HMRC - CFM98020 - i-Avoidance: Commencement And Exceptions

F(No.2)A17/SCH10/PARA34

Arrangements made before commencement

The RAAR can apply to arrangements entered into before the corporate interest restriction rules come into force if a main purpose is to ensure that a tax advantage related to the operation of those rules will arise following commencement.

Arrangements that accelerate deductions

However, there is an exclusion (F(No.2)A17/SCH10/PARA34(3)) for certain arrangements that merely accelerate deductions so that they are paid and brought into account as deductions for a period prior to commencement, and in consequence of that fact there is a reduced interest restriction post-commencement. This is intended to cover two scenarios, as illustrated by the examples below.

This exception is a limited one. It would not, for example, apply if a company sought to avoid interest restrictions by prepaying an amount that would otherwise become tax deductible after commencement if the effect of that prepayment would be to replace interest expense with some other form of deduction after commencement that is not within scope of the interest restriction rules.

Example 1: Arrangements that accelerate interest deductions

For example, assume that a company has previously had a deduction for accrued interest disallowed because the late paid interest rules in CTA09/PT5 apply, and that if the payment is made post-commencement it will be subject to interest restriction. To avoid this the company may arrange to pay the interest pre-commencement to avoid the post-commencement restriction.

There is a tax advantage because as a result of entering into the arrangement the company is no longer subject to restriction, and it was a main purpose to secure that advantage. However, the RAAR will not apply because the effect of the arrangement is to accelerate the deduction so as to reduce the amount of interest that will accrue following commencement.

Example 2: Arrangements that accelerate other deductions and in consequence increase interest capacity

A company accelerates payment of a pension contribution so that it is made before 1 April 2017 and in consequence its post-commencement EBITDA (and hence interest capacity) is not reduced by the deduction for the contribution. This arrangement has the effect of reducing the amount of interest restriction post-commencement and a main purpose of accelerating the payment was to secure that outcome. However, the RAAR will not apply because of the exception for accelerated payments.

Commercial restructuring arrangements in connection with commencement

There is a separate exclusion (F(No.2)A17/SCH10/PARA34(5)) from the RAAR for certain commercial restructuring arrangements entered into connection with the commencement of the rules that do no more than eliminate a tax disadvantage that could not originally have been anticipated when that structure was put in place.

This covers two scenarios:

Arrangements to bring loan relationships into the charge to Corporation Tax which would, absent the interest restriction rules, result in significantly more Corporation Tax becoming payable.

Commercial steps taken to restructure arrangements that would not have been entered into if the interest restriction rules had been in place at the time of the original arrangements.

Note that this exclusion is not limited to arrangements entered into before commencement or entered before another particular date; the arrangements may be entered into at a date considerably after commencement.

(A) Arrangements that would have resulted in significantly more corporation tax becoming payable

By virtue of paragraph 34(6)(a), the RAAR would not apply to a group that effectively transferred interest income from a controlled foreign company (CFC) to a UK group company in order to avoid being subject to both a CFC charge and an interest restriction.

Prior to the restructuring some or all of the interest income of the CFC could be subject to a CFC charge. By transferring this income stream to a UK group company, it will in future be subject to Corporation Tax instead of a CFC charge. It will also become tax-interest income of the group, reducing the aggregate net tax-interest expense. This could potentially reduce any interest restriction by the amount of interest income.

(B) Arrangements that are designed to secure the benefit of a relief expressly conferred

By virtue of paragraph 34(6)(b), the RAAR would not apply to a restructuring that is designed to allow a group to be able to benefit from

Designed to secure, in a way that is wholly consistent with its policy objectives, the benefit of a relief expressly conferred by a provision of the interest restriction rules; and

Is effected by taking only ordinary commercial steps in accordance with generally prevailing commercial practice.

The reference to “a relief expressly conferred by a provision” should be interpreted widely. In particular, it would cover:

Ensuring that a company genuinely falls to be a Qualifying Infrastructure Company (QIC) under the infrastructure rules.

Ensuring that a tax-interest payment made by a QIC genuinely falls to be paid to a third party or to another QIC and so can be excluded under the infrastructure rules.

Ensuring that a relevant expense amount paid by a group genuinely qualifies to be included within qualifying net group-interest expense (QNGIE) under the group ratio method.

This exclusion from the RAAR does not apply to companies contriving to fall within a particular provision - it is necessary to genuinely fall within the provision in question in a way that is wholly consistent with its policy objectives.

The reference “commercial steps in accordance with generally prevailing commercial practice” should also be interpreted widely given the wide range of transactions which regularly undertaken by corporate entities for commercial reasons. It would include, for example, typical transactions involving the transfer of ownership of companies, the refinancing of debt and separating out assets and businesses from a company.

It should be noted that this exclusion is intended to deal with cases where a group has previously entered into a particularly structure for commercial reasons without anticipating the corporate interest restriction rules and where now, following the introduction of the corporate interest restriction rules, it wishes to restructure so to give a more beneficial tax outcome under the rules. However, the restructuring is likely to be purely tax driven, given that the commercial objectives are already being achieved.

Consideration should be given as to whether the new structure is such that, had it been entered from the start, achieving the tax benefits would have been considered incidental to the commercial objectives, and not a main purpose in their own right. This exclusion from the RAAR is only likely to apply where the tax benefits achieved are incidental and secondary to the original commercial objectives achieved by the structure.

Example 3

The RAAR would not apply to cases where a group restructures so to fall within the public infrastructure rules in a way wholly consistent with the policy of those rules. For example, this could involve moving subsidiaries that cannot meet the conditions to be qualifying infrastructure companies (QICs) to a separate part of the group structure, creating a sub-group of companies that can qualify as QICs.

Example 4

The RAAR would not apply to cases where a highly leveraged group refinances debt that does not qualify to be included within qualifying net group-interest expense with debt that does qualify. For example, a group may refinance perpetual debt with debt with a fixed term of less than 50 years.

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