Taxation (International and Other Provisions) Act 2010

2010 CHAPTER 8

[F1PART 9A

CONTROLLED FOREIGN COMPANIES

[F1CHAPTER 4

THE CFC CHARGE GATEWAY: PROFITS ATTRIBUTABLE TO UK ACTIVITIES

Textual Amendments

F1 Pt. 9A inserted (17.7.2012) by Finance Act 2012 (c. 14), **Sch. 20 para. 1** (with ss. 56-58)

Modifications etc. (not altering text)

C1 Pt. 9A Ch. 4 applied (with modifications) by 2009 c. 4, s. 18HB (as substituted (with effect in accordance with Sch. 20 para. 55(2) of the amending Act) by Finance Act 2012 (c. 14), **Sch. 20 para. 6**)

371DA Introduction to Chapter

(1) Take the steps set out in section 371DB(1) to determine the CFC's profits falling within this Chapter for the purposes of step 2 in section 371BB(1) (the CFC charge gateway).

(2) In this Chapter references to the CFC's assumed total profits are to those profits excluding its non-trading finance profits and property business profits (if any).

(3) For the purposes of this Chapter—

(a) "the OECD Report" means the Report on the Attribution of Profits to Permanent Establishments of the Organisation for Economic Co-operation and Development ("OECD") dated 22 July 2010,

(b) terms used which are also used in the OECD Report have the same meaning as they have in the OECD Report,

(c) "the CFC group" means the CFC taken together with the companies with which it is connected as those companies may change from time to time,

(d) "the provisional Chapter 4 profits" has the meaning given at step 7 in section 371DB(1),

(e) "the relevant assets and risks" has the meaning given at step 1 in section 371DB(1), subject to any exclusions at step 2 or 6,

(f) "SPF" means a significant people function or a key entrepreneurial risk-taking function,

(g) an SPF is a "UK SPF" so far as the SPF is carried out in the United Kingdom—

(i) by the CFC, otherwise than through a UK permanent establishment, or

(ii) by a company connected with the CFC, and

(h) an SPF is a "non-UK SPF" so far as it is not a UK SPF.

(4) The Treasury may by regulations amend this Chapter as they consider appropriate to take account of any relevant document published by OECD from time to time.

(5) "Relevant document" means—

(a) a document which replaces, updates or supplements the report mentioned in subsection (3)(a), or

(b) a document which replaces, updates or supplements a document falling within paragraph (a) or a document which is a relevant document by virtue of this paragraph.

371DB The steps

(1) Here are the steps referred to in section 371DA(1).

The steps are to be taken in accordance with the principles set out in the OECD Report (so far as relevant).

Step 1 Identify the assets which the CFC has or has had, and the risks which the CFC bears or has borne, and from which amounts included in the CFC's assumed total profits have arisen. The identified assets and risks are called "the relevant assets and risks"

Step 2 Exclude from the relevant assets and risks any asset or risk to which subsection (2) applies (subject to subsections (3) and (4)).

Step 3 Identify the SPFs carried out by the CFC group which are relevant to—

(a) the economic ownership of the assets included in the relevant assets and risks, or

(b) the assumption and management of the risks included in the relevant assets and risks.

For this purpose, assume that the CFC group is a single company.

Step 4 Determine the extent to which the SPFs identified at step 3 are UK SPFs and the extent to which they are non-UK SPFs. If none of the SPFs is a UK SPF to any extent, then no profits fall within this Chapter and no further steps are to be taken.

Step 5 Assume that the UK SPFs determined at step 4 are carried out by a permanent establishment which the CFC has in the United Kingdom and, accordingly, determine the extent to which the assets and risks included in the relevant assets and risks would be attributed to the permanent establishment. For this purpose, assume that the non-UK SPFs determined at step 4 are all carried out by the CFC itself (if that is not otherwise the case).

Step 6 Exclude from the relevant assets and risks any asset or risk, or any assets or risks taken together, to which section 371DC applies.

Step 7 Re-determine the CFC's assumed total profits on the basis that the CFC—

(a) does not hold, or has not held, the assets included in the relevant assets and risks, and

(b) does not bear, or has not borne, the risks included in the relevant assets and risks,

so far as they would be attributed to the permanent establishment mentioned at step 5."The provisional Chapter 4 profits" are the CFC's assumed total profits so far as they are left out of the re-determined profits.

Step 8 Exclude from the provisional Chapter 4 profits any amounts which are required to be excluded by section 371DD, 371DE or 371DF. The remaining profits (if any) fall within this Chapter.

(2) This subsection applies to an asset or risk if the CFC's assumed total profits are only negligibly higher than what they would be if the CFC—

(a) did not hold, or had not held, the asset to any extent at all, or

(b) did not bear, or had not borne, the risk to any extent at all.

(3) The total number of assets and risks which may be excluded at step 2 in subsection (1) is limited as follows.

(4) As well as applying to each asset and risk separately, subsection (2) must also apply to all the assets and risks included in the total number taken together.

371DC Exclusion: UK activities a minority of total activities

(1) For the purposes of step 6 in section 371DB(1), this section applies to an asset or risk included in the relevant assets and risks if amount A is no more than 50% of amount B.

(2) Amount A is the total of—

(a) the gross amounts (that is, the amounts before deduction of expenses or transfers to or from reserves) of the CFC's income which would not have become receivable during the accounting period had the CFC—

(i) not held the asset, or

(ii) not borne the risk,

so far as it would be attributed to the permanent establishment mentioned at step 5 in section 371DB(1), and

(b) the additional expenses which the CFC would have incurred during the accounting period had the CFC—

(i) not held the asset, or

(ii) not borne the risk,

so far as it would be so attributed.

(3) Amount B is the total of—

(a) the gross amounts (that is, the amounts before deduction of expenses or transfers to or from reserves) of the CFC's income which would not have become receivable during the accounting period had the CFC—

(i) not held the asset to any extent at all, or

(ii) not borne the risk to any extent at all, and

(b) the additional expenses which the CFC would have incurred during the accounting period had the CFC—

(i) not held the asset to any extent at all, or

(ii) not borne the risk to any extent at all.

(4) Subsection (5) applies if it is not reasonably practicable to separate a number of assets or risks included in the relevant assets and risks for the purpose of determining amounts A and B in relation to each of those assets or risks separately.

(5) In subsections (1) to (3) references to an asset or risk are to be read as references to those assets or risks taken together.

371DD Exclusion: economic value

(1) Subsection (2) applies if—

(a) an asset or risk is included in the relevant assets and risks,

(b) the SPFs which are relevant to the economic ownership of the asset, or the assumption and management of the risk, are wholly or partly UK SPFs as determined at step 4 in section 371DB(1), and

(c) as a result of that determination, an amount is included in the provisional Chapter 4 profits.

(2) The amount is to be excluded from the provisional Chapter 4 profits if—

(a) the net economic value to the CFC group which results from the holding of the asset, or the bearing of the risk, exceeds what that value would have been had the asset been held, or the risk been borne, solely by UK resident companies connected with the CFC, and

(b) the relevant non-tax value is a substantial proportion of the excess value mentioned in paragraph (a).

(3) "Net economic value" does not include any value which derives (directly or indirectly) from the reduction or elimination of any liability of any person to tax or duty imposed under the law of any territory outside the United Kingdom.

(4) "The relevant non-tax value" is the excess value mentioned in subsection (2)(a) so far as it does not derive (directly or indirectly) from the reduction or elimination of any liability of any person to tax or duty imposed under the law of the United Kingdom.

(5) Subsection (6) applies if—

(a) there are SPFs which are relevant to the economic ownership of a number of assets, or the assumption and management of a number of risks, included in the relevant assets and risks, and

(b) it is not reasonably practicable to separate those assets or risks for the purpose of determining the extent to which the SPFs are relevant to the economic ownership of each of those assets, or the assumption and management of each of those risks, separately.

(6) In subsections (1) and (2) references to an asset or risk are to be read as references to those assets or risks taken together.

371DE Exclusion: independent companies' arrangements

(1) Subsection (2) applies if—
- (a) an asset or risk is included in the relevant assets and risks,
- (b) the SPFs which are relevant to the economic ownership of the asset, or the assumption and management of the risk, are wholly or partly UK SPFs as determined at step 4 in section 371DB(1),
- (c) as a result of that determination, an amount is included in the provisional Chapter 4 profits, and
- (d) the UK SPFs are carried out by companies connected with the CFC under arrangements made between the CFC and those companies.

(2) The amount is to be excluded from the provisional Chapter 4 profits if it is reasonable to suppose that, were the SPFs which are UK SPFs not to be carried out by companies connected with the CFC, the CFC would enter into arrangements with companies not connected with the CFC which—
- (a) would be structured in the same way as the arrangements mentioned in subsection (1)(d), and
- (b) would, in relation to the CFC's business, have the same commercial effect as those arrangements.

(3) Subsection (4) applies if—
- (a) there are SPFs which are relevant to the economic ownership of a number of assets, or the assumption and management of a number of risks, included in the relevant assets and risks, and
- (b) it is not reasonably practicable to separate those assets or risks for the purpose of determining the extent to which the SPFs are relevant to the economic ownership of each of those assets, or the assumption and management of each of those risks, separately.

(4) In subsection (1) references to an asset or risk are to be read as references to those assets or risks taken together.

371DF Exclusion: trading profits (the basic rule)

(1) All trading profits are to be excluded from the provisional Chapter 4 profits if the following conditions are met—
- (a) the business premises condition (see section 371DG),
- (b) the income condition (see section 371DH),
- (c) the management expenditure condition (see section 371DI),
- (d) the IP condition (see section 371DJ), and
- (e) the export of goods condition (see section 371DK).

(2) Trading profits are also to be excluded from the provisional Chapter 4 profits in accordance with section 371DI(7) and (8) (so far as applicable).

(3) This section is subject to section 371DL (anti-avoidance).

371DG Exclusion: trading profits (business premises condition)

(1) This section applies for the purposes of section 371DF(1)(a).

(2) The business premises condition is met if, at all times during the accounting period, the CFC has in the territory in which it is resident for the accounting period premises—

(a) which are, or are intended to be, occupied and used with a reasonable degree of permanence, and

(b) from which the CFC's activities in that territory are wholly or mainly carried on.

(3) "Premises" means—

(a) an office, shop, factory or other building or part of a building,

(b) a mine, an oil or gas well, a quarry or other place of extraction of natural resources, or

(c) a building site or the site of a construction or installation project, but only if the building work or project has a duration of at least 12 months.

371DH Exclusion: trading profits (income condition)

(1) This section applies for the purposes of section 371DF(1)(b).

(2) The income condition is met if no more than 20% of the CFC's relevant trading income derives (directly or indirectly) from—

(a) UK resident persons, or

(b) UK permanent establishments of non-UK resident companies.

(3) For the purposes of subsection (2) the CFC's "relevant trading income" is its trading income, excluding any income arising from the sale in the United Kingdom of goods produced by the CFC in the territory in which it is resident for the accounting period.

(4) Subsection (5) applies instead of subsection (2) if, at any time during the accounting period, the CFC's main business is banking business in relation to which the CFC is regulated in the territory in which it is resident for the accounting period.

(5) The income condition is met if the CFC's relevant UK trading income is no more than 10% of the CFC's trading income.

(6) The CFC's "relevant UK trading income" is its trading income so far as it derives (directly or indirectly) from—

(a) UK resident persons, or

(b) UK permanent establishments of non-UK resident companies,

but excluding interest received from UK resident companies which are connected or associated with the CFC.

(7) Neither subsection (2)(a) nor subsection (6)(a) covers income deriving (directly or indirectly) from a UK resident company if—

(a) the company has made an election under section 18A of CTA 2009 (exemption for profits or losses of foreign permanent establishments), and

(b) an expense corresponding to the income is brought into account for the purpose of determining any exemption adjustment in relation to the company under that section.

371DI Exclusion: trading profits (management expenditure condition)

(1) This section applies for the purposes of section 371DF(1)(c).

(2) The management expenditure condition is met if the UK related management expenditure is no more than 20% of the total related management expenditure.

(3) "The total related management expenditure" is the total of the following expenditure incurred during the accounting period by the CFC—

- (a) expenditure incurred in the employment of any member of the CFC's staff who carries out relevant management functions,
- (b) expenditure incurred in the engagement (directly or indirectly) of any individual who is not a member of the CFC's staff but who carries out relevant management functions in consequence of an arrangement between the individual and the CFC, and
- (c) expenditure incurred in the engagement (directly or indirectly) of any company related to the CFC so far as the expenditure represents expenditure incurred by the related company in—
  - (i) the employment of any member of the related company's staff who carries out relevant management functions, or
  - (ii) the engagement by the related company (directly or indirectly) of any individual who is not a member of the related company's staff but who carries out relevant management functions in consequence of an arrangement between the individual and the related company.

(4) "The UK related management expenditure" is the total related management expenditure so far as it relates to members of staff or other individuals who carry out relevant management functions in the United Kingdom.

(5) A person carries out a "relevant management function" if the person manages or controls any assets or risks included in the relevant assets and risks.

(6) This covers (for example) a person who formulates plans or makes decisions in relation to—

- (a) the acquisition, creation, development or exploitation of such assets, or
- (b) the taking on, or bearing, of such risks.

(7) Subsection (8) applies if—

- (a) the conditions mentioned in section 371DF(1)(a), (b), (d) and (e) are met but the management expenditure condition is not met,
- (b) there is an asset or risk which is included in the relevant assets and risks and to which any part of the total related management expenditure relates,
- (c) the 50% condition is met in relation to that asset or risk, and
- (d) trading profits arising from that asset or risk are included in the provisional Chapter 4 profits.

(8) The trading profits are to be excluded from the provisional Chapter 4 profits.

(9) The 50% condition is met in relation to an asset or risk if the UK related management expenditure so far as relating to the asset or risk is no more than 50% of the total related management expenditure so far as relating to the asset or risk.

(10) Subsection (11) applies if—

(a) any part of the total related management expenditure relates to a number of assets or risks included in the relevant assets and risks, and

(b) it is not reasonably practicable to separate those assets or risks for the purpose of determining the extent to which the total related management expenditure relates to each of those assets or risks separately.

(11) Subsections (7) to (9) apply in relation to those assets or risks taken together and references to an asset or risk are to be read accordingly.

371DJ Exclusion: trading profits (IP condition)

(1) This section applies for the purposes of section 371DF(1)(d).

(2) The IP condition is met unless—

(a) the CFC's assumed total profits include amounts arising from intellectual property held by the CFC ("the exploited IP"),

(b) all or parts of the exploited IP were—

(i) transferred (directly or indirectly) to the CFC by persons related to the CFC at times during the relevant period, or

(ii) otherwise derived (directly or indirectly) at times during that period out of or from intellectual property held at times during that period by persons related to the CFC,

(c) as a result of those transfers or other derivations, the value of the intellectual property held by those persons related to the CFC, taken together, has been significantly reduced from what it would otherwise have been, and

(d) if only parts of the exploited IP were so transferred or derived, the significance condition is met.

(3) The significance condition is met if—

(a) the parts of the exploited IP ("the UK derived IP") which were transferred or otherwise derived as mentioned in subsection (2)(b) are, taken together, a significant part of the exploited IP, or

(b) as a result of the transfers or other derivations of the UK derived IP, the CFC's assumed total profits are significantly higher than what they would otherwise have been.

(4) In relation to a non-UK resident person who is related to the CFC, in this section references to the transfer or holding of intellectual property by a person related to the CFC are limited to, as the case may be—

(a) the transfer of intellectual property which before the transfer was held by the non-UK resident person (wholly or partly) for the purposes of a permanent establishment which the person has in the United Kingdom, or

(b) the holding of intellectual property by the non-UK resident person (wholly or partly) for those purposes.

(5) "The relevant period" means the period covering the accounting period and the 6 years before the accounting period.

371DK Exclusion: trading profits (export of goods condition)

(1) This section applies for the purposes of section 371DF(1)(e).

(2) The export of goods condition is met if no more than 20% of the CFC's trading income arises from goods exported from the United Kingdom, excluding goods exported from the United Kingdom to the territory in which the CFC is resident for the accounting period.

371DL Exclusion: trading profits (anti-avoidance)

(1) This section applies if—

(a) a condition mentioned in section 371DF(1) is met, or

(b) the 50% condition mentioned in section 371DI is met in relation to an asset or risk (or a number of assets or risks taken together),

but it is reasonable to suppose that that would not be the case apart from an arrangement falling within subsection (3).

(2) The condition is to be taken not to be met or (as the case may be) not to be met in relation to the asset or risk (or the assets or risks taken together).

(3) An arrangement falls within this subsection if—

(a) the arrangement involves the CFC group organising (or reorganising) a significant part of its business in a particular way, and

(b) the main purpose, or one of the main purposes, of that organising (or reorganising) is to secure that—

(i) one or more of the conditions mentioned in section 371DF(1) are met, or

(ii) the 50% condition mentioned in section 371DI is met in relation to one or more assets or risks.]