

EU-UK FUTURE RELATIONSHIP - DIRECT TAX

WHAT DOES THE TRADE AND COOPERATION AGREEMENT (TCA) SAY?

Not very much.

The TCA includes:

- a commitment to implement principles of good governance and, in particular, global standards on tax transparency and exchange of information and fair tax competition;
- an affirmation of the OECD's Base Erosion and Profit Shifting Action (**BEPS**) Plan; and
- an undertaking to improve international cooperation in the area of taxation and facilitate the collection of tax revenues.

The EU and UK agreed not to weaken or reduce the level of legal protection on 31 December 2020 below that provided:

- for by the standards and rules which had then been agreed in the OECD in relation to:
 - the exchange of information concerning financial accounts, cross-border tax rulings, country-by-country reports between tax administrations, and potential cross-border tax planning arrangements; and
 - rules on interest limitation, controlled foreign companies and hybrid mismatches; or
- in relation to public country-by-country reporting by credit institutions and investment firms, other than small and non-interconnected investment firms.

Tax is excluded from the dispute resolution mechanism provided for in Part 6, Title I (*Dispute settlement*) of the TCA.

The text of the TCA is supplemented by a joint political declaration (**Political Declaration**) under which the EU and the UK affirmed their commitment to countering harmful tax regimes, in particular those that may facilitate base erosion and profit shifting in line with Action 5 of the OECD's BEPS Action Plan.

WHAT IS THIS LIKELY TO MEAN IN PRACTICE?

Regulations were laid before Parliament on 30 December 2020 to take advantage of the focus on OECD standards so as to restrict DAC 6 reporting to Hallmark D (*Common Reporting Standard and beneficial ownership*). Consultation, followed by legislation to align reporting in relation to cross-border arrangements to OECD model Mandatory Disclosure rules, are promised for 2021.

The TCA does nothing to alter the application of the Arbitration Convention to transfer pricing disputes (although the broader benefits of Directive 2017/1852/EU will not be available in relation to UK tax unless a claim was made prior to 1 January 2021).

The TCA leaves the EU, its Member States and UK free, provided the level playing field provisions contained in the TCA are not infringed and the Political Declaration is respected, to develop direct tax policy as they wish.

To the extent that EU-derived tax measures (such as the ability to pay interest and royalties gross to an associated company resident in an EU Member State) form part of UK domestic tax law, those measures continue to apply unless or until UK legislation is amended or repealed.

Since in 2018 HM Revenue and Customs (HMRC) reserved its position on the implementation from January 2022 of the "reverse hybrid" rule in article 9a of the EU's Tax Avoidance Directive (which includes an exclusion for 'collective investment vehicles'), and the consultation response HMRC published on 12 November 2020 was silent in relation to article 9a, it may be that the UK will decide not to implement (fully or at all) article 9a.

Tax is likely to remain a politically sensitive area. This has been highlighted by a letter which, we understand, a group of MEPs wrote in January 2021 to the President of the European Commission complaining about the insufficiency of the TCA's level playing field provisions in relation to tax and asking that the Commission use "leverage" retained by the EU in relation to financial services to extract more robust commitments from the UK in relation to "tax dumping and financial transparency".

An early indication of the UK's approach to post-Brexit tax policy may be revealed in the Chancellor's Budget statement to Parliament on 3 March 2021 (and the Finance Bill which will follow shortly after the Budget). Greater clarity should emerge, for example, in relation both to whether the proposed new regime for asset holding companies can allow the UK to offer a viable alternative to Luxembourg or Ireland and, also, as to the introduction of freeports.

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