EXPLANATORY MEMORANDUM TO

THE REAL ESTATE INVESTMENT TRUSTS (PRESCRIBED ARRANGEMENTS) REGULATIONS 2009

2009 No. 3315

1. This explanatory memorandum has been prepared by Her Majesty's Revenue and Customs (HMRC) and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 The regulations are designed to prevent commercial groups from artificially restructuring themselves in order to meet the tests and conditions of the Real Estate Investment Trusts (REIT) regime where they otherwise would not meet those tests. The regulations will treat any entity placed outside the regime as a result of such arrangements as a member of the REIT group. The consequence being that the REIT tests and conditions will apply to that entity and in appropriate circumstances the REIT may be removed from the regime. Where the arrangements are made for genuine commercial purposes or are between persons dealing at arm's length then the regulations will not apply.

3. Matters of special interest to the Select Committee on Statutory Instruments

3.1 The Government announced its intention to prevent groups of companies from artificially restructuring in the pre Budget Report on 24 November 2008. The intention was to stop such behaviour from the earliest date. The instrument applies retrospectively only to arrangements made on or after 7th of May 2009 (being the date the draft Regulations were first published) as long as those arrangements were during an accounting period that ends on or after the date this instrument is made.

4. Legislative Context

4.1 These are the first regulations made under the power contained in paragraph 8 of Schedule 34 to the Finance Act 2009. This paragraph inserts a new section 136A into the Finance Act 2006 titled 'Connected persons' which gives HM Treasury a power to make regulations for these purposes. These may not be made unless draft regulations have been laid before and approved by resolution of the House of Commons.

5. Territorial Extent and Application

5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

The Economic Secretary to the Treasury has made the following statement regarding Human Rights:

In my view the provisions of the Real Estate Investment Trusts (Prescribed Arrangements) Regulations 2009 are compatible with the Convention rights.

7. Policy background

7.1 The REIT regime allows qualifying property rental companies to be exempt from Corporation Tax on the profits from their property rental business. On joining the regime there are conditions relating to the types of company and the nature of their business. Once in the regime there are tests, including tests of how much of the REIT's business is the rental of property.

7.2 A number of companies that were not primarily property companies sought to join the REIT regime. These companies proposed to use artificial restructuring so that where they would not pass the tests before restructuring, they would afterwards. The Government announced at PBR that it has decided to prevent such companies joining the regime.

7.3 The Regulations take effect in circumstances where arrangements are made, with a connected person, with the purpose of passing the REIT regime tests and conditions, without which the tests and conditions would not be met. If the purpose or one of the main purposes of the arrangements is to pass the REIT conditions and tests, then the effect of the arrangements will be undone so that the connected person is treated as part of the REIT group for the purposes of the tests or conditions of the regime.

8. Consultation outcome

8.1 The draft regulations were published on the HMRC internet site. In addition they were shared with stakeholders. Feedback was received on the draft regulations and these were amended to take the feedback into account.

8.2 The principal concern was the conditions relating to genuine commercial purpose and arrangements at arm's length. It was agreed that either of these would result in the arrangements being excluded from the regulations rather than both .

9. Guidance

9.1 The Guidance on Real Estate Investment Trusts available on the HMRC internet site will be amended to explain how the regulations will apply. The draft guidance will be shared with stakeholders for their comments.

10. Impact

10.1 An Impact Assessment has not been prepared for this instrument as there is no impact on business, charities or voluntary bodies.

11. Regulating small business

11.1 The legislation does not apply to small business as the REIT legislation requires that REITs are companies listed on a recognised stock exchange.

12. Monitoring & review

12.1 None required

13. Contact

Tony Linehan at HM Revenue and Customs Tel: 020 7147 0527 or email: tony.linehan@hmrc.gsi.gov.uk can answer any queries regarding the instrument.