STATUTORY INSTRUMENTS

2007 No. 3540

CORPORATION TAX

The Real Estate Investment Trusts (Breach of Conditions) (Amendment) Regulations 2007

Made - - - -	*17th December 2007*
Laid before the House of Commons - - - -	*17th December 2007*
Coming into force - -	*7th January 2008*

The Treasury make the following Regulations in exercise of the powers conferred by sections 116, 129(2)(a) and (b), 129(3) and 144 of the Finance Act 2006(**1**).

Citation, commencement and effect

1.—(1) These Regulations may be cited as the Real Estate Investment Trusts (Breach of Conditions) (Amendment) Regulations 2007 and shall come into force on 7th January 2008.

(2) These Regulations have effect in relation to accounting periods beginning on or after 1st January 2007.

Amendments to the Real Estate Investment Trusts (Breach of Conditions) Regulations 2006

2. The Real Estate Investment Trusts (Breach of Conditions) Regulations 2006(**2**) are amended as follows.

Amendment of regulation 1

3.—(1) Regulation 1(citation, commencement and interpretation) is amended as follows.

(2) After paragraph (1) insert—

"(1A) In these Regulations—

(a) a reference to Part 4 is a reference to Part 4 of the Finance Act 2006,

(b) a reference to a section (without more) is a reference to that section of the Finance Act 2006, and

(**1**) 2006 c. 25; section 116 was amended by paragraph 7 of Schedule 17 to the Finance Act 2007 (c. 11).
(**2**) S.I. 2006/2864.

(c) a reference to a paragraph of Schedule 17 is a reference to that paragraph of Schedule 17 to the Finance Act 2006.".

(3) In paragraph (2)—

(a) in the definition of "*MCT*" omit "and" at the end of paragraph (b);

(b) omit "a reference (without more) to a numbered provision of the Finance Act 2006, is a reference to the provision bearing that number."; and

(c) insert the following definitions at the appropriate places—

""JV Regulations" means the Real Estate Investment Trusts (Joint Ventures) Regulations 2006(**3**);";

""JVG Regulations" means the Real Estate Investment Trusts (Joint Venture Groups) Regulations 2007(**4**);";

""specified accounting period" means the accounting period referred to in regulation 7(1)(a);";

""UK property rental business" means the property rental business of a UK resident company or the property rental business in the United Kingdom of a company which is not a UK resident company; and"; and

""UK resident company" means a company which is resident in the United Kingdom, and is not resident in another place in accordance with the law of that place relating to taxation.".

(4) In paragraph (3) after "6," insert "7, 7A, 7B,".

Amendment of regulation 2

4. For the heading to regulation 2 (Breach of conditions for company — take-overs) substitute "Breach of conditions for company — take-overs and demergers".

Substitution of regulation 7

5. For regulation 7 (breach of balance of business conditions) substitute—

"**Initial breach of Condition 2 in section 108(3)**

7.—(1) This regulation applies to a company if—

(a) the company gives a notice under section 109 specifying an accounting period from the beginning of which Part 4 is to apply to the company (the "specified accounting period"), and

(b) at the beginning of the specified accounting period, the company is in breach of Condition 2 in section 108(3).

(2) Part 4 shall apply to the company from the beginning of the specified accounting period if, at the beginning of the following accounting period, the company satisfies the requirements of Condition 2 in section 108(3).

(3) If paragraph (2) applies, the company's breach of Condition 2 in section 108(3) at the beginning of the specified accounting period shall not be taken into account for the purposes of paragraphs (4) and (5) of regulation 7B.

(4) Part 4 ceases to apply if—

(**3**) S.I. 2006/2866.
(**4**) S.I. 2007/3425.

(a) the company does not satisfy the requirements of Condition 2 in section 108(3) at the beginning of the following accounting period, and

(b) the Commissioners think, for the purposes of section 129(2)(c), that a breach of that requirement is so serious that Part 4 should cease to apply to the company.

(5) For the purposes of paragraph (4), section 129 shall be modified by substituting for subsection (5)—

"(5) Where a notice is given to a company in respect of an event occurring during the accounting period specified in the company's section 109 notice, this Part shall be taken to have ceased to apply to the company on the first day of that accounting period.".

Tax charge for specified accounting period

7A.—(1) This regulation applies if regulation 7(1) and (2) apply.

(2) A company to which this regulation applies shall be chargeable to corporation tax under Case VI of Schedule D on an amount of notional income calculated in accordance with this regulation.

(3) The notional income shall be treated as arising at the end of the specified accounting period—

(a) to C (residual), or

(b) to the company as a member of G (residual).

(4) The notional income is—

$$\left(\frac{\text{Market Value of Assets}}{\text{Tax Rate}}\right) \times 2\% - \text{Entry Charge Notional Income}$$

(5) In paragraph (4)—

"Market Value of Assets" means—

(a) the aggregate market value of assets involved in the UK property rental business of C (tax exempt), or

(b) if the company is a member of a group to which Part 4 applies, the aggregate market value of assets involved in the UK property rental business of G (property rental business),

together with—

(c) if the company is a venturing company or the principal company of a venturing group to which the JV Regulations apply, the value representing the proportion of the beneficial interest which that company has in the aggregate market value of the assets of the UK property rental business of the joint venture company, or

(d) if the company is a venturing company or the principal company of a venturing group to which the JVG Regulations apply, the value representing the proportion of the beneficial interest which that company has in the aggregate market value of the assets of the UK property rental business of JVG (property rental business),

and for the purposes of this definition, the market value of assets is to be determined as at the end of the specified accounting period (ignoring any asset of negative market value);

"Tax Rate" means—

(a) the percentage rate at which C (residual) is chargeable to tax on profits, or

(b) the percentage rate at which the company, as a member of G (residual), is chargeable to tax on profits; and

"Entry Charge Notional Income" means—

(a) the notional income calculated in accordance with section 112(3) which is chargeable on the company, or

(b) the notional income calculated in accordance with section 112(3) as modified by paragraph 11(1)(c) of Schedule 17 which is chargeable on the members of the group,

together with—

(c) if the company is a venturing company or the principal company of a venturing group to which the JV Regulations apply, the notional income calculated in accordance with section 112(3) as modified by regulation 7(3) or 13(4) of the JV Regulations, which is chargeable on the joint venture company, or

(d) if the company is a venturing company or the principal company of a venturing group to which the JVG Regulations apply, the notional income calculated in accordance with section 112(3) as modified by the JVG Regulations, which is chargeable on the members of the joint venture group.

(6) If the company holds an asset at the beginning of the specified accounting period but disposes of that asset during that accounting period, the Entry Charge Notional Income shall be reduced by an amount calculated as follows—

$$\left(\frac{\text{Asset Market Value}}{\text{Aggregate Market Value}}\right) \times \text{Entry Charge Notional Income}$$

(7) In paragraph (6)—

"Asset Market Value" means the market value of the asset at the beginning of the specified accounting period;

"Aggregate Market Value" means the aggregate market value of assets treated as sold and reacquired under section 111(2), or section 111(2) as modified by paragraph 9(2) of Schedule 17, (ignoring any asset of negative market value); and

"Entry Charge Notional Income" has the same meaning as in paragraph (4).

(8) No loss, deficit, expense or allowance may be set off against notional income or tax arising under this regulation.

Breach of balance of business conditions

7B.—(1) This regulation applies to a company if—

(a) Part 4 applies to the company, and

(b) the company does not satisfy the requirements of Condition 1 in section 108(2)(**5**) or Condition 2 in section 108(3) in respect of any accounting period subsequent to the specified accounting period.

(2) If the company does not satisfy the requirements of Condition 1 in section 108(2), but the profits arising from the tax-exempt business referred to in that condition are not less than 50% of the company's total profits for that accounting period, Part 4 shall continue to apply to the company.

(**5**) Section 108(2) was amended by paragraph 4 of Schedule 17 to the Finance Act 2007.

(3) If the company does not satisfy the requirements of Condition 2 in section 108(3), but the value of the assets involved in the tax-exempt business referred to in that condition has not fallen below 50% of the total value of assets held by the company, Part 4 shall continue to apply to the company.

(4) But, if the company does not satisfy the requirements of Condition 1 in section 108(2) or Condition 2 in section 108(3) in any three consecutive accounting periods, the breach is not to be considered as minor and the company may not rely upon this regulation for the purposes of section 129(2)(a).

(5) Subject to paragraph (4), if a breach of Condition 1 in section 108(2) or Condition 2 in section 108(3) lasts for more than one, but not more than two, consecutive accounting periods, it constitutes only one breach for the purposes of paragraph (7).

(6) The specified accounting period is not to be taken into account in reckoning the consecutive accounting periods mentioned in paragraph (4) and in paragraph (5).

(7) For the purposes of section 129(2)(a)—

(a) the specified number of occasions on which the company can rely on this regulation is—

(i) two in respect of a breach of Condition 1 in section 108(2), and

(ii) two in respect of a breach of Condition 2 in section 108(3); and

(b) the specified period is the ten year period beginning on the day on which the company first failed to satisfy Condition 1 in section 108(2) or Condition 2 in section 108(3) and ending immediately before the tenth anniversary of that day; and

(c) for the purposes of paragraph (b), the company shall be treated as having first failed to satisfy Condition 1 in section 108(2) on the last day of the accounting period in which its profits are assessed for the purposes of that condition.".

Amendment of regulation 8

6. In regulation 8 (multiple breaches of separate conditions) for paragraph (2) substitute—

"(2) For the purposes of section 129(2)(a), the specified number of occasions on which the company can rely on regulation 2, 3, 5 or 7B of these Regulations is four.

(3) In reckoning the number of breaches of sections 106 to 108(**6**) the following are not to be taken into account—

(a) breaches of Condition 3 in section 106(5) or Condition 4 in section 106(6) in consequence of a company to which Part 4 applies becoming part of a group (or of another group) to which Part 4 applies;

(b) breaches of Condition 3 in section 106(5) or Condition 4 in section 106(6) in respect of which a company has relied upon section 109(3), (4) and (5);

(c) breaches of Condition 1 in section 108(2) in the specified accounting period; and

(d) breaches of Condition 2 in section 108(3) at the beginning of the specified accounting period.

(4) For the purposes of section 129(2)(a) the specified period is the ten year period beginning on the day on which the company first failed to satisfy any of the conditions set out in section 106(5) or (6), 107 or 108 and ending immediately before the tenth anniversary of that day.

(**6**) Sections 106 and 107 were respectively amended by paragraphs 2 and 3 of Schedule 17 to the Finance Act 2007.

(5) For the purposes of paragraph (4), the company shall be treated as having first failed to satisfy Condition 1 in section 108(2) on the last day of the accounting period in which its profits are assessed for the purposes of that condition.

(6) Any breach of Condition 1 in section 108(2) in the specified accounting period, or any breach of Condition 2 in section 108(3) at the beginning of the specified accounting period, shall be disregarded in determining the day on which the ten year period begins.".

Dave Watts
Frank Roy
Two of the Lords Commissioners for Her Majesty's Treasury

17th December 2007

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations amend the Real Estate Investment Trusts (Breach of Conditions) Regulations 2006 (S.I. 2006/2864) ("the principal Regulations").

These Regulations make provision for the consequences flowing from a breach of the conditions in Part 4 of the Finance Act 2006 (c. 25) ("the 2006 Act"), as amended by Schedule 17 to the Finance Act 2007 (c. 11).

Regulation 1 deals with the citation, commencement and effect. Authority for the retrospective effect of these Regulations is given by section 116(3A) of the 2006 Act which was inserted by paragraph 7 of Schedule 17 to the Finance Act 2007.

Regulation 2 introduces the amendments.

Regulation 3 amends regulation 1 of the principal Regulations.

Regulation 4 amends the heading to regulation 2 of the principal Regulations as a consequence of section 126A of the 2006 Act, inserted by paragraph 11 of Schedule 17 to the Finance Act 2007.

Regulation 5 substitutes new regulations 7, 7A and 7B for regulation 7 of the principal Regulations. New regulation 7 provides for the consequences of the breach of the asset condition in section 108(3) of the 2006 Act in the accounting period specified in the company's notice under section 109 of the 2006 Act. New regulation 7A imposes a charge to tax on companies to which new regulation 7 applies. New regulation 7B provides for the consequences of the breach of the balance of business conditions in any accounting period following the accounting period specified in the company's notice under section 109 of the 2006 Act.

Regulation 6 amends regulation 8 of the principal Regulations and provides for the consequences of multiple breaches of separate conditions in different sections of Part 4.

A regulatory impact assessment for the introduction of the UK-REIT regime was published in March 2006 and is available on the website of HM Revenue and Customs at www.hmrc.gov.uk/ria and may be obtained by writing to the Ministerial Correspondence Unit, 1st Floor, HM Revenue and Customs, Ferrers House, P.O. Box 38, Castle Meadow Road, Nottingham, NG2 1BB.