

HMRC Clarifies Application of QAHC Regime to Corporate Lending Vehicles

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HMRC has recently updated the guidance relating to the UK's new qualifying asset holding company (**QAHC**) tax regime which was introduced from 1 April 2022. The new guidance clarifies HMRC's approach to whether corporate lending vehicles used by credit funds should be treated as carrying on an investment activity or a trade in the context of the requirement for a QAHC to carry out investment activity with any trading activity being purely ancillary to it, which is considered further below.

The QAHC regime was introduced with a view to increasing the UK's competitiveness as a jurisdiction for asset management. Broadly, the regime aims to provide a tax neutral holding (or, in the context of credit funds, lending) company structure where the relevant conditions are satisfied. The key benefits of the regime include:

- Exemption from withholding tax for all interest payments made by a QAHC;
- Deduction for interest arising on profit-participating (or "results dependent") loans and certain other "special securities" in respect of which interest payments would otherwise be treated as non-deductible distributions;
- Exemption from tax on capital gains realised on the disposal of shares in UK or non-UK companies (provided such companies are not UK-property rich) and non-UK real estate;
- Exemption from stamp duty and SDRT on repurchase of own shares or loan capital;
- Payments by a QAHC on redemption, repayment or purchase of its own shares are not treated as distributions (other than for portfolio company level management); and
- The remittance basis of taxation may be available to fund managers on income and gains from foreign assets held through a QAHC (subject to the special remittance basis rules applicable to carried interest).

The regime is available to UK tax resident companies where at least 70% of the owners are so-called “Category A” investors. Category A investors include certain qualifying funds, QAHCs themselves, certain specified types of investor (including those benefiting from sovereign immunity, pension schemes, charities and authorised persons carrying on long term insurance business), public authorities and certain non-UK companies wholly owned by one or more Category A investors which are not QAHCs.

At a high level, the other conditions for the availability of the regime are:

1. the company’s main activity is carrying on an investment business and any other activities are ancillary to that business and are not substantial;
2. its investment strategy does not involve the acquisition of listed securities; and
3. none of its shares are listed or traded on a recognised stock exchange.

To read more about the details of the QAHC regime and qualifying conditions, please read our submission to the 2021 PIF Annual Review and Outlook [here](#).

So, where a company is engaged in any trading activity, the regime will not be available unless the trade is merely ancillary to the main investment business and is not substantial. Following the introduction of the regime there was some uncertainty among asset managers as to whether credit funds which engage in loan origination (or other activities related to debt) might be considered to be carrying on trading activity and/or whether any fees they received in connection with their main lending activities (such as arrangement fees, facility fees and syndication fees) might be considered to be trading income. If either the basic activity were considered trading or the fees were treated as trading income which was more than insubstantial in the context of the company’s activities as a whole the regime would be unavailable. Depending on the characterisation of standard loan origination activities, this could mean that a significant number of credit funds could not use the regime and this would have had the effect of undermining the policy objectives of the regime in the context of such funds.

Following discussion with industry stakeholders HMRC has updated the relevant section of its [published QAHC guidance](#) in the context of credit funds. In summary, the guidance now confirms that loan origination is not in itself indicative of a trade and that, where loans are originated with the intention of being held on a medium to long term basis as part of the QAHC's investment strategy, it is likely that this will be part of its (main) investment business. With regard to fees, the guidance states that fees that are just a part of originating loans, such as arrangement fees, are likely to be investment income and simply part of that main investment business if the lending itself is an investment activity. However, fees received for arranging loans for others, such as syndication fees, might well be trading income arising from a separate business activity to any investment business that the company might also carry on. The guidance indicates that the best test of whether the syndication fees are ancillary and insubstantial might be the value of those fees relative to the investment returns received by the company.

Similarly, with regard to the acquisition of distressed debt, the updated guidance provides that, where such assets are acquired with the intention of being held for the medium to long term, this is likely to constitute investment activity, even where the assets are disposed of prior to termination of the loan on an opportunistic basis. Conversely, greater levels of activity in relation to distressed assets such as leading a restructuring or insolvency process (and generating fees from such activities) may be indicative of a trade. However, this is a question of fact to be assessed on a case by case basis.

This updated guidance provides a welcome clarification of HMRC's interpretation of how the QAHC legislation should apply to lending/debt acquisition companies set up by credit funds which should provide a high measure of comfort to asset managers in the credit sphere who are considering using QAHCs within their fund structures. The guidance also provides insight on HMRC's view as to whether particular loan related activities constitute trading or investment activities as a general matter and, as such, may be more widely useful for credit funds that do not envisage the use of QAHCs within their structures.

For further information on the QAHC regime, please contact a member of the Proskauer London Tax team.

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