

10th February 2004

Inland Revenue
Business Tax
Room 4W1
22 Kingsway
London WC2B 6NR

Dear Sirs

Income tax: Meaning of UK source for payments of interest and royalties

The Association

1. The Association of Corporate Treasurers was formed in 1979 to encourage and promote the study and practice of corporate finance and treasury management and to educate those involved in the field. Today, it is an organisation of professionals in corporate finance, risk and cash management operating internationally. A professional body and not a trade association, it has over 3,000 Fellows, Members and Associate Members. With more than 1,200 students in more than 40 countries, its education and examination syllabuses are recognised as the global standard setters for treasury education. Members of the Association work in many fields. The majority of Fellows work in large UK public companies, responsible for the treasury and corporate finance functions.
2. The ACT usually comments from the corporate and not the financial services sector standpoint

Introduction

3. Overall we welcome your consultation on UK source income and the moves to clarify the definitions and rules applicable

Responses to specific questions

Are respondents in favour of adopting a definition of UK source aligned with the OECD model tax convention?

4. Introduction of a statutory definition of 'UK source' would provide certainty of treatment for the taxpayer, and this increased clarity is welcomed.
5. We also accept that it would be helpful for the UK to conform to OECD principles.

Do respondents foresee any issues about adopting a definition based on place of residence of the payer?

6. See other responses below.

What problems might arise where UK residents currently pay non-UK source interest?

7. UK residents who make interest payments that are not currently treated as having a UK source would be required to deduct income tax from those payments under the proposed new definition. It is possible that they would not have entered into the arrangements giving rise to the interest had there been a requirement to deduct income tax.
8. We therefore suggest that existing arrangements, including future rollovers of existing loans with the same lender or lending group and no other changes in basic terms apart from interest rate, fees and maturity dates, should be excluded from the new rules.
9. Overseas branches of UK companies often take out loans with local banks for the purposes of the branch business. It is not clear whether interest paid on such loans would be excluded from the new definition. We believe it should be, to avoid penalising UK companies that operate through foreign branches rather than subsidiaries.

How would the definition impact UK permanent establishments or partnerships with some non-resident partners?

10. No comment.

What would be the effect of extending the definition to interest paid to non-resident landlords?

11. If the proposed definition were extended to treat interest paid by non-resident landlords on loans to acquire let property which is situated in the UK as having a UK source, regardless of the residence of the owner of the property, then non-resident landlords would be required to deduct income tax from interest payments. It seems that this would be the case even if the loan were not secured on the UK property.
12. We believe that this would increase the cost of investing in UK property for non-resident landlords and could therefore have an adverse impact on the UK property industry. We do not, therefore, think that the definition should be extended to interest paid by non-resident landlords.

Should the definition be extended to apply to annuities and other annual payments?

13. No comment.

How long would payers need to adapt their systems and would a start date of Royal Assent allow sufficient time?

14. Given that the Finance Bill is not normally published until April, with Royal Assent usually given in July or August, this would only give payers three to four months to adapt

their systems. We do not believe that this would be sufficient time to make the necessary changes and test systems.

15. As noted above, it is possible that many UK residents who are not currently required to deduct income tax from interest payments would be required to do so under the proposed new rules, but this would not have been taken into account when the arrangement giving rise to the interest payments was entered into. We therefore suggest that the new rules should only apply to payments made under arrangements entered into after the start date.

16. We note that you may wish to make all responses to formal consultations available for public inspection unless the respondent requests otherwise. These comments are on the record and may be freely quoted and made available for public inspection.

17. We hope these responses are helpful for your deliberations and if you need any further information or clarifications please contact any of the people listed below.

Yours faithfully,

Richard Raeburn
Chief Executive

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