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The Qualifying Asset Holding Company (QAHC) regime

The QAHC regime amends parts of UK tax law to make the UK an attractive location to hold global investments.

The UK Government introduced the new regime for the taxation of qualifying asset holding companies (the QAHC regime) in 2022, which were slightly amended in 2023.

The QAHC regime removes certain barriers which have historically limited investor appetite for using a UK company to act as a holding company/intermediate holding company to facilitate the flow of capital, income and gains between investors and underlying investments. Broadly, the aim of the regime is to ensure investors are in the same position as if they invested in the underlying assets directly, and the holding companies/intermediate holding companies pay no more tax than is proportionate to the activities they perform.

As at the end of October 2023, HMRC confirmed that over 275 QAHCs have elected into the regime. We have seen increasing engagement from many of our clients, of all sizes and across all asset classes, regarding the potential use of QAHCs for future investment structures. Since the inception of the regime, we have seen investors utilising QAHCs on a standalone basis within their existing investment platforms to more recently seeing a number of clients establish new funds which utilise QAHCs as their standard investment platform.

Eligibility criteria

In order to enter into the QAHC regime a company will need to satisfy the following criteria:

- It is resident for tax purposes in the United Kingdom;
- No more than 30% of the relevant rights (profits available for distribution, entitlement to assets on a winding up and voting rights) are held directly or indirectly by persons who are not 'Category A' investors;
- It meets the 'activity condition' (i.e. undertakes an investment business with any other activity being non-substantial and ancillary to that of the investment business);
- It meets the investment strategy condition (which stipulates that the strategy of the QAHC does not involve the acquisition of listed shares except in certain circumstances);
- It is not a UK REIT (which includes members of a group UK REIT) or a company within the securitisation regime;
- Its shares are not listed or traded on a public market or exchange; and
- An entry notification is in force.

Category A investors

Category A investors are broadly defined as being:

- Another QAHC;
- An 'intermediate company' which is at least 99% held by Category A investors (other than QAHCs), and meets the 'activity' condition;
- A 'qualifying fund', being a CIS or AIF that meets the 'diversity of ownership' condition, meaning:
  - It is not "close" (as defined for this purpose); or
  - It is 70% controlled by Category A investors; or
  - In the case of a Collective Investment Scheme ("**CIS**") (or is an Alternative Investment Fund ("**AIF**") that is not a CIS only by virtue of the entity being a body corporate), it meets the Genuine Diversity of Ownership ("**GDO**") requirement (either directly or as part of a multi-vehicle arrangement).
- A UK public authority (as defined); and
- A relevant qualifying investor such as: a pension scheme (both in the UK and overseas), a sovereign immune entity, an authorised long term insurance business in the UK or otherwise, an unconnected UK charity and a UK REIT or an equivalent under the law of a territory other than the UK, and certain non-UK companies which meet the property income condition.

2023 Improvements

As part of the 2023 Improvements, HMRC has provided greater clarity for those seeking to establish QAHCs (either directly as an amendment to the QAHC regime, or indirectly in respect of other parts of UK legislation, where it was necessary to make changes), including: clarifying which entities may be 'qualifying funds'; allowing for a QAHC to hold listed equity securities; as well as other welcome amendments.

Widely marketed funds relying on the GDO rules

As part of the wider changes to the GDO rules, HMRC has expanded guidance to address uncertainties as to whether funds arranged as parallel partnerships or master/feeder arrangements ('multi-vehicle arrangements') could be treated as qualifying funds via the GDO condition. Based on our experience, this route to qualifying fund status is preferable for investment funds, as (generally) the test applies at the outset of the fund and should not require ongoing monitoring (which would be the case under the Category A or close company tests).

The uncertainty in interpreting the GDO rules under the original legislation was that where a fund has, for example, parallel or feeder vehicles, only those which had been marketed for investment could rely on this condition. However, the multi-fund arrangements introduction clarifies that the GDO test should be applied to the arrangements as a whole, rather than on an entity by entity basis.

Concerns around body corporates

There was previously a concern under the rules whereby funds that were set up as body corporates may not be able to rely on the GDO conditions to be a Category A investor, as they could not be a CIS (unless they were open-ended investment companies).

Some changes to the rules have made it clear that an entity which is an 'AIF' but is not a CIS merely due to the fact it is a body corporate, can rely on the GDO definition. This change has been made retrospectively, and should remove any uncertainty around Delaware LPs being 'funds' (as some had previously considered these entities to be body corporates). The changes should also be beneficial for funds, which are typically structured with a corporate vehicle acting as the fund (e.g. Cayman company feeders).

QAHCs can now hold listed equity securities

Under the original rules a QAHC could not have an investment strategy to hold listed equity. However, a QAHC can now make an election to HMRC (they will need to be notified) so that it meets the investment strategy condition, even if it intends to hold listed equity (this should also apply to any of its parent entities that are QAHCs). As a result, the QAHC should be able to hold certain investments (i.e. equity securities that are listed on a recognised stock exchange or any other public market or exchange) directly, although any dividends received from its investments would not be able to benefit from one of the existing domestic exemptions.

Key features of the regime

Disposals

Gains on the disposal of shares or other qualifying equity interests (other than shares which derive 75% of their value from UK land) and overseas property ('qualifying assets') are exempt, with no minimum holding period. Direct and indirect disposals of overseas real estate are covered by the exemption (including disposals in entities which are deemed to be companies for this purpose).

Income from an overseas property business

The profits of an overseas property business of a QAHC are also exempt where those profits are subject to tax in an overseas jurisdiction.

Withholding taxes

The obligation to deduct income tax at the basic rate on payments of interest is disapplied. The UK does not impose withholding tax on dividend payments except for REITs (which cannot access the regime).

Additionally, as a fully taxable vehicle, a QAHC should also be able to benefit from treaty relief. Specifically, we would expect that the matching of the location of the holding company with the key decision makers for investments where there are UK based asset managers, should support applications for treaty and certain domestic relief.

Interest and other finance costs

Interest and other finance costs on debt funding the QAHC, including profit participating and convertible debt, are in principle deductible on an accruals basis. These are generally able to match income arising on debt investments except for an arm's length margin. The finance costs may also offset other income but subject to the usual interest limitation restrictions.

The late paid interest rules are switched off so that in certain situations, interest payments are relieved in the QAHC on the accruals basis rather than the paid basis.

The QAHC can also hedge (from a tax perspective) exchange gains and losses using fair value accounting, whereby certain conditions are met (including the accounting of the instrument).

Returns to investors

Payments made where a QAHC redeems, repays or repurchases its own shares are allowed to be treated as capital (except where they relate to 'qualifying employment-related securities) rather than income distributions.

Provided certain conditions are met, repurchases by a QAHC of share and loan capital are exempted from Stamp Duty and Stamp Duty Reserve Tax.

Entry into the regime

Upon entry into the regime the company will be subject to a deemed disposal and reacquisition of its qualifying assets at market value.

Any gain arising on the deemed disposal(s) would be subject to corporation tax (25%), unless (in the case of shares) the substantial shareholding exemption applies. However, where companies migrate their tax residence to the UK, and elect into the regime within 30 days there will be no UK tax charge on the deemed disposal(s). There are also provisions to mitigate (but not necessarily eliminate) the effect of multiple charges where more than one company in a chain of ownership joins the regime.

Assets entering and leaving the ring fence

For a company which has previously elected to be a QAHC and a qualifying asset subsequently enters or exits the (exempt) ring fenced business, there is a deemed market value disposal (which will be taxable at the point the asset enters the ring fenced business). For example, the shares in a company which ceases to be "UK property rich" (i.e. no longer derives at least 75% of its value from UK land) would enter the exempt ring fenced business. For assets entering into the regime, the gain/loss is taxable or allowable subject to adjustments to avoid a double charge. For assets leaving the regime, gains or losses are exempt.

Exiting the regime

Whether the QAHC elects to leave the regime, or leaves as a result of breaching the conditions, exiting will result in a deemed disposal and reacquisition of its qualifying assets at market value immediately prior to exiting the regime. As any gain will arise under the QAHC regime, however, it should be exempted, resulting in a rebasing of those 'qualifying assets' to their market value at that date.

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