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SCHEDULES

SCHEDULE A1

DETERMINATION OF PROFITS ATTRIBUTABLE TO PERMANENT ESTABLISHMENT: SUPPLEMENTARY PROVISIONS

PART 1

INTRODUCTION

Introduction

- 1 (1) The provisions of this Schedule have effect for supplementing section 11AA as regards the determination of the profits attributable to a permanent establishment in the United Kingdom of a company that is not resident in the United Kingdom (“the non-resident company”).
- (2) In this Schedule “the separate enterprise principle” means the principle in section 11AA(2) (read with subsection (3) of that section).

PART 2

GENERAL PROVISIONS

Transactions treated as taking place at arm’s length

- 2 In accordance with the separate enterprise principle, transactions between the permanent establishment and any other part of the non-resident company are treated as taking place on such terms as would have been agreed between parties dealing at arm’s length.

Application of general provision as to allowable deductions

- 3 (1) Section 11AA(4) (general provision as to allowable deductions) applies whether or not the expenses are incurred by, or reimbursed by, the permanent establishment.
- (2) The amount of expenses to be taken into account under section 11AA(4) is the actual cost to the non-resident company.

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Prohibition of deductions for payments in respect of intangible assets

- 4 (1) No deduction is allowed in respect of royalties paid, or other similar payments made, by the permanent establishment to any other part of the non-resident company in respect of the use of intangible assets held by the company.
- (2) This does not prevent a deduction in respect of any contribution by the permanent establishment to the costs of creation of an intangible asset.
- (3) In this paragraph “intangible asset” has the meaning it has for accounting purposes, and includes any intellectual property (as defined in paragraph 2(2) of Schedule 29 to the Finance Act 2002).

Prohibition of deductions for interest or other financing costs

- 5 (1) No deduction is allowed in respect of payments of interest or other financing costs by the permanent establishment to any other part of the non-resident company, except as provided by sub-paragraph (2).
- (2) The restriction in sub-paragraph (1) above does not apply to interest or other costs of financing that are payable in respect of borrowing by the permanent establishment in the ordinary course of a financial business carried on by it.
- (3) In sub-paragraph (2) “financial business” means any of the following—
- (a) banking, deposit-taking, money-lending or debt-factoring, or a business similar to any of those;
 - (b) dealing in commodity or financial futures.

Provision of goods or services for permanent establishment

- 6 (1) This paragraph applies where the non-resident company provides the permanent establishment with goods or services.
- (2) If the goods or services are of a kind that the company supplies, in the ordinary course of its business, to third parties dealing with it at arm’s length, the matter is dealt with as a transaction to which the separate enterprise principle applies.
- (3) If not, the matter is dealt with as an expense incurred by the non-resident company for the purposes of the permanent establishment.

PART 3

PROVISIONS APPLICABLE TO NON-RESIDENT BANKS

Application of this Part

- 7 (1) The provisions of this Part of this Schedule have effect where the non-resident company is a bank.

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“Bank” for this purpose has the meaning given by section 840A.

- (2) Nothing in this Part of this Schedule shall be read as preventing the application of principles similar to those provided for in this Part in applying the separate enterprise principle to a non-resident company that is not a bank.

Non-resident banks: transfer of financial assets

- 8 (1) In accordance with the separate enterprise principle, transfers of loans and other financial assets between the permanent establishment and any other part of the company are recognised only if they would have taken place between independent enterprises.
- (2) Such a transfer is not recognised where it cannot reasonably be considered that it is carried out for valid commercial reasons. For this purpose the obtaining of a tax advantage is not a valid commercial reason.

Loans by non-resident banks: attribution of financial assets and profits arising

- 9 (1) In accordance with the separate enterprise principle, loans and other financial assets, and profits arising from them, are attributed to a permanent establishment to the extent that they can reasonably be regarded as having been generated by the activities of the permanent establishment.
- (2) The following provisions have effect as regards the factors to be taken into account.
- (3) Particular account shall be taken of the extent to which the permanent establishment is responsible for—
- (a) obtaining the offer of new business;
 - (b) establishing the potential borrower’s credit rating and the risk involved in providing credit;
 - (c) negotiating the terms of the loan with the borrower;
 - (d) deciding whether, and if so on what conditions, to make or extend the loan.
- (4) Account may also be taken of the extent to which the permanent establishment is responsible for—
- (a) concluding the loan agreement and disbursing the proceeds of the loan;
 - (b) administering the loan (including handling and monitoring the service of it) and holding and controlling any securities pledged.
- (5) References in this paragraph to a financial asset include any financial risk in relation to a loan, or potential loan, that is capable of giving rise to fees or other receipts and for which the holding of capital is required (or would be required if the transaction were between parties at arm’s length).

Borrowing by non-resident banks: permanent establishment acting as agent or intermediary

- 10 (1) This paragraph applies where a permanent establishment—

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- (a) borrows funds for the purposes of another part of the non-resident company,
and
 - (b) in relation to that borrowing acts only as an agent or intermediary.
- (2) In such a case, in accordance with the separate enterprise principle—
- (a) the profits attributable to the permanent establishment, and
 - (b) the capital attributable to the permanent establishment under section 11AA(3),
- shall be that appropriate in the case of an agent acting at arm's length, taking into account the risks and costs borne by the establishment.

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