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UK Tax Alert

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Fund Board Meetings in the United Kingdom

The Background

As part of the Budget 2013, U.K. Treasury announced the U.K.'s investment management strategy.[1] The strategy is aimed at enhancing the U.K.'s position as a global leader in the investment management industry and protecting the U.K.'s position as Europe's leading centre for fund management.

One particular focus of the strategy concerns U.K. tax residence. To date, great care has been taken to ensure that funds incorporated outside of the U.K. do not become U.K. tax resident. Funds will typically:

- appoint a majority of non-U.K. resident individuals to their board
- hold all board meetings outside of the U.K.
- ensure that the fund's board cannot be chaired by a U.K. resident and that a board decision cannot be made solely by U.K. residents.

If a fund incorporated outside of the U.K. were to become U.K. resident, it could be subject to U.K. corporation tax on its worldwide income and gains. Adjustments to the operations of a fund that does become U.K. resident, to correct any inadvertent breach of accepted practice, may also crystallise exit charges payable to the U.K. Treasury.

One of the U.K. Treasury's concerns is that the fear of inadvertently making a non-U.K. fund resident in the U.K. might dissuade funds from appointing a U.K.-based manager, and also cause uncertainty for those funds that are already managed from within the U.K. In order to assuage this concern, the investment management strategy document contains a proposal to introduce rules protecting certain U.K.-managed funds from becoming U.K. tax resident. Her Majesty's Revenue & Customs (HMRC) is currently consulting on exactly how this is achieved.

https://www.gov.uk/government/consultations/residence-of-offshore-funds-extending-the-scope-of-section-363a-taxation-act-2010

Overview of Proposed Changes

HMRC's consultation is concerned with offshore funds that are managed from the U.K. HMRC's proposal aims to provide legislative certainty that managing such funds from the U.K. will not cause them to be treated as U.K. tax resident.

[1] The strategy document can be found at https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/221896/uk_investment_management_strategy.pdf

The proposed method of achieving the above is to extend current statutory protections to:

- non-UCITS[2] funds that fall within the definition of an offshore fund for U.K. tax purposes, and
- which have a U.K.-based manager that is either (i) authorised by the Financial Conduct Authority as an Alternative Investment Fund Manager (AIFM) or (ii) a U.K. branch of an AIFM that has been authorised in another member state.

Commentary

Although there has been some market commentary on the potential impact of HMRC's proposal, there are a number of key issues that we believe market participants should focus on, for example:

- Not all non-U.K. funds that are managed from the U.K. will be able to avail themselves of the statutory protection as proposed, as they will have to be offshore funds. This term has a specific meaning under U.K. tax rules and, for example, certain closed-ended funds do not fall within the definition.
- U.K. managers that are delegates of U.S. managers (where the U.S. manager is the AIFM), for example, would not meet the criteria, and so not afford any offshore funds that they manage residence protection under the current proposal.
- If the criteria above are met, then it would be possible to appoint a majority of U.K. residents to a fund's board and/or hold board meetings in the U.K. without causing the fund to be U.K. resident.

While HMRC's proposal is potentially significant, it might not have a substantial impact on existing practices within the hedge fund management industry for a number of reasons. Some of these reasons include:

- Existing central management and control (CMC) practices may still need to be observed for non-U.K. tax reasons. Non-U.K. funds requiring access to the double taxation treaties of their incorporation jurisdiction may need to hold board meetings locally. They may also have to appoint national directors to ensure they are treaty resident in their incorporation jurisdiction.
- Consideration would have to be given to whether, without changes to the U.K. Value Added Tax (VAT) rules, a practice of holding U.K. board meetings could bring fees charged to offshore entities into the charge to U.K. VAT.
- If existing non- U.K. directors of a fund entity are required to attend board meetings held in the U.K., the employment tax (including Pay As You Earn) and National Insurance contributions implications would need to be considered.

[2] Undertakings for Collective Investment in Transferable Securities.

- Non-U.K. resident directors attending board meetings held in the U.K. may have to file a U.K. personal tax return, whereas they may well not have had to do so otherwise.

- Consideration would need to be given, on a board-meeting-by-board-meeting basis, to any stamp tax issues that might otherwise not arise. For example, executing instruments relating to fund investments, such as the transfer of non-U.K. shares, at a U.K. board meeting.

- Because the statutory protection which HMRC proposes in the consultation document is available only in respect of offshore funds, non-U.K. fund management entities (incorporated in the Cayman Islands or Malta, for example) would not be within scope. Therefore, managers may prefer to consistently follow general principles (as regards avoiding U.K. tax residence) rather than differ in approach between fund and manager.

Next Steps

HMRC's consultation period closes on October 14, 2013. A summary of responses together with draft legislation will be published in autumn/fall 2013, and so final legislation is anticipated in Finance Bill 2014 (which will likely be announced in March 2014).

If you would like to discuss the above, including how you may wish to contribute to the consultation, please do not hesitate to contact any member of the team below.

Contact Information

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