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7 September 2011

Dear Ms. Hamilton and Hay,

HMRC - Consultation on Potential Debt Cap Changes for Finance Bill 2012 – HMRC Technical Note of 14 June 2011

INTRODUCTION

The Quoted Companies Alliance (QCA) is a not-for-profit membership organisation working for small and mid-cap quoted companies. Their individual market capitalisations tend to be below £500m.

The Quoted Companies Alliance is a founder member of European Issuers, which represents over 9,000 quoted companies in fifteen European countries.

The QCA Tax Committee has examined your proposals and advised on this response. A list of committee members is at Appendix A.

RESPONSE

We welcome the opportunity to respond to this technical note. We appreciate that the technical note is focused on specific points. Before turning to these we would make some general observations on the Debt Cap rules and their impact on small and mid-cap quoted companies.

We understand the Government's intentions in introducing the Debt Cap rules and would not disagree with the principle of restricting UK tax deductions in respect of interest to a level commensurate with external borrowings.

Many of our members fall within the ambit of the debt cap rules. The legislation is lengthy and complex and in our experience, it is often very time consuming for taxpayers to collate the relevant information and perform the detailed calculations. We are concerned that this results in a significant compliance burden and costs which is disproportionate for small and mid-cap quoted companies.

Furthermore, this compliance burden applies even where it is clear at the outset that no net adjustment will be required. Similarly, the calculation of the gateway test is such that many groups fail it and are required to incur additional time and costs in performing the detailed calculations, even though ultimately there may be no net adjustment.

We would therefore welcome any steps which could simplify the process and reduce the compliance burden for small and mid-cap quoted companies. More specifically:

- The exclusion of debtors less than £3m (TIOPA 2010 s262(3)) often causes the gateway test to be failed. An example is given in the HMRC Manuals at CFM90690 of the effect of a balance between UK group companies. The HMRC manuals note this was deliberate to ensure the rules do not infringe freedoms established by the EC Treaty of Rome. Failing the gateway test creates significant additional compliance work and costs for many groups in doing the full calculations We suggest that consideration is given means of avoiding the gateway test being failed unnecessarily whilst respecting EC requirements, perhaps by eliminating the exclusion of debtor balances of less than £3m so that, effectively the gateway test is on a total UK net debt basis. If necessary, this exclusion could be restricted to groups which meet certain size criterion.

- The need to undertake calculations on an entity by entity basis significantly increases the amount of information required and time to perform the calculations. We suggest that consideration is given to ways of simplifying this, perhaps in certain circumstances for groups below a certain size threshold, to calculate net debt on the basis of UK consolidated group accounting figures.

- The calculation of the gateway test can be very time consuming even if it is clear at the outset that the test will be failed. We suggest consideration is given to making the gateway test optional and permitting groups, if they so wish, to go straight to the detailed calculations.

We would also flag that we are concerned that the debt cap rules could encourage behaviour's which are not necessarily in line with a group's commercial objectives. In particular:

- The rules create and on-going requirement to monitor a group's debt position in order to ensure that financing arrangements do not inadvertently result in interest restrictions.

- As noted above, UK intra group balance could cause the gateway test to be failed so groups may seek to minimise or eliminate such balances even if there is no commercial rationale to do so.

- The rules could encourage a group to maintain external debts rather than pay them down.

Whilst it is difficult to see "quick fixes" for these issues we would be pleased to meet with you to explore these issues further. Turning to the specific points raised in the technical note:

De minimis amount

1. Do you think that there is a need to address this issue?

   We note the comments and that the impact of this for a small or mid-cap quoted company could be proportionately greater than for a larger company/group and would therefore support measures to eliminate any potential disallowance.

2. If so do you think that the proposed solution addresses the problem?

   We would agree that the ability to opt out of the £500,000 limit should address this issue.

Partnerships

3. Do you think there is a need to address the discrepancy that arises under the debt cap for loans by a partnership?

   We are not aware of examples of this area causing problems for our members, but see how an issue could arise.

4. If so do you think that this is best addressed through legislation drafted specifically for the partnership issue?

We would be concerned that any changes to the rules should not add any significant complexity to the existing legislation and would in principle prefer the approach of making calculations by reference to loan relationship rules if this simplifies matters.

Functional currency

5. Do you think that there is a need to address this issue?

   We are not aware of examples of this area causing issues for our members.

6. If so do you think that the proposed solution addresses the problem?

   The proposal appears simple and to deal with the issue

Joining/leaving and group mergers/takeovers

7. Do you think that the current debt cap rules – for example on establishing the ultimate parent of a worldwide group and dealing with situation where there are non-existent accounts will be sufficient to enable the debt cap rules to apply to companies joining and leaving groups and mergers and takeovers?

   We have not come across examples of this area causing issues for our members.

8. Do you think that it would be worthwhile legislating for changes in group structure?

   We would not welcome changes that significantly increase the length of complexity of the existing rules, though in principle prefer certainty under legislative measures rather than relying on non statutory guidance notes which may become subject to changes. We would welcome sight of draft guidance notes to comment further.

9. If so what changes to group structure do you consider should be included in such legislation?

   See 8 above.

10. If not how do you think best practice on changes in group structure and examples should be included in the debt cap guidance?

    See 8 above.

Pension scheme contributions

11. Do you think there is a need to address this issue?

    We have not come across examples of this area from our members but agree in principle that it would be helpful to clarify the position.

12. Are there any arrangements using a similar structure that unforeseen repercussions under the debt cap that you think we need to consider?

    We are not aware of any similar arrangements/structures from our members.

Changes to the definition of Available Amount

13. Do you have any views on including in the available amount the loan relationship debits identified in section 313?

    We agree that the differing definitions for various tax purposes add unnecessary complexity to the rules.

14. Do you think this would simplify application of the debt cap rules?

We agree in principle that this should simplify the position.

15. Can you identify any consequential changes that may need to be made to the debt cap rules to accommodate such a change?

    We are not at this stage aware of any such changes.

16. Can you identify any interaction between the loan relationship rules and debt cap rules that may impact on this proposed change?

    We are not at this stage aware of any such issues.

Prospective Changes to IFRS 10 Consolidated Financial Statements, IFRS 11 Accounting for Joint Arrangements and IFRS 12 'Disclosure of Interests in Other Entities'

17. Can you identify any immediate issues arising from the proposed changes? If so could you provide us with specific examples?

    We have not come across such issues from our members.

18. Do you think there is a need to address any issues that arise from the proposed changes?

    We would need further information on the exact impact, potential issues arising and any proposals to address these to comment in detail.

19. If there is a need to make changes, can you identify and solutions to the issue?

    See 18 above.

Taxes Impact Assessment (TIA)

20. If you are responding to the consultation on behalf of a particular group of companies can you provide an estimate of how many companies in the group will be subject to the de-minimis for the most recent period of account to which the debt cap rules potentially apply?

    Not applicable.

21. If you are advisers or a representative body responding on behalf of a particular group or group of companies can you provide an estimate of how many companies in those groups will be subject to the de-minimis for the most recent period of account to which the debt cap rules potentially apply?

We are not sure how many of our members would be subject to the de-minis.

22. Can you provide an estimate of how much it would cost a group to make a de-minimis election?

    Detailed information is not available.

If you would like to discuss any of these comments in more detail, we would be happy to attend a meeting.

Yours sincerely.

Tim Ward
Chief Executive

APPENDIX A

The Quoted Companies Alliance Tax Committee

Vijay Thakrar (Chairman)	Deloitte LLP
Tim Crosley (Deputy Chairman)	Memery Crystal LLP
Paul Barnes	KPMG LLP
Chris Bond	PKF (UK) LLP
David Boyd	Mazars LLP
Nick Burt	Nabarro LLP
Jason Collins	McGrigors LLP
Paul Fay	Crowe Clark Whitehill
Stephen Goldstraw	Manches
Natasha Kaye	Olswang
Neil Pamplin	Grant Thornton UK LLP
Michael Ridsdale	Wedlake Bell LLP
Amanda Solomon	Charles Russell LLP
Kate Jalbert	Quoted Companies Alliance
Tim Ward	Quoted Companies Alliance

APPENDIX B

THE QUOTED COMPANIES ALLIANCE (QCA)

A not-for-profit organisation funded by its membership, the QCA represents the interests of small and mid-cap quoted companies, their advisors and investors. It was founded in 1992, originally known as CISCO.

The QCA is governed by an elected Executive Committee, and undertakes its work through a number of highly focussed, multi-disciplinary committees and working groups of members who concentrate on specific areas of concern, in particular:

- taxation
- legislation affecting small and mid-cap quoted companies
- corporate governance
- employee share schemes
- trading, settlement and custody of shares
- structure and regulation of stock markets for small and mid-cap quoted companies;
- political liaison – briefing and influencing Westminster and Whitehall, the City and Brussels
- accounting standards proposals from various standard-setters

The QCA is a founder member of European**Issuers**, which represents quoted companies in fourteen European countries.

QCA's Aims and Objectives

The QCA works for small and mid-cap quoted companies in the United Kingdom and Europe to promote and maintain vibrant, healthy and liquid capital markets. Its principal objectives are:

Lobbying the Government, Brussels and other regulators to reduce the costing and time consuming burden of regulation, which falls disproportionately on smaller quoted companies

Promoting the smaller quoted company sector and taking steps to increase investor interest and improve shareholder liquidity for companies in it.

Educating companies in the sector about best practice in areas such as corporate governance and investor relations.

Providing a forum for small and mid-cap quoted company directors to network and discuss solutions to topical issues with their peer group, sector professionals and influential City figures.

Small and mid-cap quoted companies' contribute considerably to the UK economy:

- There are approximately 2,000 small and mid-cap quoted companies
- They represent around 85% of all quoted companies in the UK
- They employ approximately 1 million people, representing around 4% of total private sector employment
- Every 5% growth in the small and mid-cap quoted company sector could reduce UK unemployment by a further 50,000
- They generate:
    - corporation tax payable of £560 million per annum
    - income tax paid of £3 billion per annum
    - social security paid (employers' NIC) of £3 billion per annum
    - employees' national insurance contribution paid of £2 billion per annum

The tax figures exclude business rates, VAT and other indirect taxes.

For more information contact:

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