



Pension Investment
Association of Canada

Association canadienne des
gestionnaires de caisses de retraite

February 15, 2018

NRCG Consultation
HM Revenue & Customs
Room 3C/04
100 Parliament Street
London, UK
SW1A 2BQ

Via email: NRCG.Consultation@hmrc.gsi.gov.uk

Dear Sirs/Mesdames,

Re: Pension Investment Association of Canada (“PIAC”) Comments on Taxing gains made by non-residents on UK immovable property

The Pension Investment Association of Canada (PIAC) would like to thank HM Revenue & Customs for allowing us to provide comments on the consultation document: Taxing gains made by non-residents on UK immovable property released on 22 November 2017.

PIAC has been the national voice for Canadian pension funds since 1977. Senior investment professionals employed by PIAC's member funds are responsible for the oversight and management of over CAD \$1.8 trillion in assets on behalf of millions of Canadians. PIAC's mission is to promote sound investment practices and good governance for the benefit of pension plan sponsors and beneficiaries. PIAC's positions on public policy reflect the fiduciary framework in which member funds operate and its commitment to work in the best interests of plan members.

PIAC has responded below to the questions raised in the Consultation Document that are relevant to Canadian pension funds. This submission focuses on proposed rules that are either ambiguous or appear to contradict the intended policy objectives of Government, which we understand is to continue to encourage significant investment into UK real estate by institutional investors such as Canadian pension funds (including any pension schemes' holding companies) and to continue to provide an exemption from UK tax on gains realised

by overseas pension schemes. Where relevant, we suggest solutions to address our primary concerns for Canadian pension funds.

It is worth noting that Canadian pension funds are exempt from taxation on real estate investments in Canada. In addition, other major jurisdictions have recently moved to exempt overseas pension funds from taxation on the real estate investments in their jurisdictions. In particular, we draw your attention to the Foreign Investment in Real Property Tax Act (“FIRPTA”) changes in 2015, which now allows Canadian pension funds to benefit from a tax exemption in the US when investing in US real estate. It is also worth noting that, due to legislative changes in Germany which will be effective starting in 2018, foreign pension funds should also be able to benefit from a tax exemption in Germany on real estate investments when investing through certain investment funds.

1. Definition of ‘overseas pension scheme’ for the purposes of section 271(1A) TCGA 1992

Section 2.5 of the Consultation Document confirms that non-resident investors currently exempt from UK capital gains tax will continue to be exempt on taxes from UK property. This, in principle, includes direct disposals by ‘overseas pension schemes’ as set out in section 271(1A) TCGA 1992, and as explicitly noted in the Consultation Document.

Canadian pension funds provide retirement benefits to various groups of individuals in Canada. As such, from a policy perspective, we consider that Canadian pension funds fall within the group of investors that should expect to benefit from the exemption contained in section 271(1A) TCGA 1992.

However, the section 271(1A) TCGA 1992 definition of an overseas pension scheme, as supplemented by applicable statutory instruments, is a multi-layered complex definition and its application is not straightforward.

Furthermore, the section 271(1A) TCGA 1992 definition of an overseas pension scheme contains different criteria from those required to:

- i. constitute a qualifying institutional investor for the purposes of the substantial shareholding exemption under paragraph 30A(1), Schedule 7AC TCGA 1992 (“SSE”); or
- ii. constitute an ‘institutional investor’ as per section 528(4A) CTA 2010 of the REIT legislation,

both of which are relevant in the context of UK real estate investments by Canadian pension funds.

We believe using multiple definitions to identify investors, who are expected to meet the same policy objective, creates unnecessary complexity and a compliance burden, particularly for investors exempt from the direct charge.

As such, it would be more simple and clear if the simplest definition could be used for overseas pension schemes. We consider this to be the definition set out in 528(4A) CTA 2010.

2. Direct sales by subsidiaries of Canadian Pension Funds

We appreciate the policy intent of section 2.5 of the Consultation Document which sets out that an overseas pension fund should not be subject to UK tax on the disposal of an investment in UK property where that pension fund is beneficially entitled to the gain.

However, for a number of commercial and legal reasons Canadian pension funds are unlikely to hold property directly and instead may utilize various holding subsidiaries to directly own UK real estate.

This creates a mismatch between a direct disposal of UK real estate by subsidiaries of Canadian pension funds, which we understand would be taxable under the proposals set out in the Consultation Document, and either a direct disposal by Canadian pension funds (which should benefit from the exemption in section 271(1A) TCGA 1992, subject to our concerns above) or a sale of shares by a subsidiary of Canadian pension funds (which we would expect to benefit from the substantial shareholding exemption by virtue of Canadian pension funds being qualifying institutional investor, (“QII”) – see discussion below).

With the exemption for overseas pension schemes on direct disposals remaining following April 2019 and the introduction of a new exemption for QIIs in the updated substantial shareholding exemption provisions, we understand it is not the Government’s intention for overseas pension funds investing in UK immovable property to be chargeable under the proposed rules.

Based on the above, we suggest two options to ensure Canadian pension funds benefit from an exemption from taxation as follows:

- i. the exemption for direct disposals could be extended to include the disposal of UK real estate where a portion of the ultimate owner is an overseas pension fund, subject to tracing provisions similar to those enacted for the SSE. Where there are multiple investors, this benefit should only be prorated to the ownership percentage of exempt investors such as Canadian pension funds, or
- ii. the scope of the new SSE provisions could be extended to include the direct disposal of real estate assets.

3. Tracing provisions for SSE purposes

As discussed above, we understand the policy objective behind these new rules is not to tax gains realised on direct or indirect disposals of UK real estate by overseas pension schemes. We further understand the UK government intends to achieve this by extending

the SSE to cover disposals of shares in companies deriving their value from UK real estate, to non-UK sellers.

There are instances where Canadian pension funds use more than one class of shares in its holding structure to comply with Canadian pension regulations. In addition, the holding structure of Canadian pension funds may include entities such as corporations, partnerships and trusts.

The SSE provides, inter alia, that a company disposing of shares should be exempt from UK tax if 80% of the ordinary share capital is owned by QIIs, paragraph 3A(3), Schedule 7AC TCGA 1992. For these purposes, ownership is traced through corporate structures in accordance with sections 1155 to 1157 CTA 2010.

We are concerned the application of different classes of ordinary shares or the use of trusts may break the chain of ownership when tracing the QII status to a subsidiary.

We recommend the SSE provisions be clarified such that economic ownership is traced through the ownership structure (regardless of corporate vehicle) to determine the proportion of the subsidiaries' shares/interest owned by a QII, similar to the existing provisions contained in section 170 TCGA 1992.

We trust our response has been helpful. Thank you for your attention and please do not hesitate to contact us if you have any questions or concerns.

Yours sincerely,



Brenda King
Chair