SLAUGHTER AND MAY/

Slaughter and May Podcast
Tax News Highlights: June 2021

Zoe Andrews	Welcome to the June 2021 edition of our tax news highlights podcast. I am Zoe Andrews, PSL Counsel & Head of Tax Knowledge.
Tanja Velling	And I am Tanja Velling, Senior Professional Support Lawyer in the Tax department. In this podcast, we will cover a number of UK cases and some international developments. We will look at the Supreme Court decisions in *Hurstwood Properties* and *Tooth*, the Court of Appeal decisions in *Dodika* and *Heathrow Airport*, and the High Court decision in *TP Icap Ltd*. In terms of international developments, we will cover the latest on the G7 agreement in respect of the OECD's international tax reform project and the European Commission's plan to make EU business taxation fit for the 21st century. This podcast was recorded on the 15th of June 2021 and reflects the law and guidance on that date.
Zoe Andrews	For many years now the *Ramsay* principle has been understood as one of statutory construction. That means looking at the purpose of the legislation and asking whether the statutory provisions construed in the light of their purpose, were intended to apply to the transaction, viewed realistically. In *Hurstwood Properties v Rossendale Borough Council*, the Council sought, and succeeded, to apply the *Ramsay* principle to defeat a business rates avoidance scheme. The Supreme Court confirmed that the *Ramsay* principle of statutory construction is not particular to tax and should be applied when construing all legislation. The Supreme Court also clarified that the conclusions reached in the cases of *MacNiven* and *Barclays Mercantile* were examples of the Ramsay approach being followed and not a determination that the Ramsay approach did not apply in the first place. This was contrary to what Lord Justice Henderson had said in the Court of Appeal to support his argument that the legislation in this case was not amenable to a wider, purposive interpretation that would allow scope for the *Ramsay* approach to operate. Tanja, can you explain the facts of this case?
Tanja Velling	The relevant legislation imposed a charge to business rates on the owner of unoccupied business premises, subject to certain exceptions. The "owner" for these purposes was "the person entitled to possession of the properties". Hurstwood Properties and the other property owners in similar cases which stood behind this test case, had leased property to an SPV

	and argued that, under the lease, the SPV was the “owner” of the property within the meaning of the legislation. This interpretation, if correct, got the landlords off the hook for business rates, and although the SPVs were liable to pay the business rates, they did not, in practice, pay as they were put into members’ voluntary liquidation or dissolved. So the Councils stood to lose out on a lot of revenue if the schemes worked.
Zoe Andrews	The Supreme Court held that the leases should be closely examined in their context and in light of the purpose of the legislation which was to incentivise owners of unoccupied premises to bring them back into use. The legislation focused the burden of the business rates on the person who has the ability, in the real world, to bring the properties back in to use. The Supreme Court concluded that the leases did not, in fact, transfer to the SPVs the entitlement to possession required by the legislation.
Tanja Velling	This case is an important win for Rossendale Borough Council and all local authorities challenging similar business rates avoidance schemes. However, this case went all the way to the Supreme Court in the context of a claim by Hurstwood Properties to strike out the Council’s claim rather than in the context of the substantive trial. So the local authorities will have some time to wait before they can recover the unpaid business rates.
Zoe Andrews	Let’s move on to another Supreme Court decision. The decision in *HMRC v Tooth* came out on the same day as Hurstwood Properties and sparked a number of somewhat predictable, yet amusing headlines around losing teeth, getting to the root and biting the dust. Mr Tooth had engaged in a tax avoidance scheme to generate an employment related loss which HMRC wanted to challenge. But they were out of time to do so except under the extended time limit for deliberate errors. Aside from the puns, how do you feel about this case Tanja?
Tanja Velling	I would repeat the words which our colleague Sarah Osprey used in her post on the European Tax Blog – I have “intractable feelings of crossness” about this case for reasons I will explain. There were two issues before the Supreme Court, the obvious one on the basis of which Mr Tooth won his battle and which makes me rather cross, and the less obvious one on which, one might say, HMRC won the war.

	Looking at the first issue, the paper return for the relevant years had a neat little box for employment-related losses such as those Mr Tooth claimed he suffered. But this box was missing from the electronic version filed on Mr Tooth's behalf using HMRC-approved software. So, Mr Tooth's advisers included the employment-related loss in the partnership loss box. The end result for tax owing (or not owing) was the same as if the loss had been included in the correct box and the advisers explained the misplaced loss in the "white space" for additional comments. HMRC then said – and in my head, this looks like a comic-style switching on of a light bulb, finger shooting up into the air moment – aha! You deliberately put the loss into the wrong box. So, we have a deliberate error, the longer limitation period applies and we are not out of time and can raise an assessment. Thankfully, the Supreme Court finally gave that argument the resounding rejection it deserved, confirming that the test is not whether a "deliberate statement" in a return turns out to be inaccurate, but whether that statement was "deliberately inaccurate".
Zoe Andrews	The second issue concerns the concept of staleness which has for some time now been exercising the lower court. The issuing of a discovery assessment necessitates a "discovery". This means that something new must have come to light and the assessment must be issued on the back of that something new and in temporal proximity to its coming to light. If HMRC waits too long, the discovery becomes stale and no assessment can be made. The Supreme Court has now drawn a red line through the staleness concept, stating that there is no such thing. A "discovery" remains a discovery no matter how long ago the discovery was made. Moreover, no new facts need to have come to light for there to be a "discovery"; all that is needed is for the insufficiency of tax to newly appear to an HMRC officer. This is a broadly subjective test and gives HMRC significant leeway. So the concept of staleness now looks to be confined to the realms of public law and the as yet untested possibility of a judicial review claim that a discovery assessment was, by virtue of the staleness, irrational!
Tanja Velling	Moving on to the Court of Appeal in *Dodika*. The issue in this case was whether the contractual notice provisions had been complied with in the context of a tax covenant claim following the purchase of a company. The sellers had applied for summary judgment to release funds held in escrow. But the buyer had given notice of a tax covenant claim in respect of a transfer pricing issue under investigation by the Slovene tax authorities. The share purchase agreement did not specify precisely what

	information would have to be included in a notice of claim, but merely required "reasonable detail" of the "matter which gave rise to the claim".
Zoe Andrews	The High Court had sided with the sellers (as is often the case in tax covenant claims) and concluded that the notice provisions had not been complied with because although the notice gave reasonable detail of the nature of the claim, it failed to give reasonable detail of the **matter** which gave rise to the claim. The Court of Appeal agreed with the High Court that the "matter" giving rise to the claim is the underlying facts and not the mere existence of an investigation, but concluded the notice was valid as it did contain sufficient detail. On the facts of the case, the sellers knew all about the details of the course of the investigation anyway. They also knew that the Slovene tax authority had refused to elaborate on its suspicions that the transfer pricing was inappropriately low, so there was no more detail that the buyer could have usefully provided.
Tanja Velling	As Lord Justice Popplewell said "*What is reasonable takes its colour from the commercial purpose of the clause, and what businessmen in the position of the parties would treat as reasonable. Businessmen would not expect or require further detail which served no further purpose. That would be the antithesis of what was reasonable*." So although the buyer in this case had a narrow escape, it is a warning to those drafting notice provisions to specify exactly what information is required rather than ending up in court arguing about whether something is "reasonable"!
Zoe Andrews	The *TP Icap Ltd* case also concerns tax warranty and tax covenant claims. The target companies, through their provision of interdealer broking services to third parties under investigation, became involved in the German authorities' investigation of the cum-ex scandal. So the purchaser purported to notify claims in respect of adverse consequence that could arise once the investigation had concluded. "Purported" is a key word here. The High Court threw out some of the claims on the basis that, instead of actually making a claim, the purchaser had merely notified that it may, in the future, make a claim. That was insufficient under the contractual notice provisions.

Tanja Velling	Similarly, claims in respect of the tax covenant were judged to be too vague and premature. Given that the investigation was still ongoing, the High Court decided that there was not yet any tax liability in respect of which the covenant could bite and that included the provision in the tax covenant which would cover the purchaser for costs incurred in avoiding, resisting or settling a tax liability which would otherwise fall to be compensated under the tax covenant. Another interesting point from the decision is the fact that the High Court accepted that, given their drafting, certain tax warranties looked not only at the tax affairs of the target companies, but also at those of third parties. Given the business of the target companies (and, perhaps, with the benefit of hindsight in seeing the type of investigation at issue here), the Court thought it commercially unsurprising that such a warranty would be given.
Zoe Andrews	The Court of Appeal in *Heathrow Airport Ltd and others* rejected a challenge to the government's decision to withdraw two VAT reliefs from IP completion day. Although this particular case was about tax free shopping in airports and arguably is a bit niche, it is interesting for the approach of HMRC to Extra Statutory Concessions, or ESCs, more generally. ESC 9.1 effectively said that, if you were an approved tax free or duty free shop selling goods to a passenger headed out of the EU, you were regarded as the exporter of the goods and could zero rate the supply. This is why you were always asked to scan your boarding pass, to make sure the correct VAT treatment was applied. Post-Brexit, the UK considered it was required to apply a level playing field across the EU and non-EU and so faced a policy choice between applying VAT across the board or zero-rating across the board. Having initially indicated it was minded to do the latter, it plumped for the former which is why airports, duty free operators etc. were up in arms. But the claim for judicial review failed.

Tanja Velling	One of the better arguments for the application for judicial review was that it looked like the government might have got the law wrong. The government's view was that in light of *Wilkinson*, the concession had been unlawful. Until Brexit, however, the risk of challenge was minimal and so this concession had not been a priority for review. The Court of Appeal agreed that HMRC couldn't remake or extend ESC 9.1 because of the *Wilkinson* case. It all seems a bit odd though, given that there have been several updates to the ESC since the *Wilkinson* case was decided in 2005. The last one of those was in 2017, and all of the changes were made without a hint of suspicion that there was an issue. Plus, post-*Wilkinson*, HMRC embarked on a review of ESCs putting those that were thought ultra vires on a statutory footing. So this case is worth bearing in mind if you are looking to rely on an ESC!
Zoe Andrews	There has been much press coverage of the G7's "deal" on international tax reform which the UK Treasury's press release describes as "seismic" and "historic". But although the communiqué from the G7 is important and provides momentum, there is still a lot of work to be done to get the G20 on board and then the rest of the 139 countries which form the OECD's Inclusive Framework. And even what has been agreed amongst the G7 is lacking in detail (for example there are no sector based carve-outs) and areas of contention are already showing with the UK pushing for a carve-out from the new taxing right for financial institutions and France being supportive of this. The UK will argue for this carve-out at the G20 summit in July, but the US is expected to oppose this.
Tanja Velling	So what has been agreed in principle by the G7?
Zoe Andrews	On Pillar 1, the new taxing right, market countries would be awarded taxing rights on at least 20% of profit exceeding a 10% margin, for the largest and most profitable multinational enterprises. This means the rules would apply only to global firms with at least a 10% profit margin. All digital services taxes and other relevant similar measures on all companies will be removed – given that it is expected that more than 50% of companies subject to digital services taxes would not fall within the scope of pillar 1 it may prove difficult for the G7 to persuade some jurisdictions to remove their digital services taxes for companies which are not caught by pillar 1, especially for jurisdictions like India where the tax has been applied for a number of years already. On pillar 2, the global minimum tax, a rate of at least 15% has been agreed and will be applied on a country-by-country basis. France has already

	made it clear that 15% is a starting point and France will fight for a higher rate. It has been agreed that both measures will progress in parallel as a package – something the UK has been insistent on. This is an important development as the US expects pillar 1 to be revenue neutral for them and is most interested in pillar 2 and, for a time, there were suggestions that pillar 2 might be implemented first.
Tanja Velling	Will the new taxing right apply to all companies commonly thought of as large digital players?
Zoe Andrews	The UK has said all along that the problem to be solved was that of taxing digitalised businesses fairly and the UK does not want to see the scope of the new taxing right narrowed so much that this issue is not resolved. So it was interesting that the media initially reported that Amazon would not be caught as its overall operating profit margin in 2020 was only 6.3%. This was then followed up with the news that, for the purposes of assessing profitability for the new taxing right, different divisions of Amazon's business will be treated separately and so the cloud computing unit, Amazon Web Services (which as a division on its own has profitability of 30%), will be caught. The details are yet to be worked out, but the final agreement will need to set out how the rules would apply to companies with different activities and business lines.
Tanja Velling	Does the G7 agreement align with what the Biden administration have asked for?
Zoe Andrews	Broadly yes. The communiqué has not said the Pillar 1 new taxing right should be limited to no more than 100 multinationals (which was the US treasury's suggestion) – but the scope has not yet been agreed so it might still work out this way. And the minimum effective tax rate of at least 15% is consistent with the US Treasury's plans, but will be a hard sell for some jurisdictions, such as Ireland, as the OECD discussion was previously at the 12.5% range. China, too, has expressed concerns about a minimum tax rate and wants a carve-out for tax incentives to attract high tech industries and research. The UK would also benefit from such a carve-out as the patent box rate is 10%. There is understandably nothing in the communiqué about a substance carve-out from the minimum rate of tax which is a key requirement for many jurisdictions and was included in the OECD blueprint. The Biden administration does not want a substance carve-out and this mirrors the change it proposes to GILTI to remove a substance carve-out. The tax rate which will eventually be agreed is dependent on what agreement is reached globally on a substance carve-out because, if a decent substance carve-out can be agreed, jurisdictions will be more relaxed about the rate.

	And a carve-out for substance targets the measure at base erosion and profit shifting, rather than tax competition. And it was, in the beginning, supposed to be addressing remaining BEPS issues that the BEPS project itself had not dealt with.
Tanja Velling	It does sound as if a lot of work is left to be done. So, we will no doubt be returning to this topic in a future edition of this podcast. But, for now, let's move on to another topic. In mid-May the European Commission published a tax plan BEFIT-ting the 21st century.
Zoe Andrews	I know that you are trying a pun here, but this one really only works in writing where you can see that "BEFIT" is in capital letters to mark the new acronym for the Commission's optimistic second attempt at harmonising corporate taxation in the EU. BEFIT replaces the ill-fated proposal for a common consolidated corporate tax base. It will piggy-back off the OECD's international tax reform proposals. Common rules for calculating the tax base would borrow from Pillar 2 and a formulary apportionment would build on the profit reallocation under Pillar 1. Whether the OECD's project is able to put sufficient wind into the sails of BEFIT to help it sail through the Council is anyone's guess.
Tanja Velling	But it is not the only initiative into which the Commission hopes the OECD's project will breathe new life. They hope that the Interest and Royalties Directive will finally be recast to make the elimination of withholding tax conditional on payments' being subject to tax in the destination state. This particular proposal has been languishing before the Council since 2011.
Zoe Andrews	Speaking of long-living (or long-dying) initiatives, it seems that the Commission has still not given up on the Financial Transaction Tax. Also, it is planning to publish a proposal for a digital levy on the 14th of July. The stated intention is that this will be compatible with World Trade Organisation rules and sit alongside the OECD's project. Quite how the Commission is going to pull this off – in particular in light of the recent G7 agreement to "provide for appropriate coordination between the application of the new international tax rules and the removal of all Digital Services Taxes, and other relevant similar measures, on all companies" – remains to be seen.
Tanja Velling	Another interesting point is the Commission's suggested introduction of DEBRA – a debt equity bias reduction allowance which is intended to, using the words of Executive Vice-President Dombrovskis, "promote investment and innovation by addressing the debt-equity bias in corporate taxation".

	For UK parent companies of EU subsidiaries, the details of the DEBRA proposal will be of crucial importance to determine whether it could switch off the UK's exemption from corporation tax for distributions received because the distribution would be deductible for the payor.
Zoe Andrews	One final development to mention in respect of EU tax is that, as per a press release from the Council issued on the 1st of June, political agreement has been reached between the Council and the EU Parliament on the proposed directive requiring public country-by-country reporting. And now, what is there we can look forward to over the next month?
Tanja Velling	• Hearings in two employment tax cases are scheduled to take place later in June and early July. The Upper Tribunal will be hearing appeals in the *Peter Wilson* case on the employment status of an LLP member and in *RALC Consulting* on the application of IR35. • The 30th of June marks the beginning of the end for the temporary increase of the SDLT nil rate band for residential property. The nil rate band will drop from £500,000 to £250,000 on the 30th of June and, from the 30th of September, it will revert to the pre-pandemic level of £125,000. • Then we have the call for evidence on the effectiveness of the Office of Tax Simplification which closes on the 6th of July. The outcome is expected to be published in the autumn. • The 14th of July is going to be a big day for tax in the EU. Amongst other things, the European Commission is due to publish its proposal for a digital levy to which we already referred.
Zoe Andrews	That leaves me to thank you for listening. If you have any questions, please contact Tanja or me, or your usual Slaughter and May contact. Further insights from the Slaughter and May Tax department can be found on the European Tax Blog – www.europeantax.blog. And you can also follow us on Twitter - @SlaughterMayTax.