L-day analysis

The impact on MNCs

Speed read

The draft Finance Bill contains a number of provisions which will be of interest to multinational companies (MNCs), with particular highlights being the implementation of certain changes prompted by EU Directives. A significant portion of the draft legislation will also implement the previously announced changes to the taxation of real estate income and gains of non-resident companies.

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Timing and space (as well as not wanting to duplicate the excellent articles elsewhere in this edition) mean that this cannot be a comprehensive analysis of all the relevant draft provisions impacting MNCs, and further analysis over the coming weeks and months will be needed on the details of the legislation. So think of this article as your starter, with several courses yet to come.

EU law changes

There has been increasing momentum in the field of tax dispute resolution at both an international and EU level, as a result of the ongoing implementation process of the OECD's multilateral instrument and, as readers will be aware, the European Council adopting Council Directive 2017/1852/EU on 10 October 2017. This Directive relates to tax dispute resolution mechanisms in the EU and member states are required to bring into force the provisions necessary to comply with the Directive by 30 June 2019. Clause 39 of the draft Finance Bill introduces such statutory powers by means of:

- a new section which allows the Treasury to make regulations to give effect to the Directive, any instrument which modifies or supplements it, and any other agreements or arrangements connected to double taxation disputes;
- a further section for regulations which require HMRC commissioners to give effect to an agreement, decision or opinion; and
- a section permitting disclosure of information under international agreements.

The aim of the Directive is to complement rather than supplant existing dispute resolution mechanisms. However, there are aspects of the Directive intended to improve the functioning of these mechanisms, from a scope and process perspective. It should also help certain related aspects of dispute resolution to become more streamlined over time, such as the time commitment to a mutual agreement procedure before alternative options are available. This will evolve over time, but nonetheless represents a positive step for taxpayers who want more efficient and transparent ways to resolve cross border tax disputes.

Despite my best efforts, I struggle to be positive about the changes proposed at clause 40 on disclosable arrangements. Obviously, this provision is simply intended to implement Directive 2018/882/EU (which amends Directive 2011/16/EU), commonly known as DAC 6. It allows the Treasury to make regulations to facilitate the mandatory exchange of information in relation to reportable cross-border arrangements. Cross-border arrangements are those which affect two member states, or a member state and a third country, in each case if they meet at least one of the hallmarks. Should the government choose to do so, DAC 6 would also permit the implementation of the OECD's model mandatory disclosure rules.

There are several concerns with the provisions in DAC 6. Whilst the first notifications of reportable transactions are not due until August 2020, they may need to cover the period from 25 June 2018 onwards. This will depend on the domestic implementation process in each member state. Whilst there will be some limited discretion on the scope of the requirements and potential exclusions, we are still concerned about potential retroactive effect, particularly given that there is no specific de minimis carve out from the provisions.

I had hoped that the right for an intermediary to waive the reporting obligation, if this would breach legal professional privilege, would be applied more consistently and not left to implementation under the relevant domestic law. The equivalent concept of privilege is narrowly defined in certain EU jurisdictions and therefore may lead to inconsistent rules being applied to the same arrangements in different jurisdictions.

In addition, the hallmarks and the definition of intermediary are both very broad. In the case of the hallmarks, some apply if the main benefit is the avoidance of tax, but others apply to certain circumstances with no main benefit test to act as a filter. (In the US in the late 1990s, an incredibly broad and onerous regime led to huge amounts of disclosure. The IRS eventually chose to amend the obligations on the taxpayer to save its own sanity!)

HMRC has also confirmed that no decisions have yet been made as to how these provisions will interact with the existing UK disclosure regimes.

Clause 37 and Sch 16 will adapt the existing rules on corporation tax exit charges to implement the provisions of Directive 2016/1164/EU (known as the Anti Tax Avoidance Directive (ATAD)). The exit charge changes will have effect from 1 January 2020, and are primarily administrative, with two new sections also being introduced to enable the rebasing of certain assets so no double taxation occurs on their value at the point of exit. The government has also announced that Finance Bill 2019 will contain two ATAD related controlled foreign company (CFC) changes, which will broaden the control definition in the existing domestic rules and amend the finance exemption in TIOPA 2010 Part 9A chapter 9, but has not confirmed when the draft legislation will be available.

The turn of real estate

The government announced last year that it was seeking to tax gains which arise from April 2019 when both commercial or residential property is sold (directly or indirectly) by a non-UK resident person or entity; and also to charge the profits of a UK property business and other UK property income of non-resident companies to corporation (rather than income) tax from April 2020.

Clause 6 and Sch 1 of the Finance Bill contain the draft provisions, which seek to bring gains made by non-UK residents (other than companies) on interests in UK

land within the charge to capital gains tax. Non-resident companies will be charged to corporation tax on chargeable gains, and the draft provisions also abolish the charge to tax on ATED related gains.

The proposal sought to capture indirect disposals by requiring tax to be paid on the increase in the value of an entity being sold which is 'property rich' (broadly, where 75% or more of the asset being disposed of derives its value from UK land, and where the non-UK resident holds, alone or with connected persons, 25% or more of that entity). These are also defined in Sch 1, and include a trading exemption to the 75% test if the person making the disposal can reasonably conclude that the land in an entity being disposed of is used in the course of a trade (or if not, that the land in question is of insignificant value) and that trade has been ongoing for at least 12 months prior to the disposal and is expected to continue. It will also be possible in certain circumstances to opt to either rebase property values to April 2019 or use the original acquisition cost, for both direct and indirect disposals.

Schedule 2 contains a number of administrative provisions on notifications, amendments to returns and enquiries, and also gives effect to the proposals in the separate technical consultation on payment windows for residential property.

Clause 7 and Sch 3 extend the territorial scope of charge to corporation tax for a non-resident company carrying on a UK property business. This includes loans relationships and derivative contracts that the company is a party to for the purpose of its property business or generating income. There are various consequential amendments to CTA 2009 to deal with scoping provisions, deductible item and exclusion rules, deemed realisation provisions and intangible degrouping elections.

Given that certain policy decisions in respect of the non-resident gains proposals have yet to be finalised by HMRC, it is perhaps to be expected that not all of the relevant legislation would be available. However, I still do not understand the need to stagger the introduction of the two measures between 2019 and 2020 (as opposed to introducing both in 2020). If it is necessary, why not introduce the extension of the scope of corporation tax to non-resident companies first (and not just for real estate companies if that is the ultimate policy goal)? That is surely the simpler way to amend the rules, and would also offer an opportunity to amend all parts of the tax code impacting real estate (including SDLT) in a more considered and holistic way.

The consultation document in November 2017 provided that the UK would seek to renegotiate any tax treaties with jurisdictions which could be exploited to keep profits and gains outside of such provisions. An anti-forestalling rule will apply to arrangements entered into on or after 22 November 2017 (and a further rule in the context of indirect disposals with effect from 6 July 2018).

Details are still awaited on how the new rules will impact investment through collective investment vehicles, and consultation with various stakeholders is ongoing. In principle, vehicles which fulfil certain conditions and adhere to reporting requirements will be able to elect for transparent or exempt (depending on their status) treatment under the rules, with taxation occurring at the investor level.

The substantial shareholding exemption was also expanded recently and may, in certain cases, apply to corporate disposals by qualifying institutional investors. There is an open policy question as to whether this should be expanded to include the disposals of interests in entities such as property unit trusts. There is a further open question as to whether repurchases or redemptions of shares (or other returns of value) should be excluded from the definition of disposal under this legislation where they are proportionate to all investors in a collective investment vehicle.

Other measure to note

As usual, a number of measures supplement or amend existing legislation. The main ones applicable to MNCs are summarised below:

- Clause 8 and Sch 4 make a number of changes to the loss reform rules in CTA 2010 Part 7ZA to restrict relief for certain carried forward losses. These include changes to the calculation of restricted losses for all companies, and amendments to terminal relief under CTA 2010 s 45F. There are also specific amendments to how deductions are calculated for insurers within the basic life assurance and general annuity business (BLAGAB) rules.
- There are certain technical amendments to the corporate interest restriction rules. These include provisions on the calculation of adjusted net group interest expense, group EBITDA, amendments to the public infrastructure rules and the rules impacting REITs. There are also further amendments to the hybrid rules in TIOPA 2010 Part 6A, in relation to permanent establishments and regulatory capital.
- There are a number of detailed technical changes to the petroleum revenue tax provisions on relief for decommissioning expenditure and a new Schedule with a proposed mechanism to enable an oil company to transfer a portion of its historic profits, and associated tax paid on such profits, to another company on the sale of an oil licence.
- Following consultations ending in February 2018, there are a number of technical changes to the leasing rules for income and corporation tax, as a result of the adoption of IFRS 16.
- There are new rules on allowing non-corporate entities into VAT groups, and legislation to transpose Directive 2016/1065/EU governing the VAT treatment of vouchers into UK law.
- Stamp duty and SDLT exemptions are introduced for certain transfers, following the exercise of resolution powers under the Banking Act 2009 for managing failing financial institutions.

Final points

I have not covered the new profit fragmentation rules in any detail here, as they are covered elsewhere in this edition and I had assumed that MNC arrangements would not be within their scope. My initial observation is that the draft legislation seems extremely broad in its possible application, and has some similarities to the diverted profits tax (DPT) (the obvious differences being that it extends to individuals and has no carve-out for SMEs). The difficulties currently faced with interpreting and applying the DPT rules could be even more pronounced with this set of draft rules, and it does beg the question as to what exactly HMRC is targeting. It would also be helpful to incorporate a sensible motive test into the provisions. So I would suggest keeping an eye on these proposals until things (hopefully) become clearer.

So there are lots of things for MNCs to get excited about, monitor or otherwise resign themselves to. As we move into the next phase of uncertainty caused by the Brexit pantomime, perhaps it is meant to be reassuring that the constant tinkering with the UK tax code continues. ■