

Improvements to the Real Estate Investment Trust Regime

Who is likely to be affected?

Existing and future real estate investment trusts (REITs).

General description of the measure

The measure will make improvements to the REIT regime by addressing barriers to entry and investment in the regime, and reducing the costs of complying with the requirements of the regime.

Barriers to entry improvements include:

- the entry charge paid by a company joining the regime is to be abolished;
- the requirement for a REIT to be listed on a recognised stock exchange is to be relaxed; and,
- the diverse ownership requirement a REIT has to meet is being reduced.

REIT condition improvements include:

- the rules regarding the REIT's assets are being relaxed to reduce the likelihood that commercial decisions are being influenced by the conditions of the REIT legislation;
- the condition regarding the level of borrowing for a REIT is being made simpler to comply with; and,
- there are also a number of other minor changes to the regime.

Policy objective

This measure helps to support expansion of the property sector and so encourage further investment and stimulate the construction industry.

Background to the measure

REITs are a tax advantaged vehicle introduced to encourage investment in the property sector.

The Government indicated in its response to the consultation *Investment in the UK Private Rented Sector* in September 2010 that it would look further at the barriers to entry to the REITs regime with the view to facilitating, in the longer term, the establishment of residential REITs. Subsequent further consultation with interested parties suggested that the best way to support the REITs industry in general (and the development of residential REITs in particular) was in part to reduce barriers to entry for new REITs and to ensure that the regime does not inhibit good business practice.

To date over 20 REITs have been created with particular focus on commercial property investment.

This measure was announced at Budget 2011 and a subsequent informal consultation on the measure took place between 5 April 2011 and 10 June 2011.

Detailed proposal

Operative date

The measure as it relates to the barriers to entry to the regime will have effect for companies that join the regime on or after the date of Royal Assent to Finance Bill 2012. For the balance of the measures they will have effect for REITs in the regime on or after the date of Royal Assent to Finance Bill 2012.

Current law

All legislative references are to the Corporation Tax Act 2010 unless otherwise indicated.

Section 528 requires that a REIT is listed on a recognised stock exchange (the listing requirement).

Section 528 also requires that a REIT is not a close company, that is, a REIT cannot be controlled by a small number of people (the non close company requirement).

Section 530 requires that a REIT distributes 90 per cent of its profits from its property rental business to investors (the distribution requirement)

Section 531 ensures that a REIT is primarily a property investment company by requiring that profits and assets of the property rental business of the REIT are 75 per cent or more of the total profit or assets of the REIT (the balance of business test).

Section 538 requires a company joining the REIT regime to pay a conversion charge equivalent to two per cent of the value of its assets involved in its property rental business (the entry charge).

Section 543 restricts the amount of borrowing undertaken by a REIT in respect of its property rental business by charging to tax the amount by which its financing costs exceed a limit (the profit financing cost ratio).

Section 556 determines the treatment of assets involved in the property rental business and when disposal of the asset by the REIT does not benefit from the exemption from tax.

Proposed revisions

Legislation will be introduced in Finance Bill 2012 to make the following changes:

The listing requirement will be relaxed so that REITs can be listed on trading platforms such as AIM, Plus and their foreign equivalents.

The non close company requirement will be amended to allow a new REIT time to meet this requirement. The non close company requirement will also be relaxed so that certain institutional investors will not make a company close for the purposes of the REIT regime. The amended legislation will list the types of institutional investors that will not make the REIT a close company. There will be a power to make regulations to add, modify or remove categories of investors to or from the list.

The distribution requirement will be amended to ensure that tax is charged at the correct time.

The balance of business test, as it applies to assets, will be relaxed so that cash will be added to the assets of the property rental business for the purpose of the balance of business test.

The conversion charge will be abolished.

The profit finance cost ratio will be amended so that financing costs will consist only of interest. The amount of tax paid when financing costs exceed the limit will be restricted to a proportion of the property profits.

The legislation will make clear that the section 556 treatment of assets disposed of will not apply where the disposal is to a company that is part of the same REIT group.

Summary of impacts

Exchequer impact (£m)	2011-12	2012-13	2013-14	2014-15	2015-16
	-	negligible	negligible	negligible	negligible
	This measure is expected to have a negligible impact on the Exchequer. Any impact will be set out at Budget 2012.				
Economic impact	The measure should facilitate increased investment in REITs and the private rental sector. This may in turn stimulate the construction sector. No significant macroeconomic impacts are anticipated.				
Impact on individuals and households	This measure will not impact on individuals and households as it only concerns REITs.				
Equalities impacts	The change only affects companies that elect to join the REIT regime and not individuals. It is therefore considered that these proposals have no effect on protected equality groups.				
Impact on business including civil society organisations	With the aim of encouraging new REITs, the measure will make entry to the REIT regime easier by abolishing the entry charge, and relaxing the close company and listing requirements. The changes also better align the regime conditions with a REIT's commercial needs by changing how cash is dealt with for the balance of business asset test, and by removing one-off costs from the profit financing cost ratio. These changes have a negligible impact on compliance costs because the changes only affect a small number of businesses.				
Operational impact (£m) (HMRC or other)	No operational impact is expected to be caused by the measure.				
Other impacts	The potential for other impacts has been considered and none have been identified.				

Monitoring and evaluation

HMRC will continue to monitor the REIT industry and seek to maintain a dialogue with it to establish the impact of the changes.

Further advice

If you have any questions about these changes, please contact Tony Linehan on 020 7147 0527 (email: tony.linehan@hmrc.gsi.gov.uk).

1 Real estate investment trusts

Schedule 1 makes provision about real estate investment trusts.

SCHEDULES

SCHEDULE 1

Section 1

REAL ESTATE INVESTMENT TRUSTS

Introduction

- 1 Part 12 of CTA 2010 (real estate investment trusts) is amended as follows.

Being a UK REIT: conditions for company - close companies

- 2 (1) Section 525 (becoming a UK REIT: supplementary provision) is amended as follows.
- (2) In subsection (1)(c) for “the conditions” substitute “conditions A, B, C, E and F”.
- (3) In subsection (4)(a) omit “D,”.
- (4) Omit subsections (5) to (8).
- 3 (1) Section 527 (being a UK REIT in relation to an accounting period) is amended as follows.
- (2) After subsection (4) insert—
- “(5) Subsections (2)(a) and (3)(a) are also subject to subsections (6) to (8).
- (6) If the accounting period ends during the first 3-year period, condition D in section 528 does not have to be met.
- (7) If the accounting period begins, but does not end, during the first 3-year period, condition D in section 528 only has to be met throughout the part of the accounting period falling after the end of the first 3-year period.
- (8) In subsections (6) and (7) “the first 3-year period” means the period of 3 years beginning with the date specified in the notice given under section 523 or 524.”
- 4 (1) Section 528 (conditions for company) is amended as follows.
- (2) In subsection (4)—
- (a) omit the “or” after paragraph (a), and
- (b) after paragraph (b) insert “, or
- (c) is a close company only because it has an institutional investor as a participator (within the meaning given by section 454)”.

(3) After subsection (4) insert –

“(4A) “Institutional investor” means any of the following persons –

- (a) the trustee or manager of –
 - (i) an authorised unit trust scheme (as defined in section 237(3) of FISMA 2000), or
 - (ii) a unit trust scheme (as defined in section 237(1) of FISMA 2000) which is authorised under the law of a territory outside the United Kingdom in a way which makes it, under that law, the equivalent of an authorised unit trust scheme (as defined in section 237(3) of that Act);
- (b) a company –
 - (i) which is an open-ended investment company (as defined in section 236(1) of FISMA 2000) incorporated by virtue of regulations under section 262 of that Act, or
 - (ii) which is incorporated under the law of a territory outside the United Kingdom and is, under that law, the equivalent of an open-ended investment company (as defined in section 236(1) of FISMA 2000);
- (c) the trustees or managers of a pension scheme (as defined in section 150(1) of FA 2004);
- (d) a person acting in the course of a long-term insurance business (that is, the activity of effecting or carrying out contracts of long-term insurance within the meaning of the Financial Services and Markets (Regulated Activities) Order 2001 (S.I. 2001/544)) who –
 - (i) is authorised under FISMA 2000 to carry on such business, or
 - (ii) has an equivalent authorisation under the law of a territory outside the United Kingdom to carry on such business;
- (e) a person who cannot be liable for corporation tax or income tax (as relevant) on the ground of sovereign immunity.

(4B) The Treasury may by regulations amend the definition of “institutional investor” by inserting, omitting or amending a description of person in subsection (4A).”

- 5 (1) Section 558 (demergers: disposal of asset) is amended as follows.
 - (2) In subsections (3) and (6) for “C to F” substitute “C, E and F”.
- 6 (1) Section 559 (demergers: company leaving group UK REIT) is amended as follows.
 - (2) In subsections (6) and (9) for “C to F” substitute “C, E and F”.
- 7 (1) Section 561 (notice of breach of relevant Chapter 2 condition) is amended as follows.

- (2) After subsection (4) insert –
- “(5) The following subsections apply in relation to condition D in section 528.
 - (6) In accordance with section 527(6) and (7), a notification does not have to be given under subsection (1) or (2) if condition D ceases to be met during the first 3-year period.
 - (7) If condition D is not met at the start of the first day after the end of the first 3-year period, for the purposes of subsections (1) to (4) condition D is treated as having ceased to be met at the start of that day.
 - (8) In subsections (6) and (7) “the first 3-year period” has the meaning given by section 527(8).”
- 8 (1) Section 562 (breach of conditions C and D in section 528) is amended as follows.
- (2) In the heading for “**conditions C and D**” substitute “**condition C**”.
 - (3) In subsection (1) for the words from “or D” to “conditions)” substitute “in section 528”.
 - (4) In subsection (2) –
 - (a) for “both conditions C and D are” substitute “condition C is”, and
 - (b) for “breaches are” substitute “breach is”.
 - (5) Omit subsections (3) and (4).
 - (6) In subsection (5) –
 - (a) in paragraph (a) for “either condition C or D” substitute “condition C”, and
 - (b) in paragraph (b) omit “or (3)”.
- 9 After section 562 insert –
- “562A Breach of condition D in section 528 (conditions for company)**
- (1) This section makes provision about cases relating to breaches of condition D in section 528 in relation to –
 - (a) the principal company of a group UK REIT, or
 - (b) a company UK REIT.
 - (2) In accordance with section 527(6) and (7), a breach of condition D during the first 3-year period is to be ignored.
 - (3) If condition D is not met at the start of the first day after the end of the first 3-year period, the group or company (as the case may be) is to be treated as having ceased to be a UK REIT at the end of the first 3-year period.
 - (4) If condition D is not met at any time after the start of the day mentioned in subsection (3), the group or company (as the case may be) is to be treated as having ceased to be a UK REIT at –
 - (a) the end of the accounting period preceding the accounting period in which the breach began, or
 - (b) if later, the end of the first 3-year period.

- (5) Neither subsection (3) nor subsection (4) applies if condition D is not met as a result of –
 - (a) the principal company of a group UK REIT becoming a member of another group UK REIT, or
 - (b) a company UK REIT becoming a member of a group UK REIT,and, accordingly, the breach is to be ignored.
 - (6) Subsection (4) does not apply if –
 - (a) condition D is not met as a result of anything done (or not done) by a person other than the company in question, and
 - (b) the company remedies the breach not later than the end of the accounting period after that in which the breach began,and, accordingly, the breach is to be ignored.
 - (7) But if, in a case within subsection (6), the breach of condition D is not remedied by the time mentioned in that subsection, the group or company (as the case may be) is treated as having ceased to be a UK REIT at the end of the accounting period in which the breach began.
 - (8) In this section “the first 3-year period” has the meaning given by section 527(8).”
- 10 (1) Section 572 (termination by notice given by HMRC) is amended as follows.
- (2) In subsection (2) after “573,” insert “573A,”.
 - (3) After subsection (5) insert –

“(5A) Subsection (4)(a) has effect subject to section 573A(4).”
- 11 After section 573 insert –

“573A Notice under section 572: condition D in section 528 not met

- (1) An officer of Revenue and Customs may give a notice under section 572(1) if –
 - (a) at any time during the first 3-year period, condition D in section 528 is not met, and
 - (b) as at that time, subsection (2) has applied to a member of the group or the company (as the case may be) for a period exceeding 3 years or for a number of periods which in total exceed 3 years.
- (2) This subsection applies to a company at any time when –
 - (a) the company is, or is a member of, a UK REIT,
 - (b) condition D in section 528 is not met in relation to the UK REIT, and
 - (c) the first 3-year period in relation to the UK REIT has not ended.
- (3) Subsection (4) applies if –
 - (a) a company ceases to carry on a business (“the transferred business”) which it carried on at a time (“the relevant time”) when subsection (2) applied to the company, and
 - (b) another company (“company X”) begins to carry on the transferred business.

- In paragraph (a) the reference to a business includes a part of a business.
- (4) Subsection (2) is to be taken to have applied to company X at the relevant time (including for the purposes of subsection (3)(a) if company X subsequently ceases to carry on the transferred business (or a part of it)).
 - (5) In this section “the first 3-year period” has the meaning given by section 527(8).
 - (6) If a notice is given under section 572(1) in a case within this section, subsection (7) applies instead of section 572(4)(a).
 - (7) The group or company (as the case may be) is to be taken to have ceased to be a UK REIT on –
 - (a) the first day of accounting period 1, or
 - (b) such later day as may be specified by the officer of Revenue and Customs in the notice.”
- 12 (1) Section 577 (multiple breaches of conditions in Chapter 2) is amended as follows.
- (2) In subsection (5)(a) –
 - (a) omit “and (3)”, and
 - (b) before “section 563(2)” insert –
“section 562A(5) and (6),”.
 - (3) In subsection (7) –
 - (a) in paragraph (b) omit “or D” and “or (5) to (7)”, and
 - (b) in paragraph (c) for “C to F” substitute “C, E and F”.
 - (4) After subsection (7) insert –
“(8) In accordance with section 527(6) and (7), a breach of condition D in section 528 during the first 3-year period (as defined in section 527(8)) is also to be ignored for the purposes of this section.”
- 13 (1) The amendments made by paragraph 2 have effect in relation to notices given under section 523 or 524 specifying a date which is on or after the day on which this Act is passed.
- (2) The amendments made by paragraphs 3 to 12 have effect in relation to –
 - (a) groups of companies in respect of which notices are given under section 523 specifying a date which is on or after the day on which this Act is passed, and
 - (b) companies which give notices under section 524 specifying a date which is on or after the day on which this Act is passed.

Being a UK REIT: conditions for company - trading of shares on recognised stock exchange

- 14 (1) Section 527 (being a UK REIT in relation to an accounting period) is amended as follows.
- (2) In subsections (2) and (3) after paragraph (a) insert –
“(aa) the condition in section 528A (trading of shares on recognised stock exchange) must be met in relation to the period,”.

- 15 (1) Section 528 (conditions for company) is amended as follows.
(2) In subsection (3) for “listed” substitute “admitted to trading”.
- 16 After section 528 insert –
- “528A Condition as to trading of shares on recognised stock exchange**
- (1) In the case of a group UK REIT, the condition in this section is met in relation to an accounting period if shares forming the principal company’s ordinary share capital are traded on a recognised stock exchange during the period.
- (2) In the case of a company UK REIT, the condition in this section is met in relation to an accounting period if shares forming the company’s ordinary share capital are traded on a recognised stock exchange during the period.”
- 17 (1) Section 561 (notice of breach of relevant Chapter 2 condition) is amended as follows.
(2) In subsection (3) before “conditions A and B in section 529” insert –
“the condition in section 528A (trading of shares on recognised stock exchange),”.
- 18 Before section 563 insert –
- “562B Breach of condition as to trading of shares on recognised stock exchange**
- (1) This section applies if the condition in section 528A (trading of shares on recognised stock exchange) is not met in relation to an accounting period.
- (2) The group or company (as the case may be) is to be treated as having ceased to be a UK REIT at the end of the previous accounting period.”
- 19 The amendments made by paragraph 14 to 18 have effect in relation to –
- (a) groups of companies in respect of which notices are given under section 523 specifying a date which is on or after the day on which this Act is passed, and
- (b) companies which give notices under section 524 specifying a date which is on or after the day on which this Act is passed.

Being a UK REIT: condition as to distribution of profits

- 20 (1) Section 530 (condition as to distribution of profits) is amended as follows.
(2) In subsection (6D) for “three” substitute “6”.
- 21 After section 530 insert –
- “530A Condition as to distribution of profits: increase in profits after delivery of tax return**
- (1) Section 530(1) applies subject to subsection (2) below in relation to an accounting period if –
- (a) the principal company of the group delivered with its tax return for the period the financial statement under section

-
- 532(2)(b) showing the amount of the UK profits of the group arising in the period, and
- (b) as at the relevant date, those profits have been increased from the amount originally shown in the statement.
- (2) Any distribution of those profits made by the principal company before the end of the relevant period is to be treated as having been made within the deadline set by section 530(1)(c).
- (3) But the total amount of profits that may be treated as having been distributed within that deadline by virtue of subsection (2) is limited to 90% of the amount of the increase in profits.
- (4) In subsections (1) and (2) (and this subsection) –
 “the relevant date” means the date on which the principal company’s tax return can no longer be amended,
 “the relevant period” means the period of 3 months beginning with the relevant date, and
 “UK profits” has the meaning given by section 530(2).
- (5) Section 530(4) applies subject to subsection (6) below in relation to an accounting period if –
 (a) the company delivered its tax return for the period showing the amount of the profits of its property rental business arising in the period as calculated in accordance with section 599, and
 (b) as at the relevant date, those profits have been increased from the amount originally shown in the return.
- (6) Any distribution of those profits made before the end of the relevant period is to be treated as having been made within the deadline set by section 530(4)(b).
- (7) But the total amount of profits that may be treated as having been distributed within that deadline by virtue of subsection (6) is limited to 90% of the amount of the increase in profits.
- (8) In subsections (5) and (6) (and this subsection) –
 “the relevant date” means the date on which the company’s tax return can no longer be amended, and
 “the relevant period” means the period of 3 months beginning with the relevant date.
- (9) In this section “distribution” is to be read in accordance with section 530(6A) and (6B).”
- 22 (1) Section 564 (breach of condition as to distribution of profits) is amended as follows.
- (2) Omit subsections (5) to (8).
- 23 (1) Section 565 (which defines the amount to be charged to corporation tax where there is a breach of the condition in section 530) is amended as follows.
- (2) In subsections (2) and (3), in the definition of “D” –
 (a) for “on or before” substitute “within”,

- (b) in paragraph (a) for “filing date referred to in” substitute “deadline set by”, and
 - (c) in paragraph (b) for “date specified” substitute “deadline set”.
- (3) After subsection (3) insert –
 - “(4) The definition of “D” in subsections (2) and (3) needs to be read with section 530A (so far as applicable).”
- 24 (1) The amendment made by paragraph 20 has effect in relation to distributions made on or after the day on which this Act is passed.
- (2) The amendments made by paragraphs 21 to 23 have effect in relation to accounting periods starting on or after the day on which this Act is passed.

Being a UK REIT: conditions as to balance of business

- 25 (1) Section 531 (conditions as to balance of business) is amended as follows.
- (2) For subsection (5) substitute –
 - “(5) Condition B is that at the beginning of the accounting period the sum of –
 - (a) the value of the assets relating to property rental business, and
 - (b) the value of the assets relating to residual business so far as consisting of cash,is at least 75% of the total value of assets held by the group or company (as the case may be).”
- (3) In subsection (6)(b) after “business” insert “(and the amount of the group’s cash is to be determined accordingly)”.
- (4) After subsection (7) insert –
 - “(8) In this section “cash” means –
 - (a) money held on deposit (whether or not in sterling),
 - (b) stocks or bonds of any description included in Part 1 of Schedule 11 to FA 1942 (gilts), or
 - (c) money held in any other way, or any investment of any other form, specified in regulations made by the Commissioners for Her Majesty’s Revenue and Customs.”
- 26 (1) Section 547 (funds awaiting reinvestment) is amended as follows.
- (2) Omit subsection (3).
- 27 The amendments made by paragraphs 25 and 26 have effect in relation to accounting periods starting on or after the day on which this Act is passed.

Abolition of entry charge

- 28 Omit sections 538 to 540 (entry charge).
- 29 (1) Section 545 (cancellation of tax advantage) is amended as follows.
- (2) In subsection (5) omit the words from “(and includes,” to “538)”.
- 30 (1) Section 556 (disposal of assets) is amended as follows.

- (2) Omit subsection (4).
- 31 (1) Section 558 (demergers: disposal of asset) is amended as follows.
(2) In subsection (4) omit “and section 538 (entry charge)”.
- 32 (1) Section 559 (demergers: company leaving group UK REIT) is amended as follows.
(2) In subsection (8) omit “section 538 (entry charge),”.
- 33 (1) Section 583 (overview of Chapter 10 relating to joint ventures) is amended as follows.
(2) Omit subsection (4)(b).
- 34 Omit sections 595 to 597 (additional entry charges in cases involving joint ventures) and the italic heading before section 595.
- 35 The amendments made by paragraphs 28 to 34 have effect in relation to companies whose entry is on or after the day on which this Act is passed.

Financing cost ratio

- 36 (1) Section 543 (financing cost ratio) is amended as follows.
(2) In subsection (1) after “period” insert “(unless it is nil or a negative amount)”.
(3) For subsection (3) substitute –
 “(3) The excess is charged to corporation tax in relation to the accounting period under the charge to corporation tax on income.
(3A) “The excess” means –
 (a) the amount equal to –
 (i) PFC, minus
 (ii) the property financing costs which would cause the calculation in subsection (2) to equal 1.25 for the accounting period, or
 (b) if less, the amount equal to 20% of PP.”
- 37 (1) Section 544 (meaning of “property financing costs” etc) is amended as follows.
(2) In subsection (3) –
 (a) in paragraph (a) –
 (i) for “the financing costs” substitute “interest on loans”, and
 (ii) for “excluding financing costs” substitute “excluding interest”, and
 (b) in paragraph (b) for “the financing costs” substitute “interest on loans”.
(3) In subsection (4) for ““financing costs” means the cost of debt finance” substitute ““loan” has the same meaning as in Part 5 of CTA 2009 (see section 476(1) of that Act)”.
(4) Omit subsection (5).

- 38 The amendments made by paragraphs 36 and 37 have effect for accounting periods starting on or after the day on which this Act is passed.

Disposal of assets

- 39 (1) Section 556 (disposal of assets) is amended as follows.
- (2) In subsection (1) –
- (a) omit the “and” after paragraph (a), and
 - (b) after paragraph (b) insert “, and
 - (c) if the company is a member of a UK REIT, the disposal is not to another member of the UK REIT”.
- (3) In subsection (3) –
- (a) omit the “and” after paragraph (b), and
 - (b) after paragraph (c) insert “, and
 - (d) if the company is a member of a UK REIT, the disposal is not to another member of the UK REIT”.
- 40 The amendments made by paragraph 39 have effect in relation to disposals occurring on or after the day on which this Act is passed.

EXPLANATORY NOTE

IMPROVEMENTS TO THE REIT REGIME

SUMMARY

1. This clause and Schedule amend Part 12 (Real Estate Investment Trusts) (REIT) of the Corporation Tax Act 2010 (CTA 2010). The amendments relax the conditions of entry to the REIT regime and relax requirements while in the regime.

DETAILS OF THE SCHEDULE

2. Paragraph 1 introduces amendments to Part 12 of CTA 2010. All references to amendments to legislation are to Part 12 CTA 2010 [unless otherwise stated].
3. Paragraph 2 amends section 525 which requires a company or group that gives a notice to be a REIT to include in the notice a statement that it can meet the REIT regime conditions, including those in section 528 (the company conditions). The amendments change the form of the notice to be given to reflect the changes being made to section 528 as detailed at 6 and 7 below.
4. Paragraph 3 amends section 527 which sets out the conditions for being a REIT in an accounting period. Condition D in section 528, which states that a REIT cannot be a close company, will not apply for the first three years after a company joins the regime.
5. Paragraph 4 amends Condition D in section 528, that a REIT cannot be a close company, so that the shareholding of an institutional investor will not, on its own, make a company close for REIT purposes. Paragraph 4 also introduces a new subsection 4A which defines what an institutional investor is for these purposes. In addition new subsection 4B grants a power to make Regulations concerning the definition of who is or is not to be regarded as an ‘institutional investor’ for the purposes of this section.
6. Paragraphs 5-6 make changes to sections 558 and 559, which cover how the demerger of a REIT is dealt with, to accommodate the changes being made to the conditions to be met by a REIT in section 527.
7. Paragraphs 7-8 amend sections 561 and 562 which deal with breaching the REIT conditions, including those in section 528, so that the REIT does not have to give notice that it has not met condition D

of section 528 in the first three years after joining the regime as a consequence of the amendment to section 527.

8. Paragraph 9 introduces a new section 562A which determines the circumstances when a breach of Condition D in section 528 is either to be ignored or to result in the REIT leaving the regime.
9. Paragraphs 10 and 11 amend section 572 which deals with notices to leave the regime and introduce new section 573A, so that a notice to leave the regime can be issued in certain circumstances where condition D in section 528 is not met.
10. Paragraph 12 amends paragraph 577, which deals with multiple breaches of the conditions by which a company or a group qualifies as a REIT, to reflect the changes being introduced to condition D of section 528.
11. Paragraph 13 sets out that the changes in paragraphs 2 – 12 will apply to those electing to become REITs with effect from on or after the date of Royal Assent to the Finance Bill.
12. Paragraphs 14-18 amend section 528(3), the REIT company condition that requires that shares in the company are listed on a recognised stock exchange. The amendment is to allow that shares are admitted to trading on a recognised stock exchange and a new section 528A is introduced which requires that such shares are traded. The introduction of new section 562B deals with the consequence of not meeting the trading condition in new section 528A, which will be that the group or company will cease to be a REIT.
13. Paragraph 19 sets out that the changes in paragraphs 14-18 will apply to those electing to become REITs with effect from on or after the date of Royal Assent to the Finance Bill.
14. Paragraph 20 amends section 530 which requires that 90% of the profits of the property rental business have to be distributed by the date at which the REIT's tax return is filed. This is referred to as the 'distribution requirement'. The amendment extends the date by which profits have to be distributed from three months after the filing date to six months after the filing date. This amendment only applies in particular circumstances where a stock dividend has been issued and a market value of the stock dividend has had to be used in accordance with section 530(6C)(b) and this has caused the distribution requirement not to be met.
15. Paragraph 21 introduces a new section 530A which deals with how the distribution requirement (see 15 above) is to be met in situations where profits of the property rental business are increased after the tax return has been submitted. This clarifies under what

circumstances additional time is given to meet the distribution requirement and when a charge to tax for not meeting the distribution requirement can be made.

16. Paragraphs 22-24 amend sections 564 and 565, which charge tax on the amount by which the distribution requirement is not met. The amendments clarify when a charge to tax can be made when the distribution requirement is not met and include the circumstances where the time limit is extended under section 530 or new section 530A. These changes apply to distributions made on or after the date of Royal Assent to the Finance Bill.
17. Paragraph 25-27 amends section 531 'conditions as to the balance of business'. This section requires that at the beginning of an accounting period, the REITs profits and assets are primarily derived from and involved in its property rental business. Currently Condition B in section 531 requires that at least 75% of the assets of the group or company relate to the property rental business. Following amendment the requirement will be that cash and assets involved in the property rental business should be at least 75% of the total assets of the business. The change will apply to accounting periods beginning on or after Royal Assent.
18. Paragraphs 28-35 abolish the entry charge for companies entering the REIT regime. The abolition applies to those companies that enter the regime on or after the date of Royal Assent to the Finance Bill.
19. Paragraphs 36-38 amend sections 543 and 544 which limit the amount of property financing costs that a REIT can pay in connection with its tax exempt business. For accounting periods starting on or after the date of Royal Assent to the Finance Bill, the limit will be based on interest on loans and will exclude the costs of arranging loan finance, and other accounting costs will no longer be included. The amendments also limit the amount charged to corporation tax under section 543 (4) to an amount equal to 20% of the property profits.
20. Paragraph 39-40 amends section 556 which deals with the tax treatment of an asset of the property rental business that is disposed of by way of a trade (ie the disposal is taxed). The amendment ensures that section 556 does not apply to disposals made to another member of the REIT. The amendment takes effect where the disposal is on or after the date of Royal Assent to the Finance Bill.

BACKGROUND NOTE

21. REITs are a tax advantaged vehicle introduced to encourage investment in the property sector. REITs are exempted from

corporation tax on the profits and gains arising from their property rental business. REITs have to distribute 90% of the profits of the property rental business to shareholders in whose hands this income is treated as income from property. In this way taxation of income from property is moved from the corporate level to the investor level.

22. The REIT regime was introduced in FA 2006. The legislation was subsequently rewritten to CTA 2010. To date, over 20 REITs have been created with particular focus on commercial property investment.
23. The Government indicated in its response to the 2010 Private Rental Sector consultation that it would look further at the barriers to entry to the REIT regime with the view to facilitating, in the longer term, the establishment of residential REITs. Subsequent further consultation with interested parties suggested that the best way to support the REITs industry in general (and the development of residential REITs in particular) was among other things, to reduce barriers to entry for new REITs and to ensure that the regime does not inhibit good business practice.
24. If you have any questions about this change, or comments on the legislation, please contact Tony Linehan on 020 7147 0527 (email: tony.linehan@hmrc.gsi.gov.uk).