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The Autumn Budget measures relevant to financial institutions include a reduction in bank surcharge to 3% from April 2023 and a consultation on re-domiciliation of companies permitting a change in place of incorporation whilst preserving the legal identity of the entity. The Finance Bill 2022 legislation contains just two triggers for uncertain tax treatment notification as the government continues to consider how to make the third trigger workable. Changes are announced to diverted profits tax with immediate effect which: prevent HMRC issuing a closure notice until after a DPT review period has ended; extend the period during which corporation tax returns can be amended during a DPT review period; and ensure DPT is a covered tax for MAP. A consultation is promised on the design of rules enabling life insurers to spread the transitional impact of IFRS 17 for tax purposes and removing the requirement to spread acquisition expenses over seven years. Political agreement is reached on further aspects of international tax reform including agreement with the US on how the UK, and four other countries, will transition from their unilateral digital services taxes to the new global rules.

Autumn Budget/Finance Bill measures relevant to financial institutions

Bank taxation

A review of bank taxation has been taking place to ensure banks do not pay too high a rate of tax when the corporation tax rate increases to 25% in 2023. Banks currently pay a corporation tax rate of 27%, comprised of standard corporation tax at 19% and the 8% surcharge.

The rate of the bank corporation tax surcharge will reduce from 8% to 3% so that in 2023 banks will pay a corporation tax rate of 28% (25% plus 3%). This is still an increase of 1% on what banks currently pay – but is described as competitive with other financial centres including New York and Paris (although the rate of corporation tax in France is set to fall to 25% in 2022!). In order to support growth for small and mid-sized banks within the UK banking market, which in turn promotes competition and is beneficial for consumers, the group profits threshold above which the surcharge kicks in will be reduced from £25m to £100m. You could also be forgiven for missing the fact it will still result in an overall increase in the corporation tax rate on banking profits amidst the “Budget for champagne swilling bankers!” headlines.

Re-domiciliation regime consultation

Continuing with the theme of making the UK an attractive jurisdiction in which to locate a business and in which to invest, the government has launched a consultation on re-domiciliation which is open until 7 January 2022. The consultation invites responses to a number of questions considering the possibility of allowing a foreign-incorporated company to change its place of incorporation to the UK while maintaining its legal identity as a foreign body. It also considers, but seems more luke-warm about, the possibility of UK incorporated companies re-domiciling abroad. If outward re-domiciliation were to be permitted, measures to protect against unintended consequences and risks to the UK’s economic interests will be required.

Although the idea of re-domiciling is, in principle, a good one (reducing the administrative complexity and costly regulatory issues or tax consequences of other routes of relocating to and incorporating in the UK), in practice it may not be as useful as it sounds because you would only be able to re-domicile from the limited number of other jurisdictions which allow outbound re-domiciliation. That said, both the Cayman Islands and Jersey are on that list and many groups still have UK tax resident companies which are incorporated there for various historic reasons and have asked in the past whether it is possible to reincorporate them in the UK because various external parties identity them as tax haven group companies notwithstanding their UK tax

residence. Clearly this would be a welcome development for them.

The tax implications, including the impact on a company's tax residence status and the need to prevent loss importation, of implementing a UK re-domiciliation regime are considered and inevitably these include protections against re-domiciliation being used as a means of avoiding UK tax.

One proposal which goes broader than just for re-domiciliation and would be a welcome change relates to capital gains and intangible asset base cost. Under current rules, when companies migrate residence to the UK, assets brought into the UK corporation tax net are brought in at their market value if the migration is from an EU country. The government is considering whether those rules should be expanded to migrations of companies from non-EU jurisdictions. This could also apply to migrations achieved under change in the central management and control of a company as well as to migration of residence resulting from re-domiciliation.

Tax is just one of the many considerations in play and this is just the start of the journey for this proposal. It will take some time to reach implementation by primary legislation but it will be interesting to follow its progress.

Notification of uncertain tax treatment for large business

The Finance Bill 2022 legislation published on 4 November contains just two of the three triggers which were in the draft legislation published in July. The third trigger, where there is a substantial possibility that a tribunal or court would find the taxpayer's position to be incorrect in material respects, was omitted from the Finance Bill but the government is considering it further for possible inclusion later. HMRC has been keen on the third trigger as a way of finding out and correcting problems with the legislation. But it has caused the most concern amongst taxpayers as it is so imprecise and difficult to apply. The two triggers which did make it into the Finance Bill, where provision has been made in the accounts for the uncertainty and where the tax treatment applied is not in accordance with HMRC's known position, are much clearer for the taxpayer to apply.

Impact of IFRS 17 on insurance companies

Finance Bill 2022 contains powers to lay regulations for insurance companies to spread the transitional impact of IFRS 17 for tax purposes and to revoke the requirement for life insurers to spread acquisition expenses over seven years for tax purposes. There will be a consultation on the design of these rules.

Post-Brexit flexing

It was interesting to see in this budget that the UK is starting to flex its post-Brexit muscles and make changes that would not have been possible when we were still part of the EU (such as the abolition of cross-border group relief, changes to the tonnage tax regime, air passenger duty, alcohol duty and R&D reliefs). Hopefully, this bodes well for potential changes to VAT on financial services and other measures to increase the UK's tax competitiveness.

Diverted profits tax

There has been much written about the recent First-tier Tribunal (FTT) case of Vitol Aviation UK Ltd and others v HMRC [2021] UKFTT 0353 (TC) which highlighted the difficulties faced by taxpayers trying to resolve transfer pricing disputes. Initially, this decision in which the FTT directed a closure notice to be issued even though the DPT review period was still open provided a welcome clarification of the interaction of DPT and corporation tax. A month later, however, it was announced that from 27 October the legislation is being amended in Finance Bill 2022 so that if a Tribunal directs a closure notice be given in a case with an open DPT review period, the direction will not have effect until the DPT review period has ended (which was the outcome HMRC had argued for in *Vitol)*. So although Vitol was successful in obtaining a closure notice when the DPT review period was still open, this will not be possible for other taxpayers unless their application for a direction for a closure notice was made before 27 September (the date of the *Vitol* decision).

The period in which taxpayers can amend their corporation tax return to make transfer pricing adjustments (and thus avoid a DPT charge) is also extended from the first 12 months of the 15-month review period to any time in the DPT review period, other than the last 30 days.

A further change to DPT included in Finance Bill 2022 ensures that for the purposes of the mutual agreement procedure (MAP) under a double tax treaty DPT is regarded as a covered tax for MAP decisions reached after 27 October 2021. TIOPA 2010, s 2 lists the taxes to which double tax treaties apply and currently does not specifically include DPT and HMRC has been known to contend that DPT should not be covered by the UK's double tax treaties arguing it is not a 'substantially similar' tax to corporation tax. This change will be welcomed by taxpayers seeking to resolve cross border transfer pricing disputes using MAP.

International tax reform

The political agreement of 136 countries announced on 8 October on the two pillars of international tax reform filled in some of the remaining blanks but there are still

many details to be worked through before implementation of the complex proposals, most of which are ambitiously scheduled for 2023.

The scope of Pillar One (re-allocation of taxing rights to market jurisdictions) is now very different from the OECD's unified approach and captures only a small number of the largest, most profitable multinational enterprises (MNEs). So one might ask whether it is really the solution to the problems of taxation of the digitalised economy? The answer is probably, not really but the important thing seems to be that it is a political solution which should lead to the 'tax peace', which Pascal Saint Amans speaks fondly about, by ensuring a rolling back of, and prevention of any new, unilateral measures.

The agreed quantum for allocation under Amount A of Pillar One is 25% of residual profit of in scope companies in excess of 10% of revenue. This was apparently agreed at the last minute as a compromise between those wanting 10% and those arguing for 30%.

One issue the G20/OECD political agreement left open was how those jurisdictions with unilateral measures already in place would go about transitioning from those unilateral measures to the new global solution and when this would happen. Then on 21 October it was announced that the US has reached a compromise agreement with 5 jurisdictions, including the UK, on this transition. The mechanism involves a DST-credit system to bridge the gap between the DSTs and the new system. In return, the US will not levy tariffs in response to the existing DSTs nor impose further trade actions and the parties to the deal can keep the revenues raised from their respective DSTs until the Pillar One reforms become operational.

In the UK this means that MNEs will be able to use the difference between the amount of UK DST that they have accrued from January 2022 until the earlier of 31 December 2023 and the date on which the Pillar One multilateral convention comes into force, and what their UK tax liability associated with Amount A as computed under Pillar One would have been if Pillar One (rather than the DST) had been in effect for that interim period, as a credit against their future UK corporation tax liability arising from the new taxing right under Pillar One.

The first payments of UK DST were due at the start of October for companies with an accounting period ending 31 December 2020. The DST was originally forecast to raise £500m per year, increased in the Spring 2021 Budget forecast to raising £3.2bn overall by April 2026. The Autumn Budget 2021 forecast clearly has not factored in the DST transition as it shows a further £0.7bn revenue is expected from DST by April 2026. Perhaps more certainty around the implementation of Pillar One and the compromise on DST is needed before this can be reflected in the forecast.

Interestingly, it was announced at the Autumn Budget that there will be a consultation on an online sales tax but the Red Book was careful to link this to a reduction in business rates rather than suggesting it as in any way replacing the DST. Whether the US will be persuaded to see it as something quite separate and not a 'relevant similar measure' to DSTs is an argument to be had in the future!

The big news on Pillar Two (global effective minimum taxation) is that a minimum rate of tax of 15% has been agreed and, because all the EU countries which are part of the inclusive framework, including Ireland, have now agreed to this, the European Commission intends to implement Pillar Two in the EU by way of a directive which will be proposed in January 2022. The formulaic substance carve outs start higher but transition over 10 years to an amount of income that is 5% of the carrying value of tangible assets and 5% of payroll. The substance carve outs are accordingly only of very limited effect.

What to look out for:

- **On 25 November the Court of Appeal is scheduled to hear the appeal in *Embiricos v HMRC* (whether a partial closure notice can be issued under section 28A of the Taxes Management Act 1970 without specifying the amount of tax due).**

- **On 6 December, the Upper Tribunal hearing is scheduled to begin in the appeal in *Royal Bank of Canada v HMRC* (the First-tier Tribunal held that a Canadian bank was subject to UK tax on royalties assigned to it during the receivership of a debtor. This was permitted by the UK/Canada double tax treaty and mandated by UK law.)**

- It was promised at the Budget that there will be a consultation on the VAT treatment of fund management fees 'in the coming months' and that there will be further 'tax administration and maintenance' announcements later in the Autumn.

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