

CLIENT ALERT

New UK Tax Regime for Qualifying Asset Holding Companies

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On 20 July 2021 the UK government published draft legislation for a new tax regime for qualifying asset holding companies (**QAHCs**), which is intended to come into force on 1 April 2022.

The draft legislation follows two rounds of consultation on the tax treatment of asset holding companies in fund structures, and forms part of the UK government's wider review of the UK funds regime. The aim of this review is to enhance the UK's competitiveness as a location for asset management and investment funds in order to compete with other jurisdictions (such as Luxembourg) commonly used by investment managers.

Overall, the objective of the new QAHC regime is to tax investors in QAHCs broadly as if they had invested in the underlying assets directly and to ensure that the intermediate holding companies pay no more tax than is proportionate to the activities they perform; in doing so, the regime addresses some of the most significant tax issues which currently exist when considering the UK as an asset holding jurisdiction.

Tax Advantages

A QAHC will benefit from quite generous tax advantages, which broadly look to put investors, from a tax perspective, in the position they would otherwise be in if they held the underlying investments directly.

In particular, the key features of the QAHC regime include:

- exemption on capital gains on disposal of "shares", including interests in a company which has no share capital, except where the company derives 75% or more of its value from UK land.

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- exemption on capital gains on overseas property.
- exemption of profits from an overseas property business where those profits are subject to tax in an overseas jurisdiction.
- exemption from withholding tax on interest payments to investors in the QAHC.
- deductibility of certain interest payments that would otherwise be disallowed as distributions (for example, interest paid on profit participating loans).
- capital, rather than income, treatment on buybacks of shares by the QAHC.
- exemption from stamp duty and Stamp Duty Reserve Tax on the repurchase by a QAHC of its own shares and loan capital (but no exemption on transfer of shares in the QAHC).

The range of reliefs available for QAHCs should therefore address many of the main tax obstacles which currently exist in considering the UK as a jurisdiction for locating asset holding companies and, helpfully, the form of these reliefs is currently relatively simple.

Eligibility

The regime is intended to be available only to investment arrangements that involve the pooling of investor funds with professional investment managers. As such, to be eligible for the regime, a company must be UK tax resident and meet the following conditions:

- **Ownership:** The company must be at least 70% owned by “Category A investors”, which include other QAHCs, diversely owned funds managed by regulated managers, and certain institutional investors. In respect of managed funds, it is expected that the final legislation will include an additional condition to require the fund manager to meet an independence test.
- **Activities:** The main activity of the company must be investing its funds with the aim of spreading investment risk and giving investors in the company the benefit of the results of the management of its funds. If the company carries out other activities (for example, trading), these activities must not be carried out “to any substantial extent”.
- **Other investment entities:** The company must not be a REIT and none of the company’s equity securities can be listed or traded on a recognised stock exchange or any other public market or exchange.

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- **Election:** A company meeting the other eligibility criteria must elect into the regime if it wishes to be treated as a QAHC.

The eligibility criteria should encompass most holding companies established solely by investment funds or other institutional investors co-investing alongside investment funds. However, care will need to be taken that the 30% limit on non-Category A investors is not exceeded in more complicated cases, for example, where non-qualifying institutional investors or carried interest holders participate in investments at the level of the holding company.

What next?

The draft legislation only provides the preliminary outline for the new framework for taxing QAHCs and focuses on the eligibility conditions for a company to be a QAHC. The government is still considering certain other issues (including specific compliance requirements and the interaction of the QAHC regime with existing employment-related securities rules), and so we expect to see further draft legislation published later this year.

The draft legislation is now open for technical consultation, closing on 14 September 2021, following which it is expected the legislation will be included in Finance Bill 2021-22 to have effect from 1 April 2022.

In addition, as part of the UK government's wider review of the UK funds regime, a wider call for evidence on the funds regime closed in April 2021, on which the government's response is awaited, and the timing of publication of a previously announced consultation on the VAT treatment of fund management fees is currently unknown.

Final Thoughts

There are, of course, many considerations beyond tax which go into deciding where to establish investment holding structures. However, the details published to date indicate that the new QAHC regime should address many of the most significant tax roadblocks faced in considering a UK holding structure, and it is a welcome and promising development towards making the UK a viable investment holding jurisdiction.

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