# Proposals for a UK Asset Holding Company Regime

On 25 February 2021, the UK government's second stage consultation on a new tax regime for a UK asset holding company ("UK AHC") finished. The government's objective is to establish a regime for a UK AHC that can be used as an intermediate asset-holding entity in private fund structures (e.g., private equity funds, credit funds and real estate funds) and that will provide a credible UK equivalent to AHCs in other jurisdictions, such as the Irish section 110 company and the Luxembourg S.a.r.l. However, it remains a guiding principle of the government's approach that the use of a UK AHC should not confer any UK tax advantages over direct investment — investors (whether UK or non-UK) should be in roughly the same tax position when investing via a UK AHC as they would be in if they had held the relevant investments directly.

The second stage consultation identified and sought solutions for a number of key obstacles that had been identified to the establishment of a usable and attractive regime for a UK AHC. One significant problem that the government has posed for itself is the attempt to create a UK AHC regime that will facilitate a UK AHC holding investments across a wide variety of asset classes. The current proposals envisage that the UK AHC might be used in the contexts of private equity, securitization, real estate and private or alternative credit. The creation of a UK AHC regime that will enable a UK AHC to be a suitable vehicle in all these different settings — particularly real estate investing — but which does not create opportunities for unacceptable tax avoidance gives rise to a number of specific challenges:

1. *Capital Gains and Investor Taxation*. The government's current proposals are for a broad participation exemption for capital gains at the level of the UK AHC itself. However, the second stage consultation proposes adding a 'tracing' methodology, so that investors are treated as having themselves realised their respective shares of capital gains of the UK AHC (and taxed on those attributed capital gains according to their particular UK tax status). This gives rise to difficult issues where non-UK resident investors invest in a UK AHC which realises capital gains from disposals of direct or indirect interests in both UK land and non-UK land. It is far from clear how a UK AHC regime could achieve the "right" result of taxing non-UK resident investors on their share of UK AHC gains from disposals of interests in UK land, but not on their share of UK AHC gains from disposals of interests in non-UK land.

2. *Withholding Taxes*. AHCs in other jurisdictions — such as Ireland and Luxembourg — are typically funded by some form of profit-participating debt, in order to enable a tax-efficient means of profit extraction. These jurisdictions do not impose withholding tax on interest payments on this debt funding. The United Kingdom, by contrast, imposes a 20% withholding tax on interest on unlisted debt in many cases. A useable UK AHC regime will therefore need to provide an exemption from UK withholding tax on interest, particularly given that a UK AHC is likely to be utilised by funds or other widely held collective investment vehicles which are unlikely to be able to take advantage of double tax treaties with the United Kingdom to eliminate or mitigate the UK withholding tax.

3. *Value Added Tax*. Without the benefit of special rules, a UK AHC would be subject to UK VAT on its management fees. By contrast, management fees for AHCs in competitor jurisdictions such as Luxembourg and Ireland are generally exempt from VAT. Solving this VAT issue is therefore a key requirement before the United Kingdom can introduce a useable and effective UK AHC regime. However, current indications are not encouraging, as the government has announced that the question of VAT charged to a UK AHC will be considered as part of the United Kingdom's ongoing wider funds review.

The government originally intended to include legislation for the introduction of a UK AHC in Finance Bill 2021. However, it would seem that the difficulties of introducing an effective and attractive UK AHC regime at the same time as addressing the government's long-standing concerns over tax avoidance, erosion of the tax base and preservation of revenues in a time of economic downturn are proving difficult to overcome and no draft legislation has yet been published.