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By post to:

Carol Johnson  
Room 2/E1  
HM Treasury  
1 Horse Guards Road  
London  
SW1A 2HQ

9 February 2011

Dear Ms Johnson

**Comments of the Revenue Law Committee on the Draft Legislation for Finance Bill 2011 in relation to Foreign Branches**

The City of London Law Society (“CLLS”) represents approximately 14,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi jurisdictional legal issues.

The CLLS responds to a variety of consultations on issues of importance to its members through its 17 specialist committees. This response in respect of the draft legislation dealing with the taxation of foreign branches has been prepared by the CLLS Revenue Law Committee.

We are grateful for the opportunity to comment on the draft legislation for reforming the taxation of foreign branches. Our comments on this draft legislation are set out below.

## **Section 18A**

### **Profits or losses of foreign permanent establishments**

We are supportive of an "opt-in" exemption from corporation tax for the profits of foreign branches of UK companies. It is not, however, clear to us from the draft legislation that the "opt-in" applies to all foreign branches of each UK company in a group and we recommend this is clarified if that is the intention.

In addition, it is not clear to us how the draft legislation is intended to operate in the context of companies with permanent establishments in more than one territory, or companies with multiple permanent establishments in the same territory. Section 18A(1), for example, refers to "the" foreign permanent establishments amount being left out of account, and section 18A(3) defines "relevant foreign territory" in the context of a non-UK territory in which a UK company carries on business through "a" permanent establishment.

#### **Sections 18A(5)(b) and 18A(7)(b):**

We wonder if the use of "incorporated" is too vague.

#### **Sections 18A(6)(b) and 18A(8):**

The "assumption" referred to in the draft legislation could be clarified. For example, in Section 18A(5)(b) there appear to be two relevant assumptions. It might be clearer to include references to "assumptions" in sections 18A(5)(b) and 18A(7) as a signpost for the reader.

#### **Sections 18A(9)(a) and (b):**

It is not clear to us how the wording: "in the case of which a loss which is an allowable loss for those purposes accrues on its disposal" and "in the case of which a gain which is a chargeable gain for those purposes accrues on its disposal" is intended to operate. There are other references in the draft legislation to the interaction of the chargeable gains regime with foreign profits exemption (for example, section 18B(7)). It is also not entirely clear to us how sections 18A(9)(a) and (b) are intended to interact with these other references.

#### **Section 18A(10):**

We wonder whether this section is necessary given that the effect of the election will be to leave the foreign permanent establishments amount out of account.

## **Section 18B**

### **Effect of election**

#### **Section 18B(1)(a)**

We are concerned whether an election to "opt-in" should be irrevocable in all circumstances. For example, we think consideration should be given to introducing a right to revoke an election on a change of ownership of a UK company where its shares

are sold to a third party which does not wish the exemption regime to apply to the company's foreign branches.

**Section 18B(3):**

The word “secures” should be replaced with “ensures” or “has the effect”.

**Sections 18B(4)-(10):**

We think that the draft legislation is mechanically complex and, in parts, difficult to follow. Section 18B(5), for example, refers to a point in time that is six years before “that...”. Presumably “that” should be the end of the accounting period in which the election is made, but this is not clear. We also find it difficult to follow the drafting in section 18B(6) and suggest that consideration could be given to simplifying the drafting. The formula in section 18B(8) does not appear to work; as an example, the amount under step 1 will be a negative (say -1). Step 2 then applies if the relevant amount is negative (say, -2), and the draft legislation states this should be added to the amount under step 1 (so presumably,  $-1 + -2 = -3$ ). Step 3 applies if an amount if the relevant amount is positive (say 5), and the draft legislation states this should be subtracted to the amount under step 1 but so as not to cause the result to exceed nil. Confusingly, no reference is made to Step 2 in the drafting for Step 3. Applying the draft legislation for Step 3 gives  $-1 - 5 = -6$ : it is not clear here how the result can ever exceed nil.

**Section 18C**

**Section 18C(2) and (4):**

The drafting here refers to “profits or losses for the purposes of section 18A”, and we wonder whether this should instead refer to the concepts of “relevant profits amount” and “relevant losses amount”. We are also not sure whether the words “in respect of chargeable gains” are necessary.

**Section 18C(3)(b):**

We suggest replacing “that” with “making investments”, and inserting the words “to that company” between “apply” and “for the relevant accounting period”.

**Section 18D**

**Anti-diversion rule**

We are supportive of measures being included in the legislation to prevent profits being artificially diverted from the UK. We assume, however, that any such measures will be revisited and, potentially, revised once the reform of the CFC regime is complete so that the two sets of rules are compatible. We do, however, have a concern that, the only defences to the “anti-diversion rule” under the draft legislation are the “entry limit” and the “motive test”. In the context of the current CFC regime a “motive test” has historically been difficult to apply in practice and we suggest that other defences (perhaps other defences which are applicable to or which are being considered in the context of the CFC regime) are considered.

**Section 18F**

**Section 18F(2):**

We think that the drafting of the definition of "Relevant non-discrimination provision" is unclear and could be improved.

Yours sincerely

A handwritten signature in black ink, appearing to read "Bradley Phillips". The signature is written in a cursive style with a large initial 'B' and a long, sweeping tail.

**Bradley Phillips**  
**Chair**  
**City of London Law Society Revenue Law Committee**



**THE CITY OF LONDON LAW SOCIETY  
REVENUE LAW COMMITTEE**

Individuals and firms represented on this committee are as follows.

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