The EU Referendum: Tax Q&A

July 2016

In brief

With the situation becoming unclear in many areas of business since the referendum decision last week for the UK to leave the EU, we have prepared a quick Q&A guide for tax related matters below.

In detail

Background

Q. How does exiting the EU actually work?

A. Article 50 of the Treaty on the Functioning of the European Union ("TFEU") needs to be triggered in order to start the 2 year exit procedure. When the UK will do this is unclear and the UK may not formally exit the EU for some time.

David Cameron has made it clear it is the job of the new Prime Minister to steer the UK through this stage. Therefore a formal exit may not be triggered until at the earliest October, when a new leader of the Tories and the Prime Minister is expected to have been chosen.

The UK may choose to try and negotiate its exit deal as much as possible before formally triggering the exit. This would obviously further delay the actual exit. It is unclear however, whether the remaining Member States will agree to this or whether, for example, the other Member States may refuse to negotiate a deal until the UK has activated the exit under the TFEU.

Q. How will EU Directives apply?

A. Directives implemented into domestic legislation will continue to apply unless and until they have been repealed (e.g. Merger Directive, Parent Subsidiary Directive, Interest and Royalties Directive). Such legislation may, however, require some amendments to ensure that they work as intended (see section below on UK law influenced by EU law).

The UK would not be required to adopt future directives if implementation deadlines are set for after the date the UK formally leaves the EU. The position regarding Anti Tax Avoidance Directive ("ATAD") will obviously depend on the timing of the exit. The UK is, however, already in the process of implementing the main BEPS actions and so the practical consequences of not being required to implement ATAD are limited.

Q. How will UK law, influenced by EU law change?

A. It is expected that the European Communities Act will be repealed, removing the direct application of the TFEU in the UK.

How other legislation is changed is as yet unclear. Some areas may be repealed and others will require wording changes. This will depend on how the legislation is currently worded and if it still works or makes sense as it is currently drafted. There are likely to be some areas where references to transactions or payments with "another Member State" no longer works and/ or the legislation cross-refers to other EU based Statutory Instruments.

UK courts will no longer be bound by the CJEU case law when applying the UK legislation.

There is an interesting question regarding ongoing claims based on EU law. It would appear that these claims remain in place post Brexit. There may however, be some risk (very difficult to quantify given political sensitivities) that subsequent legislation is introduced in an attempt to negate some of these claims (given the significant amounts involved).

What changes are actually made may to some extent be politically driven and may be a balancing act between the desire to raise revenue but remain competitive.

BEPS

Q. Will we still adopt BEPS?

A. The UK is still expected to continue to adopt BEPS measures, as the driving force behind these changes is the OECD, not the EU. A slowing down on the adoption of some actions may, however, be observed. This would depend on policy towards taxation going forwards. It is likely, however, that changes already announced, such as anti hybrid rules and restriction on interest deductibility will continue to be implemented.

No expected changes to the recommendations on PE rules or to Action Plan 6 (treaty abuse) as a result of an EU exit.

Key tax issues that should be considered all Japanese inbounds

Q. How will WHT apply?

A. UK Double Tax Treaties concluded by the UK and in force will continue to apply. As the UK will not be covered by the EU Parent Subsidiary Directive there are a number of treaty partners which could apply WHT on dividend payments in the future, including the following (this is not an exhaustive list):

Treaty Partner	WHT rate (%)
Germany	5/10/15
Italy	5/15
France	0/5/15
Spain	10
Portugal	10/15
Netherlands	0/5/15
Ireland	0/5/15
Belgium	10
Sweden	0/5/15
Poland	0/10

EU member states will still be bound by Free Movement of Capital with third countries (now the UK) therefore the ability to impose WHT may require, for example, a comparison with the taxation suffered by domestic companies on the receipt of dividends.

Exit Taxes

Exit tax legislation where changes were EU motivated could be subject to a change in part as an opportunity for UK to demonstrate 'taking back control' post Brexit as well as to raise revenue.

The Transfer of Assets Abroad legislation may also be a target for change for similar reasons.

Customs and VAT

At a high level, the biggest impact appears to be with Customs Duty.

The default position, for Customs, without negotiation would be that the UK is subject to tariffs in the same way as other non-EU countries are. There are however, several options as to where the UK could end up on Customs Duty including:

- "Swiss model" - series of bilateral agreements with agreed tariffs negotiated on an individual basis
- "Turkish option" - Turkey has a customs union with the EU with no tariffs on exports to the EU
- "Norway Solution" - the UK would continue to have access to the single market as a member of the EEA (but without a vote on the EU rules)
- Third country rules - a range of tariffs between 0 - 30% as agreed between WTO member countries

UK as still an attractive place to do business

Q. What does this mean for UK as a Hub?

A. The UK still has a very competitive corporation tax environment (even if the UK's corporation does not drop further to 17%) and a (soon to be) "BEPS compliant" tax system.

The UK is still an attractive location for moving key business people, although clearly any impact to the fundamental freedoms of movement for people may make it harder in the future to bring people to the UK. Any immediate change to the existing freedom of movement rules is, however, not expected.

The above may need to be set against the potential for increased costs in the UK, for example, if there is an increase in income tax rates.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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