Slaughter and May Podcast
Tax News: February 2024

Zoe Andrews	Welcome to the February 2024 edition of Slaughter and May's "Tax News" podcast. I am Zoe Andrews, PSL Counsel & Head of Tax Knowledge.
Tanja Velling	And I am Tanja Velling, Tax PSL Counsel. We will discuss the First-tier Tribunal's decision in *Bolt Services* and the Court of Appeal's decision in *Dolphin Drilling*, and another fun case, but I won't tell you the name quite yet! We're also going to discuss some transfer-pricing related points, the OECD's ICAP statistics and Pillar 2 impact assessment and some exciting things to look out for. The podcast was recorded on the 6th of February 2024 and reflects the law and guidance on that date. Shall we start with the cases?
Zoe Andrews	Sure, what's this mystery case of yours then?
Tanja Velling	Well, let's do the following. I'll read you the quote that the Financial Times picked out when it reported on the case, and you tell me what you think the case is about. So: "Nominative determinism is not a characteristic of snack foods: calling a snack food "Hula Hoops" does not mean that one could twirl that product around one's midriff, nor is "Monster Munch" generally reserved as a food for monsters." So, what do you think?
Zoe Andrews	Well, there's really only one area of tax that tends to generate such priceless quotes. It must be a case about VAT classification! How about *Walkers Snack Foods v HMRC*?
Tanja Velling	Indeed! It concerned the question whether Walkers' Sensations Poppadoms are standard-rated or zero-rated for VAT purposes. Of course, HMRC contended for the former, Walkers argued for the latter. The First-tier Tribunal then had to decide whether Sensations Poppadoms were potato-based products similar to crisps and packaged for human consumption without further preparation. If so, they would be standard-rated.
Zoe Andrews	I do recall that you were quite excited about that case, so let's get our teeth stuck into it! During the hearing, Walkers dropped the argument around the need for "further preparation" (which had been based on the product being "designed to be used with dips, chutneys and pickles, and as a side with a meal"). So, the first real question was whether the products were sufficiently potato-based. Walkers argued that the FTT should take into account only the ingredients listed in the legislation – namely potato, potato flour and potato starch – which would have given a potato content of around 17%. The FTT, however, agreed with HMRC that the legislation should not be construed restrictively in this respect: other potato-based materials – potato granules and modified potato starch, in this case – could also be taken into account. As a result, the FTT found that, with a potato content of around

	40%, Sensations Poppadoms were sufficiently potato-based. Further arguments around gram flour being the key ingredient were dismissed.
Tanja Velling	And then comes what I suspect would have been the best part of the case – deciding whether Sensations Poppadoms were similar to potato crisps. The FTT tasted the products and comparators provided. Applying a multifactorial test, it ultimately concluded that there were sufficient similarities. Instead of going into this in detail, I'll highlight some points in relation to one factor that's relevant to the analysis: marketing – and this is what the quote picked by the Financial Times related to. The products were marketed under the name "poppadoms", but that didn't mean much – especially because the overarching brand – "Sensations" – was more prominent. The FTT also considered that the marketing materials "showed the products being eaten in settings which we consider are not dissimilar to those in which one would expect to find potato crisps: for example, being eaten by an individual from a bowl in front of a computer" – although, in my view, such marketing should really come with a warning about crumbs in the keyboard… But anyway, do we have time for one more fun fact related to the case?
Zoe Andrews	Go on then!
Tanja Velling	When the case made the rounds in the tax department, one of the associates actually went out and bought a packet of the Sensations Poppadoms, so we could sample the product! I did sample it, and I'd say that the FTT's description of the texture was quite accurate: "crunchy at the first bite; they then become somewhat softer thereafter although they did not dissolve completely in the mouth".
Zoe Andrews	Such a shame I was working from home on that day! Although I'm still trying to figure out whether that description makes me want to try them more or less. Anyway, I think we have probably spent enough time on this perhaps more frivolous discussion. There's another VAT case that is worth a brief mention. Back in December 2023, the FTT considered the VAT treatment of taxi rides booked through the ride-hailing app Bolt. The FTT decided that the Tour Operators Margin Scheme applied. This means essentially that VAT is charged on Bolt's profit margin, and not on the full price of the taxi ride. What's quite interesting about this is that, around the middle of 2023, it was reported that Uber's use of the Tour Operators Margin Scheme was also being challenged by HMRC. So, this decision in respect of Bolt would likely bolster Uber's position – although there may be an interesting difference in the fact patterns. The Tour Operators Margin Scheme generally applies to services bought-in from another person. In *Bolt Services*, part of the factual matrix as set out by the FTT was that the drivers are independent contractors. But back in 2021, the Supreme Court decided that Uber's drivers are workers and not independent contractors (as a matter of fact, a similar case is reportedly being brought against Bolt as well). It's difficult to

	predict the FTT's decision, if it was asked to consider the application of the Tour Operators Margin Scheme to Uber and what weight the drivers' worker status might have. But these cases certainly indicate how new models of doing business throw up tricky questions when applying existing laws.
Tanja Velling	You may also be wondering why we have included a case concerning the hire cap under the oil contractors' regime. A little bit niche for this podcast? Although arguably no less niche than the classification of Sensations Poppadoms for VAT purposes…. But anyway, the Court of Appeal's decision in *Dolphin Drilling* caught our eye because it contains discussion of the meaning of the word "incidental", and that may be relevant in other tax contexts, such as main purpose tests where it is argued that something is not a main purpose, or one of the main purposes, of a transaction because it is merely incidental to the transaction. From April 2014 the hire cap limits a contractor's ability to bring into account payments it makes under a lease of an asset from an associated person. Dolphin leased a vessel, the Borgsten, from an associated company and provided it to Total, the operator of the Dunbar oil platform. On the facts of the case, the hire cap would apply to limit Dolphin's deductions for the lease payments unless it was "reasonable to suppose" that the use of the vessel as accommodation for those who worked on the Dunbar oil platform "is unlikely to be more than incidental to another use, or other uses, to which [the Borgsten] is likely to be put". So what did the Court of Appeal say about the construction of this statutory language?
Zoe Andrews	There was no definition of "incidental" in the relevant legislation and so the word takes on its ordinary meaning. But how do you ascertain the ordinary meaning of a word? The meaning of an ordinary word is, according to the Court of Appeal, not to be found so much in a dictionary but rather in looking at how it is in fact ordinarily used in everyday contexts. The FTT had substituted other words for incidental by saying something is incidental to another matter if it is subordinate, or secondary, to it. The Upper Tribunal then failed to allow HMRC's appeal. The Court of Appeal held this approach was wrong as most ordinary words have nuances and shades of usage that cannot be precisely captured by substituting other words. Although it may be true that if one use, A, is incidental to another use, B, then use A will be of lesser or secondary importance to use B, it does not mean that being subordinate or secondary is what incidental means.
Tanja Velling	The example Counsel for HMRC gave which resonated with the Court of Appeal was of a laptop used by a barrister primarily to write opinions (use B) but also being used to write a shopping list (use A). In this example, the use of the laptop to a write a shopping list is not incidental to the use of it to write opinions as the two uses are not connected (except that they happen to make use of the same laptop) but it can be said that the use to write a shopping list is of minor or secondary importance to the use of the laptop for writing opinions. Taking into account this example and others, the Court

	of Appeal concluded that in order for use A to be incidental to use B there must be some link between them which is not the case if use A is an unconnected and independent purpose in itself. Use A is incidental to use B if it "arises out of use B, or as a by-product of use B".
Zoe Andrews	In order to decide whether the use of the Borgsten to accommodate offshore workers was incidental to its other uses the relevant question was whether its use as such accommodation was an independent end in itself (of some significance), unconnected with its other uses, or whether it was something that arose out of its other uses. On the facts of the case, the use of the vessel to accommodate offshore workers could not be said to arise out of the other uses and so was not incidental to those other uses. The taxpayer has announced its intention to appeal this decision to the Supreme Court. In the meantime, there are various cases on "main purpose" tests going through the courts this year so it will be interesting to see if the Dolphin case is used to argue that one purpose (obtaining a tax advantage, for example, in the loan relationship unallowable purpose test) is a by-product of another purpose (the commercial driver for the transaction) and so should not be treated as a main purpose.
Tanja Velling	Now that's it in terms of our discussion of recent cases. Our next topic is transfer pricing, and this has three elements – although we can probably deal with two of these quite quickly. HMRC added a new page to the International Manual – the reference is 485025 – discussing the 6-step process in Chapter I of the OECD's Transfer Pricing Guidelines to analyse which risks are assumed by each party to a transaction which will then feed into the determination of how that transaction should be priced. The guidance here is rather detailed – with 131 paragraphs, it must be one of the longest pages in the Manuals, but it usefully fleshes out HMRC's view of the OECD's Guidelines (although it should not be treated as a definitive answer). It confirms, for instance, that HMRC disagrees with the view expressed by some commentators that, where a party contributes to the control of a risk, but doesn't assume it, the remuneration should never include a share of the up- or downside of that risk. And I suppose we could leave it at that for the first transfer pricing item.
Zoe Andrews	The second item is the summary of responses to HMRC's consultation on reforming transfer pricing, permanent establishment and diverted profits tax legislation. Our colleague, Tom Gilliver, commented on this on the European Tax Blog under the headline "The DPT is dead; long live the DPT!" as the most eye-catching point of the summary of responses is that the government wants to go ahead with bringing diverted profits tax into corporation tax framework. So, it would no longer be a separate tax, but HMRC could issue a "diverted profits assessment" which would attract tax at the higher DPT rate. According to the summary of responses, "The government expects that MAP will be available where a diverted profits

	assessment results in double taxation." Details of the interaction will be set out in a technical consultation.
Tanja Velling	The availability of MAP would certainly be a welcome development, although I'm still somewhat sceptical as to whether other jurisdictions would agree. Also, overall, I think incorporating DPT into the corporation tax framework is only a second-best outcome. Respondents had suggested that, with the implementation of Pillar 2, it could perhaps be time to consider abolishing DPT altogether. Unsurprisingly, HMRC disagrees, considering that "DPT remains a useful tool". On a slightly more hopeful note, the summary of responses also states that "It will be appropriate, once the Pillar 2 rules are in place, to review its impact on CT. This review may identify opportunities for reforms that could further simplify UK tax rules and reduce compliance burdens, without exposing the UK tax base to significant risk." This is far from a commitment to scaling back anti-avoidance provision that may be less relevant following Pillar 2, but it indicates that there may be some hope.
Zoe Andrews	It looks as if the government will also take forward some of the other measures consulted on around aligning domestic rules with OECD standards, but we won't go into any further detail here. A technical consultation on draft legislation can be expected sometime this year. And what's the third transfer pricing item?
Tanja Velling	The Transfer Pricing and Diverted Profits Tax statistics for the tax year 2022/ 2023 which were published at the end of January. The transfer pricing yield has gone up from the previous year, but remains below the high of 2021/ 2022. In contrast, the net DPT amount has decreased – it's about a fifth of what it was last year. The amount of additional tax from settled DPT investigations has also decreased, although less steeply. The number of DPT notifications has gone down as well. The number of agreed APAs and ATCAs has further declined, but the average time it takes to agree an APA has also come down from 58.3 to 45.5 months (whereas the average time to agree an ATCA has increased to 58 months). There are also statistics on MAP and the use of the profit diversion compliance facility.
Zoe Andrews	Large MNE groups now have an alternative to APAs and MAP for getting increased and earlier tax certainty. The International Compliance Assurance Programme (ICAP) is a voluntary programme for multilateral cooperative risk assessment and assurance for large MNE groups headquartered in the jurisdiction of one of the participating tax administrations. The UK has participated since the first pilot kicked off in 2018 together with Australia, Canada, Italy, Japan, the Netherlands, Spain, and the US. After the success of two pilots, it is now an established programme with more than 20 participating tax administrations, and more are in discussion about joining. So how is the programme shaping up?

Tanja Velling	The OECD statistics published at the end of last month showed that ICAP is working effectively with 20 cases having been completed by October 2023. Looking at those 20 cases, 40% of the groups had low-risk assessments regarding key transfer pricing risk areas. A low-risk assessment means that a tax administration does not anticipate that any further enquiries will be required for the periods covered by the risk assessment. ICAP does not provide the binding legal certainty of an APA or the mutual agreement procedure (MAP) which may still be the preferred route for higher-risk areas but at least ICAP allows an MNE to see which risk areas are not low-risk and focus resources on resolving those, for example by requesting an APA. And if other action is required following ICAP, such as an audit, APA or MAP, information from the ICAP will be used in the follow-up action and will significantly speed up these processes. So what is the benefit of ICAP for taxpayers and how long does it take to get a risk assurance letter through the ICAP process?
Zoe Andrews	The average time taken from the start of the ICAP process to the issuance of risk assessment outcomes was 61 weeks – this was higher than the target of 52 weeks set out in the OECD's ICAP Handbook, but this was in part due to the impact of the pandemic on the second pilot. The benefit to the taxpayer is that it is a quick and efficient way to get a risk assessment from multiple tax administrations. The statistics show that the average number of tax administrations involved in a risk assessment is five but there have been up to nine tax administrations involved. One of the significant benefits of ICAP is that if issues are identified in the risk assessment, steps can be taken to resolve it within the ICAP process (for example to agree a transfer pricing adjustment) avoiding the need for audit and MAP. In the 20 cases referenced in the statistics, 32% of them involved issue resolution within ICAP. It is quite remarkable really, that the ICAP timeline is so short given that multiple jurisdictions are involved, multiple risk areas are considered and that the timeline may also include some issue resolution. So what sort of risk areas are covered by ICAP?
Tanja Velling	So far, ICAP has focused on five core areas of international tax risk: tangible goods, intangibles, services, financing and permanent establishment. Financing and intangibles had the highest proportion of not low-risk outcomes but even in these areas, 75% of tax administrations provided low-risk outcomes. According to the ICAP Handbook, other areas (such as hybrid mismatch arrangements, withholding taxes and treaty benefits) can be included in the risk assessment if MNE groups and the tax administrations agree.

	So if an MNE group wants to get into ICAP what should it do?
Zoe Andrews	There are two annual application deadlines for MNE groups to apply for ICAP in their headquarter jurisdiction: 31 March and 30 September. The application should be made to the tax administration in the MNE group's headquarter jurisdiction.
Tanja Velling	And now moving away from statistics to look at estimates. An updated OECD impact assessment on the effect of the global minimum tax on the taxation of MNEs was published by the OECD in January, and it appears that revenue yields, as estimated by the OECD, remain significantly higher than estimates by national governments. The OECD's latest estimate is that this new tax will result in additional global tax revenues of between USD 155 and USD 192 billion (which translates to between 6.5 and 8.1% of annual global corporate income tax revenues). Two-thirds of the additional tax revenues are expected to come directly from the global minimum tax and the other third from reduced profit-shifting as a result of behavioural change.
Zoe Andrews	That has gone down, then, from the estimate in January 2023 of USD 220 billion or 9% of global CIT revenues. Why is that?
Tanja Velling	Well, yes, the estimates have gone down. But we must remember that the process of assessing the economic impact of the global minimum tax is an iterative one which has come a long way in both methodology and figures from the first impact assessment in October 2020. The decrease in expected additional revenues since January 2023 is partly because the latest assessment used data from 2017-2020 which includes the period of the pandemic when many MNEs experienced lower profitability than was taken into account in the 2016-2018 data used a year ago. Another factor is that the new modelling and data more effectively account for the interaction of US GILTI and developments in the GloBE rules and take into account losses. But the impact analysis is still subject to many caveats, assumptions and modelled scenarios that will continue to vary.
Zoe Andrews	What I find quite interesting in the latest assessment is that there is substantial low-taxed profit in high-tax jurisdictions. "High-tax" here means average effective tax rate (or ETR) above 15%. According to the OECD's research, more than 50% of low-taxed profit globally is located in high-tax jurisdictions. Low-taxed profit in high-tax jurisdictions is mainly due to tax incentives such as tax holidays and patent boxes. Previous assessments had focused on low-taxed profit in low-tax jurisdictions. So which jurisdictions does the OECD expect to gain the most?
Tanja Velling	It appears that every jurisdiction would gain additional tax revenues unless they do not implement the rules and forgo revenues that would otherwise accrue to them! The distribution of revenue gains depends on implementation (you have to be in it to win it) and the behavioural reactions

	of MNEs. The jurisdictions with the most low-taxed profits (so, investment hubs) are expected to gain the most revenues in the short term (if they adopt a QDMTT to tax their low-taxed profits) but are expected to lose approximately 30% of their tax base over time due to reduced profit-shifting – this would then lead to revenue gains in other jurisdictions. So how much of the revenue gains from the global minimum tax is the UK expecting to see?
Zoe Andrews	The OECD does not make public the jurisdiction-specific impact so we have to look to information from the UK for this. At the Autumn Statement 2023 it was announced that: "The Multinational Top-up Tax, Domestic Minimum Tax and Undertaxed Profits Rule are expected to raise approximately £12.7 billion in the UK in total over the next 6 years." So about £2 billion a year then, assuming we do go on to implement the UTPR. The proof will be in the pudding, so to speak. We will only find out how accurate these estimates are once MNEs start to pay additional tax (which in the UK, for a qualifying multinational group with a year-end accounting period, will be 30 June 2026 for domestic top-up tax and multinational top-up tax). Any increased revenues due to the behavioural change which the OECD is expecting will be trickier to measure with any accuracy!
Tanja Velling	There is also some Pillar Two news in respect of the EU. The European Commission adopted a package of infringement decisions in respect of Member States' failures to transpose directives. Estonia, Greece, Spain, Cyprus, Latvia, Lithuania, Malta, Poland and Portugal were named as Member States who failed to communicate national measures transposing the Pillar Two Directive. Other transposition failures relate to DAC7, the EU Emissions Trading System and measures to counter VAT fraud, as well as a number of other Directives.
Zoe Andrews	For the first half of this year, Belgium holds the Council Presidency. The programme indicates that the fight against tax evasion, avoidance and aggressive planning will be given priority, as well as the "VAT in the Digital Age" package. The Belgian Presidency also "welcomes" the Business in Europe Framework for Income Taxation and "supports" Unshell (also often referred to as ATAD3) – although these appear to rank lower on the list of priorities. So, one might remain sceptical as to the likely progress of these two measures over the next six months. But what do we have coming up over the next month or so?
Tanja Velling	Well, let me start with a plug for an upcoming event! Slaughter and May will be hosting an International Women's Day Celebration on the evening of the 5th of March for Women in Tax, Women of the IFA Network, the CIOT and ADIT. You can sign up through to the event through the Women in Tax Eventbrite.

	Zoe and I are super excited about the event, and we're certainly planning to go. It would be great to see some of our listeners there!
Zoe Andrews	Otherwise, in the UK, we're still following the passage of the Autumn Finance Bill through Parliament. There were a few government changes, including to add provisions for the investment allowance for the Electricity Generator Levy. In addition to the International Women's Day event, the 5th of March will see the Court of Appeal hearing in the *BlackRock* unallowable purpose case. And there will be the Spring Budget on the 6th of March.
Tanja Velling	I have also heard that people are expecting the OECD to publish a new section on Amount B for the Transfer Pricing Guidelines; we will have to wait and see on that.
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.