in UK property rich assets.

On the whole, the draft regulations[1] set out for consultation look to achieve the outcome that the policy announcement in the explanatory memorandum lays down. **We urge HMRC to lay these before Parliament at the earliest opportunity so that any remaining uncertainty can be alleviated as early as possible and non-UK investors can once again look to favourably consider UK as an attractive investment location.**

We have in this letter set out some of the practical areas where minor changes to the rules or supporting guidance would serve to clarify some of the more technical elements of the rules.

Our Response

The draft regulations proposed are aimed to exempt from UK NRCGT charge, holdings of less than 10% by non-resident CIVs and offshore Life Insurance Companies in UK Property Rich entities including Real Estate Investment Trusts and Property Authorities Investment Funds.

We understand that entities meeting the relevant criteria can avail the portfolio exemption without requiring any additional UK filing requirements. We have in this note highlighted a few operational and administrative issues which we believe may cause some friction in the intervening months before these regulations are given effect.

We have listed below a number of areas where further clarification or additional guidance would be helpful:

A. Umbrella or Sub-fund

The portfolio exemption, as currently designed, offers a test which requires an investor to monitor the value of their holding in a UK Property Rich entity relative to the total market capitalisation. The rules however do not stipulate whether this check should be conducted at an umbrella or sub-fund level in case of CIVs set up as umbrella funds.

Consistent with HMRC guidance treating sub-funds as separate entities for UK tax purposes under the NRCG rules, we request HMRC to issue clarification to confirm that the holdings test would also apply at sub-fund level. This will ensure consistency of application of the NRCG rules to sub-funds.

Applying the test at the sub-fund level will also allow fund managers to monitor this requirement on an on-going basis, ensuring that each individual sub-fund manager is able to operate their portfolio independently.

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[1] (Draft) The UK Property Rich Collective Investment Vehicles (Amendment of the Taxation of Chargeable Gains Act 1992) Regulations 2021

Our Ask: We request HMRC to clarify that the test would be done at sub-fund level consistent with the rest of NRCG provisions either by (a) amending the draft regulations before being laid before the Parliament or (b) through further guidance.

B. Administration - Nil Returns and Unwinding Registrations

We recognise that the consultation does not specifically seek to address the operational issues of previous versions of these regulations. However, by virtue of the new regulations solving the core policy issues, a number of operational issues arise for non-resident CIVs and insurance investors until such time as they are legally out of scope of the rules due to the portfolio exemption.

The Finance Act 2019, which introduced these rules, meant that from April 2019 disposals in UK Property Rich assets by non-resident CIVs were in scope. While subsequent guidance now allows for annual returns to be filed, at the time once a disposal had been made tax payers were required to register for a Unique Tax Reference within 30 days and treat disposals as a single day accounting period. As a result, a significant population of CIVs have registered with HMRC.

Further changes made through *The UK Property Rich Collective Investment Vehicles (Amendment of the Taxation of Chargeable Gains Act 1992) Regulations 2020* and the rewording to the definition of a UK REIT has meant that very few disposals have ultimately triggered the need for a tax filing. This however means that many CIVs who have registered have been issued with late filing penalties as HMRC systems cannot deal with this mismatch and automatically generate a notice when they cannot link a period to a filed return.

We understand that in communication with HMRC Compliance Teams our members have been told that in order to avoid penalty notices for missed filings CIVs which have already registered for a UTR should submit nil returns to reflect that any disposals are not in scope. We have also heard from members that HMRC has also issued penalties for single day accounting periods (per the initial iterations of the rules).

This approach has caused concern for some of our members and while there is a complete understanding and appreciation that ultimately there will be no UK tax payment requirements, the potential of penalty notices means that they cannot chose to do nothing at this stage and at the very least need to consider either to file nil returns for any entity registered for UK CT or notify HMRC to treat the entity as dormant for the time being, before eventually deregistering the entity when the new regulations are laid. Similarly, an issue also arises for the 30-day notification requirement under the NRCG rules for any offshore entity not already registered for UK CT purposes, even though the entity will be out of scope of the rules once the new regulations take effect.

With support from members we have set out a number of common scenarios that members face as a result of the various changes in rules to date:

- Registered for UK CT, but no chargeable disposals to date
- Registered for UK CT, UK tax paid and tax filing done before changes to the rules were announced. Tax reclaimable
- Registered for UK CT and have made some disposals to date, UK tax theoretically due

- Not registered, but 30-day condition for registering triggered by a disposal
- Not registered, but may have disposals between now and April 2021 which are expected to fall out of scope following adoption of the Amendment as drafted

This is not an exhaustive list and individual firms will have facts and circumstances which require different levels of comfort to allay their compliance concerns.

Our Ask: We request HMRC to consider any approach which can alleviate the need to submit nil returns for entities registered under the current rules but which will no longer be within the scope of UK taxes due to these changes, as this will ensure administrative easement for taxpayers and HMRC. We understand from our discussion with HMRC Policy teams that they recognise these issues and while these issues cannot be solved by individual compliance or policy units, the matter has been raised with dedicated Administrative Policy Leads to identify and support a possible solution. We would be very happy to participate in further discussions and offer our help and support in finding an appropriate solution to this issue.

Conclusion

We would once again like to thank HMRC for introducing the portfolio exemption through the proposed legislation and would welcome any opportunity to discuss these changes or our comments further. If you have any questions or would like to discuss any aspects of this letter, please contact Anshita Joshi on Anshita.joshi@theia.org.