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BRIEFING

CHANGES TO DOUBLE TAXATION TREATY PASSPORT

APRIL 2017

- AS OF 6 APRIL 2017 THE DTTP SCHEME HAS BEEN SIMPLIFIED AND WIDENED TO UK NON-CORPORATE BORROWERS AND SOME FOREIGN NON-CORPORATE LENDERS
- THIS SHOULD MAKE IT EASIER TO LEND TO UK BORROWERS BY REDUCING ADMINISTRATIVE BARRIERS AND COSTS FOR OVERSEAS LENDERS

The Double Taxation Treaty Passport ("DTTP") scheme has improved the system for lenders and borrowers accessing treaty relief from UK withholding tax. The scheme has now been extended to cover a broader range of borrowers (including partnerships) and non-corporate lenders.

Summary

- On 6 April 2017, the Government issued updated Terms and Conditions ("T&Cs") and guidance that have simplified and widened access to the DTTP scheme.
- Prior to the DTTP scheme, the only way to obtain relief from withholding tax on UK source interest paid to non-UK residents on unlisted debt was through a lengthy double taxation treaty application, which had to be repeated each time a new loan was made by the same lender or if a new lender became a party.
- The DTTP scheme, introduced in 2010, streamlined the process by allowing lenders to obtain a DTTP, entitling a lender to simply provide a UK borrower with their passport number when it makes a loan. The borrower then only has to inform HMRC and treaty clearance typically follows within 30 days.
- The DTTP scheme was initially accessible only to corporate borrowers and non-UK corporate lenders.
- However, thanks to its popularity (around 3,000 passports have been issued since 2010), and as a result of responses to a Consultation issued by HMRC, the DTTP scheme has been widened. It now provides a route for all UK non-corporate borrowers and some foreign non-corporate lenders, to obtain the benefit of

double tax treaty relief in the UK without the administrative hassle of a full double tax treaty application.

- Lenders that currently have a DTTP will not have to obtain a new passport as a result of the updated T&Cs.

Position without a passport

The UK imposes a 20% withholding tax on certain interest payments.

In the absence of relief, there is a risk of double taxation as the interest could be taxed in the UK (through the withholding) and again in the jurisdiction where the lender is resident.

Lenders can also suffer a cash flow cost even if they obtain credit for withholding tax.

“OBTAINING TREATY RELIEF WITHOUT A PASSPORT IS A LENGTHY PROCESS AND OFTEN SUBJECT TO DELAYS.”

A lender may be entitled to relief in respect of all or some of any withholding if the jurisdiction where it is resident has a double taxation treaty with the UK.

Double tax treaties often include provisions that aim to reduce or eliminate double taxation of income arising in one jurisdiction and paid to a resident of another.

Although a useful and reliable route to exemption from withholding tax, the double taxation treaty procedure is lengthy and often subject to delays.

The lender must complete a detailed form that is first sent to its own tax authority, which confirms the lender is a resident, and the form is then sent to HMRC. Once the form is received and processed, HMRC will normally issue a Direction to the borrower to pay interest without the need for withholding. This process can take over six months to complete, and can be unattractive to borrowers and lenders, particularly if it necessitates postponement of an interest payment date on the loan.

The DTTP scheme

“THE DTTP SCHEME HAS STREAMLINED THE ADMINISTRATIVE PROCESS FOR FOREIGN LENDERS LENDING TO UK CORPORATE BORROWERS.”

The DTTP scheme has streamlined the administrative process for foreign lenders lending to UK corporate borrowers.

By applying for its DTTP, an overseas lender can obtain a one-off certification that, in effect, entitles it to the benefit of a double tax treaty between its jurisdiction of residence and the UK. This DTTP is valid for five years, and can easily be renewed provided the lender's status or circumstances have not changed materially.

A passported lender needs only to provide its passport number to the borrower – it does not need to file any forms or liaise with its home tax authority.

The borrower then must notify HMRC that it is entering into a loan agreement with a DTTP holder using the short and simple DTTP2 form.

The approval process is, as a result, far quicker and less administratively burdensome.

“ALL TYPES OF UK BORROWERS MAY NOW MAKE USE OF THE SCHEME.”

Changes to the DTTP scheme

The DTTP scheme has been a success and the Government/HMRC have confirmed their commitment to it and extended the scheme.

The main improvements are:

1. all UK borrowers including UK partnerships, individuals and charities may now use the scheme (as it is no longer limited to corporate borrowers);
2. sovereign wealth funds and pension funds that are using tax treaty withholding rates/exemptions may be admitted into the scheme on the same grounds as other lenders; and
3. transparent entities (including partnerships) may be admitted to the scheme as lenders where all of the constituent beneficial owners of the income are entitled to the same treaty benefits under the same double taxation treaty.

For loans entered into between 1 September 2010 and 5 April 2017, only loan interest payments made by UK corporate borrowers fall within the scheme. These loans are still subject to the old DTTP T&Cs.

A guarantor may also use the scheme, and the date from which the guarantee is called is treated as the start of a new loan for which a DTTP may be used.

The borrower can access and submit the DTTP2 form to HMRC online. If the DTTP2 form is submitted before the first interest payment date and the online filing process has been used and acknowledged by HMRC, the borrower may, if it wishes, withhold at the relevant treaty rate in advance of receiving a formal Direction.

If a UK borrower has a loan with frequently changing multiple lenders, HMRC is willing to consider entering into arrangements with that borrower whereby individual notifications can be swept up into one monthly DTTP2A notification.

The DTTP scheme is not extended to sovereign lenders that are relying on sovereign immunity (as opposed to sovereign wealth funds claiming relief under a double tax treaty) on the basis that no administrative simplification is achieved.

A positive effect

The scheme has been a success and it is helpful that access to the scheme has been widened significantly. The scheme now applies to more lenders and borrowers, and is not restricted to corporate lenders and corporate UK borrowers. This should have a positive effect on the UK's debt markets by helping to reduce the administrative barriers and costs for overseas lenders, making it easier to lend to UK borrowers.

FOR MORE INFORMATION

Should you like to discuss any of the matters raised in this Briefing, please speak with the authors below or your regular contact at Watson Farley & Williams.

RICHARD STEPHENS
Partner, London
D +44 20 7814 8239
rstephens@wfw.com

CLARE VIVIAN
Trainee, London
D +44 20 3314 6340
cvivian@wfw.com

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