A Consultation on Land and Buildings Transaction Tax Rules for Property Authorised Investment Funds

SCOTTISH GOVERNMENT
JULY 2015

The Scottish Government
Riaghaltas na h-Alba

Contents

Chapter 1: Introduction

Purpose

1. The purpose of this consultation is to gather views from the investment management industry and other interested stakeholders on the potential introduction of an exemption from Land and Buildings Transaction Tax (LBTT), for the transfer of properties from Authorised Unit Trusts (AUTs) to Open Ended Investment Companies (OEICs) in Scotland, in certain specified circumstances. As a result of the consultation, we hope to understand the impact that this proposed change in tax treatment would have on the asset management sector, the property sector and the Scottish economy more generally. We also aim to ensure that the introduction of such an exemption would be consistent with the Scottish approach to taxation. Proposed draft regulations can be found in Annex A.

Scope

2. LBTT replaced UK Stamp Duty Land Tax (SDLT) on land transactions in Scotland on 1 April 2015. The legal underpinning for the tax is found in the Land and Buildings Transaction Tax (Scotland) Act (the LBTT Act), which received Royal Assent on 31 July 2013.

3. LBTT legislation differs from SDLT in a number of areas, better aligning the legislation with Scots law and practices and ensuring appropriate reliefs and exemptions are applied. Scottish Ministers have also made clear that they wish to take all reasonable steps to reduce the risk of artificial avoidance of the devolved taxes, to foster a climate of tax compliance and thus help to safeguard public finances. To minimise opportunities for artificial avoidance, the Scottish approach seeks to ensure that tax reliefs and exemptions are introduced only where they are supported by a strong evidence base.

4. Section 46 of the LBTT Act provides for a regulation-making power which enables Scottish Ministers to exempt from tax properties held by an AUT when it converts to, or amalgamates with, an OEIC. The Scottish Government consulted on proposals for LBTT subordinate legislation in May 2014. The proposed suite of secondary legislation did not include regulations under section 46 of the Act. No representations were received at that time on the absence of regulations, and no regulations were made on AUTs and OEICs. Consequently, LBTT remains chargeable on the transfer of Scottish properties held by AUTs converting to OEICs. However, no SDLT is payable in the same circumstances on the transfer of properties situated in England, Wales or Northern Ireland.

5. Since LBTT became operational, the investment management sector has raised concerns about the impact of the LBTT charge on the planned conversion of AUTs to Property Authorised Investment Funds (PAIFs), a form of OEIC, where these AUTs hold property in Scotland. The Scottish Government is committed to ensuring that Scotland remains an attractive location for investment. We are therefore now considering proposals to exempt such transactions from LBTT.

Chapter 2: Property investment in Scotland

6. AUTs have been the traditional mechanism for collective investment in the UK property market for a considerable period of time. Over the last few years however many AUTs have converted to OEICs. The main purpose of converting an AUT to an OEIC is usually to obtain Property Authorised Investment Fund (PAIF) status. This is an investment structure introduced by the UK Government in 2008 to provide a tax efficient vehicle for collective investment in rental property. A number of fund managers are in the process of converting existing AUT to PAIFs.

The benefits of Property Authorised Investment Funds

7. PAIFs were designed to ensure that investors are taxed on rental income from the PAIF in the same way as if they had invested directly in the property. This benefits investors with certain tax exemptions, such as charities, pension funds, life companies and ISA investors, who would otherwise receive property rental income from AUTs net of income tax, which they would be unable to reclaim. Tax-exempt investors in a PAIF do not bear any tax charge on the rental income which they receive from the fund.

8. An AUT that invests in property cannot benefit from the PAIF regime without first converting into, or amalgamating with, an OEIC. This entails property and other assets being transferred (or seeded) from one legal entity to another.

9. Due to economic conditions and the administrative steps involved in conversion, take up of PAIFs by the industry was lower than anticipated when they were introduced in 2008 and when further reforms were made to the scheme in 2012.

Property fund assets based in Scotland

10. HM Treasury believed that £60 billion worth of UK property was held in investment funds as at July 2014[1]. We understand that the vast majority of property assets owned by these funds are non-residential and that funds generally hold properties across the UK, including in Scotland.

11. The SDLT/LBTT treatment is not dependent on where the fund is based or domiciled. The determining factor in terms of tax treatment is the location of the property in question. So property situated in Scotland will be subject to LBTT and property situated in England, Wales and Northern Ireland will be subject to SDLT, regardless of where the fund owning the property is itself managed. As the legislation currently stands, if an AUT converts to a PAIF with property being seeded into the PAIF, no SDLT liability will arise on property in England, Wales and Northern Ireland, but each property held in Scotland will be subject to an LBTT charge. This could make it less attractive for fund managers who are considering conversion to invest in properties in Scotland, and potentially could encourage dis-investment.

[1] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/332079/Stamp_Duty_Land_Tax_rules_for_property_investment_funds.pdf

Question 1: What are the risks and impacts for the fund management and investment sector in Scotland arising from the absence of an LBTT exemption?

Question 2: What are the risks and impacts for the property sector in Scotland arising from the absence of an LBTT exemption?

Chapter 3: Proposals for an exemption

12. The investment management and property sectors are of strategic importance to Scotland's economy and we wish to ensure that LBTT supports our commitment to Scotland remaining an attractive location for collective investment in property. Subject to the outcome of this consultation, we propose to bring forward changes to legislation to introduce an exemption from LBTT for AUT to OEIC conversion or amalgamation transactions, using the regulation-making power in section 46(1) of the LBTT Act. Any such proposal would of course be subject to scrutiny and approval by the Scottish Parliament.

13. Such an exemption would ensure parity in tax treatment for LBTT with other types of corporate transactions in which there is a change in the legal form, rather than the substance, of ownership. For example, group relief (available under schedule 10 of the LBTT Act) and acquisition relief (available under schedule 11 of the LBTT Act).

14. Annex A is a draft of this legislation, provisionally entitled *Land and Buildings Transaction Tax (Open-ended Investment Companies) (Scotland) Regulations 2015,* which the Scottish Government intends to introduce to Parliament at the start of the next parliamentary session, subject to the outcome of this consultation. The regulations are intended to provide an exemption from LBTT when an Authorised Unit Trust converts to an OEIC or amalgamates with an already existing one. These proposals largely mirror '*The Stamp Duty Land Tax (Open-ended Investment Companies) Regulations 2008*'[2].

15. The conversion or amalgamation of an AUT to an OEIC exemption from Land and Buildings Transaction tax charge is designed to allow investment companies to transfer assets from AUTs to an OEIC without incurring a charge. It is also designed to minimise the opportunity for artificial tax avoidance.

16. As such it is therefore proposed that the following conditions would apply:

- the exemption is only applicable if assets are transferring from the target AUT to an OEIC;

- the transfer of property assets is a conversion (or amalgamation) of an AUT to an OEIC, whereby the whole of the available property of the target trust becomes the whole (or part if undergoing an amalgamation) of the property of the acquiring company;

- under the arrangement all the units in the target trust are extinguished so that the target trust therefore will no longer exist;

- the conversion or amalgamation consists of or includes the issue of shares in the acquiring company to the persons who held the extinguished units, helping ensure ownership of the two investment vehicles are the same;

[2] http://www.legislation.gov.uk/uksi/2008/710/made

- the shares issued to those persons are in proportion to their holdings of the extinguished units, helping to ensure that asset transfers between owners of the extinguished units does not provide opportunities for tax avoidance;

- the arrangement does not include anything other than the discharge by the acquiring company of liabilities of the trustees of the target trust; and

- the exemption must be claimed by making a return to Revenue Scotland.

17. The Scottish Government has considered the potential for such an exemption to create opportunities for tax avoidance. We think the proposed Scottish regulations as drafted in Annex A mitigate the risk of tax avoidance.

Question 3: Do you think that the Scottish Government should introduce an exemption from LBTT for properties held by AUTs converting or amalgamating with an OEIC?

Question 4: Do you think that an exemption as drafted in Annex A could create opportunities for tax avoidance? If so, how?

Question 5: Are there any additional comments you would like to make in relation to the draft regulations in Annex A?

Chapter 4: Responding to this consultation

- This consultation is your opportunity to share your views on whether the Scottish Government should introduce an exemption from LBTT for Authorised Unit Trusts converting to Open Ended Investment Companies and to help us shape any such relief in subordinate legislation. **Responses should be submitted by Friday 28 August 2015.**

- It would be helpful for you to send your response through https://consult.scotland.gov.uk/fiscal-responsibility/land-and-building-transaction-tax

- We are, of course, happy to receive written submissions too.

Written comments

You can respond to this consultation by sending your response to the Scottish Government.

We are inviting written responses to this consultation paper e-mail or by post **by Friday 28 August 2015**. Please send your response, along with the completed Respondent Information Form to:

Fiscal Responsibility Division
Scottish Government
Area 3B South
Victoria Quay
Edinburgh
EH6 6QQ

We would be grateful if you would use the consultation questionnaire provided or would clearly indicate in your response which questions or parts of the consultation paper you are responding to, as this will aid our analysis of the responses received.

Handling your response

We need to know how you wish your response to be handled and, in particular, whether you are happy for your response to be made public. Please ensure that you send a copy of your respondent information form (see page 9) with any responses so that we have your details and know if you are happy for your response to be made publicly available.

If you ask for your response not to be published, we will regard it as confidential and treat it accordingly. All respondents should be aware that the Scottish Government is subject to the provisions of the Freedom of Information (Scotland) Act 2002 and would therefore have to consider any request made to it under the Act for information relating to responses made to this consultation exercise.

Next steps

If you tell us we can make your response public, we will put it in the Scottish Government Library and on the Scottish Government consultation web pages. We will check all responses where agreement to publish has been given for any wording that might be harmful to others before putting them in the library or on the website. If you would like to see the responses please contact the Scottish Government Library on 0131 244 4565. Responses can be copied and sent to you, but a charge may be made for this service.

What happens next?

Following the closing date, all responses will be analysed and considered along with any other available evidence to help us reach a decision about the finalised versions of the relevant subordinate legislation. We will issue a report on this consultation process which will be published on the Scottish Government's website at:

http://www.scotland.gov.uk/Publications/Recent

Comments and complaints

If you have any comments about how this consultation exercise has been conducted, please send them to:

Fiscal Responsibility Division
Scottish Government
Area 3B South
Victoria Quay
Edinburgh
EH6 6QQ

Scottish Government consultations

This consultation, and all other Scottish Government consultation exercises, can be viewed online on the consultation web pages of the Scottish Government website at:

www.scotland.gov.uk/consultations

The Scottish Government has an e-mail alert system for consultations. This system, called SEconsult, allows individuals and organisations to register and receive a weekly email with details of all new consultations (including web links). SEconsult complements, but in no way replaces, Scottish Government distribution lists. It is designed to allow people with an interest to keep up to date with all Scottish Government consultation activity. You can register at SEconsult:
http://www.scotland.gov.uk/consultations/seconsult.aspx

A CONSULTATION ON LAND AND BUILDINGS TRANSACTION TAX RULES FOR PROPERTY AUTHORISED INVESTMENT FUNDS

RESPONDENT INFORMATION FORM

Please Note this form **must** be returned with your response to ensure that we handle your response appropriately

1. Name/Organisation

Organisation Name

Title Mr ☐ Ms ☐ Mrs ☐ Miss ☐ Dr ☐ Please tick as appropriate

Surname

Forename

2. Postal Address

Postcode	**Phone**	**Email**

3. Permissions - I am responding as…

Individual / **Group/Organisation**

☐ **Please tick as appropriate** ☐

(a) Do you agree to your response being made available to the public (in Scottish Government library and/or on the Scottish Government web site)?

Please tick as appropriate
☐ **Yes** ☐ **No**

(b) Where confidentiality is not requested, we will make your responses available to the public on the following basis

Please tick ONE of the following boxes

(c) The name and address of your organisation **will be** made available to the public (in the Scottish Government library and/or on the Scottish Government web site).

Are you content for your **response** to be made available?

Please tick as appropriate
☐ **Yes** ☐ **No**

Yes, make my response, name and address all available ☐

or

Yes, make my response available, but not my name and address ☐

or

Yes, make my response and name available, but not my address ☐

(d) We will share your response internally with other Scottish Government policy teams who may be addressing the issues you discuss. They may wish to contact you again in the future, but we require your permission to do so. Are you content for Scottish Government to contact you again in relation to this consultation exercise?

Please tick as appropriate ☐ **Yes** ☐ **No**

CONSULTATION QUESTIONS

Q1 What are the risks and impacts for the fund management and investment sector in Scotland arising from the absence of an LBTT exemption?

If you have any comments, please outline them below.

Q2 What are the risks and impacts for the property sector in Scotland arising from the absence of an LBTT exemption?

If you have any comments, please outline them below.

Q3 Do you think that the Scottish Government should introduce an exemption from LBTT for properties held by Authorised Unit Trusts converting or amalgamating with an Open Ended Investment Company?

Yes ☐ **No** ☐

If you have any comments, please outline them below.

Q4 Do you think that an exemption as drafted in Annex A could create opportunities for tax avoidance? If so, how?

Yes ☐ **No** ☐

If you have any comments, please outline them below.

Q5 Are there any additional comments you would like to make in relation to the draft regulations in Annex A?

If you have any comments, please outline them below.

S C O T T I S H   S T A T U T O R Y   I N S T R U M E N T S

2015 No.

LAND AND BUILDINGS TRANSACTION TAX

The Land and Buildings Transaction Tax (Open-ended Investment Companies) (Scotland) Regulations 2015

Made - - - -	*2015*
Laid before the Scottish Parliament	*2015*
Coming into force - -	*2015*

The Scottish Ministers make the following Regulations in exercise of the powers conferred by section 46(1) of the Land and Buildings Transaction Tax (Scotland) Act 2013(**a**) and all other powers enabling them to do so.

Citation and commencement

1. These Regulations may be cited as the Land and Buildings Transaction Tax (Open-ended Investment Companies) (Scotland) Regulations 2015 and come into force on [ ] 2015.

Interpretation

2.—In these Regulations—
"the Act" means the Land and Buildings Transaction Tax (Scotland) Act 2013.
"authorised unit trust" means a unit trust scheme in the case of which an order under section 243 of the Financial Services and Markets Act 2000(b) is in force;
"land transaction" has the meaning given by section 3 of the Act; and
"land transaction return" has the meaning given by section 65 of that Act.

Conversion of an authorised unit trust to an open-ended investment company — exemption from land and buildings transaction tax charge

3.— (1) A land transaction transferring any property which is subject to the trusts of an authorised unit trust ("the target trust") to an open-ended investment company ("the acquiring company") is exempt from charge to land and buildings transaction tax if the conditions set out in paragraph (2) are fulfilled.
(2) Those conditions are that—

(a) the transfer forms part of an arrangement for the conversion of an authorised unit trust to an open-ended investment company, whereby the whole of the available property of the target trust becomes the whole of the property of the acquiring company;
(b) under the arrangement all the units in the target trust are extinguished;
(c) the consideration under the arrangement consists of or includes the issue of shares ("the consideration shares") in the acquiring company to the persons who held the extinguished units;
(d) the consideration shares are issued to those persons in proportion to their holdings of the extinguished units; and

(**a**) 2013 asp. 11.
b 2000 c. 8.

(e) the consideration under the arrangement does not include anything else, other than the assumption or discharge by the acquiring company of liabilities of the trustees of the target trust.

(3) Relief under this regulation must be claimed in a land transaction return or an amendment of such a return.

(4) In this regulation and in regulation 4 "the whole of the available property of the target trust" means the whole of the property subject to the trusts of the target trust, other than any property which is retained for the purpose of discharging liabilities of the trustees of the target trust.

(5) For the purposes of this regulation and regulation 4, each of the parts of an umbrella scheme (and not the scheme as a whole) shall be regarded as an authorised unit trust, and "umbrella scheme" has the same meaning as in section 45 of the Land and Buildings Transaction Tax (Scotland) Act 2013.

Amalgamation of an authorised unit trust with an open-ended investment company — exemption from land and buildings transaction tax charge

4.— (1) A land transaction transferring any property which is subject to the trusts of an authorised unit trust ("the target trust") to an open-ended investment company ("the acquiring company") is exempt from charge to land and buildings transaction tax if the conditions set out in paragraph (2) are fulfilled.

(2) Those conditions are that—

(a) the transfer forms part of an arrangement for the amalgamation of an authorised unit trust with an open-ended investment company, whereby the whole of the available property of the target trust becomes part (but not the whole) of the property of the acquiring company;

(b) under the arrangement all the units in the target trust are extinguished;

(c) the consideration under the arrangement consists of or includes the issue of shares ("the consideration shares") in the acquiring company to the persons who held the extinguished units;

(d) the consideration shares are issued to those persons in proportion to their holdings of the extinguished units; and

(e) the consideration under the arrangement does not include anything else, other than the assumption or discharge by the acquiring company of liabilities of the trustees of the target trust.

(3) Relief under this regulation must be claimed in a land transaction return or an amendment of such a return.

A member of the Scottish Government

St Andrew's House,
Edinburgh
2015

EXPLANATORY NOTE

(This note is not part of the Regulations)

These Regulations make provision for the exemption from land and buildings transaction tax of land transactions transferring property on the conversion of an authorised unit trust to, or its amalgamation with, an open-ended investment company.

Regulation 1 provides for citation and commencement, and regulation 2 for interpretation.

Regulation 3 exempts from land and buildings transaction tax a land transaction transferring property of a unit trust to an open-ended investment company, where the transfer is made as part of the conversion of the trust to the company. Exemption is given where the units of the unit trust are extinguished and the unit holders receive as consideration shares in the company, in proportion to their holdings of units in the trust.

Regulation 4 makes similar provision for exemption from stamp duty land tax, where the property is transferred as part of the amalgamation of a unit trust with an open-ended investment company.

This publication is available at **www.gov.scot**

Any enquiries regarding this publication should be sent to us at
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