



Advocates for International Development
Lawyers Eradicating Poverty

Brexit Briefing: Impact on Tax Matters

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Brexit Briefing: Impact on Tax matters

Executive Summary

- Many of the UK's tax laws should remain unchanged following Brexit
- Certain tax rules which derive from EU law are most at risk of change, although these changes are unlikely to occur for some time
- Organisations, including charities, with both UK and EU group members, and those who make supplies which are subject to VAT and/or customs and excise duties, should be aware of the changes which may be made to these areas of UK tax law following Brexit
- The availability of certain reliefs for charities may be at risk following Brexit, although the extent of any changes is unclear at this stage

Introduction

There is likely to be minimal immediate impact on the majority of the UK's direct tax law as a result of Brexit, as these taxes are purely domestic. Taxes which derive from or are impacted by EU law have largely been enacted into UK legislation, or reflected in the practice of Her Majesty's Revenue & Customs ("HMRC"), so these are also expected to survive Brexit, although they are likely to be a priority for reform post-Brexit. Any material changes to the UK tax system are likely to come only after Article 50 has been invoked and the two-year negotiation period has concluded. While the potential impact on UK tax law remains uncertain, we have identified four primary areas in which there is real potential for organisations including charities to be adversely affected. Given the current status of Brexit negotiations, organisations will need to wait and see as plans progress. The expectation is that, in due course, the UK government and HMRC will provide more clarity and detail around any proposed changes to the UK tax system, at which point organisations will be in a better position to consider what practical steps could be taken to mitigate the tax impact of such changes. We have set out below some thoughts on steps that could be taken in the medium term, once there is more certainty around the extent of any changes.



1. VAT

a) What will happen to VAT law on Brexit?

VAT is generally applied only within the EU and is regulated in accordance with EU-wide rules. Any form of Brexit would give the UK the freedom to amend or repeal its VAT rules. We think this is unlikely, however, given that VAT is so well established within the UK tax regime. There is therefore unlikely to be an immediate impact upon the assessment or collection of VAT. However, it is expected that UK VAT laws will diverge from the doctrines of EU law over the long term. UK companies may no longer be afforded protection under EU VAT principles, or have a right of appeal to the European Court of Justice.

The potential for changes to the existing VAT regime may have particular impact on charities. It is possible that, once able to make unilateral changes to the VAT system, HMRC will look to narrow the availability of zero rating (which is of key benefit to charities). Conversely, this may provide an opportunity for wider reform of the VAT system, including the creation of new exemptions and reduced ratings which could benefit the charitable sector. At this stage, charities will need to closely monitor discussions around potential amendments to the VAT landscape as a result of Brexit.

b) What should you be doing now?

Whilst currently we are in a period of “wait and see”, as the process of Brexit moves forward you may want to consider the following:

- You should consider your existing VAT position in light of possible changes to VAT law (e.g. particularly the rules on intra-EU supplies);
- You should consider whether any precautionary VAT planning should be undertaken;
- If you benefit from zero-rated (or exempt) supplies, you should identify any potential VAT risk you might incur if such exemptions were narrowed or repealed post-Brexit;
- You should review invoicing and systems requirements which may require updating in the event the UK ceases to be an EU member state; and
- You should assess whether your organisation benefits from any EU VAT reliefs which could be lost.



2. UK headquartered groups or resident companies

a) What will be the tax impact on UK headquartered groups, or groups with UK companies following Brexit?

The most significant and immediate tax consequence for group structures is likely to be in relation to withholding taxes. Currently, the EU Parent-Subsidiary Directive and the EU Interest and Royalties Directive operate to eliminate withholding taxes on the receipt of interest, royalties and dividends by EU companies from EU subsidiaries, subject to certain conditions. UK headquartered groups could lose this benefit post-Brexit. Double tax treaties, available tax credits and certain domestic exemptions may reduce the rate of tax in some cases, but not in all. EU headquartered groups with UK subsidiaries may also face additional taxes on receipt of dividends from UK companies post-Brexit, as the exemption provided by the EU Parent-Subsidiary Directive will no longer apply. The effect of losing the benefit of these Directives will vary on a country-by-country basis. It may be possible to effect a reorganisation or corporate restructuring in order to mitigate increased overseas tax bills, but this could have wider commercial and tax implications. Multi-national groups may also find that their position in relation to tax losses becomes less favourable post-Brexit if the rules which allow UK companies to surrender losses to and from their foreign affiliates are removed.

The above applies generally to taxable entities, and charities should take separate advice on the extent to which the unavailability of these EU Directives might impact them.

b) What should you be doing now?

Whilst currently we are in a period of “wait and see”, as the process of Brexit moves forward you may want to consider the following:

- If you rely on the Directives, you should review arrangements to identify:
 - (a) whether a group structure has only EU-wide protection and no separate UK domestic protection in respect of withholding tax on dividends, interest and royalties;
 - (b) whether withholding taxes can be mitigated; and
 - (c) the extent to which an existing group structure may be subject to a wider reorganisation resulting in associated tax costs or leakage.
- If you surrender to or receive losses from EU subsidiaries, you should consider whether these losses can be utilised before Brexit.



3. Customs and excise duties

a) What will happen to application of the EU customs code following Brexit? What will be the impact on UK companies?

There is an existing intra-EU customs union, and the UK currently applies the Common Customs Tariff. If the UK were to leave the customs union, there may be an increase in customs or excise duties and increased administration costs of EU/foreign trade. The worst case scenario would be that customs duty may apply to EU imports and exports, leading to increased costs of goods imported to the UK, and for UK goods sold into EU countries. It is likely that the UK would need to implement a new domestic tariff system. The UK will also risk losing the benefit of the EU Free Trade Agreements with third countries, which will be a potential barrier to trade. The UK will need to negotiate trade agreements with major partners, which is likely to be a protracted and uncertain process.

Whilst most goods imported into the UK by charities are exempt from customs duties, some of these exemptions rely on EU law and therefore these could be subject to amendment following Brexit. It is however unlikely that reliefs available to charities would be a focus for HMRC. Any changes will therefore be more likely to impact non-profit organisations that do not have charitable status.

b) What should you be doing now?

Whilst currently we are in a period of “wait and see”, as the process of Brexit moves forward you may want to consider the following:

- You should consider the impact that increased customs or excise duties could have on your activities;
- You should assess potential leakage or associated compliance costs that may arise in the event the UK leaves the customs union, or enters into new free trade agreements; and
- If you have cross-border supply chains, you should assess how new tariffs may increase (or indeed reduce) costs, and the related compliance burden.

4. Gift aid and other reliefs

a) What will happen to the availability of Gift Aid and certain other charitable reliefs and exemptions following Brexit?

In line with the EU wide mandate of harmonisation, UK taxpayers currently benefit from tax reliefs (in respect of income tax (“Gift Aid”), capital gains tax and inheritance tax) on charitable donations made to European charities and, similarly, UK charities can receive donations from EU donors which benefit from any tax reliefs applicable in the local donor country. Brexit is likely to impact this position, as the UK government will no longer be “bound” to provide this level playing field as between the UK and the EU, and EU countries may choose not to provide domestic reliefs for donations made to UK charities (or to impose conditions on such reliefs). It



should however be noted that these cross-border reliefs are only available where the non-UK charity meets specific conditions in order to demonstrate its charitable status, which only a small number of foreign charities have met to date. The loss of these reliefs may therefore have a limited overall impact on the tax efficiency of cross-border donations.

b) What should you be doing?

Whilst currently we are in a period of “wait and see”, as the process of Brexit moves forward you may want to consider the following:

- Consider the extent to which your charity benefits from EU donations as these could reduce as a result of post-Brexit changes; and
- To the extent that you have operations in other EU countries which receive donations from the UK, consider whether you can offer UK-based donation routes going forward, which may provide more certain tax reliefs to UK donors.

Checklist of Key Action Points

Whilst currently we are in a period of “wait and see”, as the process of Brexit moves forward you may want to consider the following for each issue:

- ✓ Monitor changes to the UK’s VAT rules as they are announced and consider what additional VAT costs you may incur if current VAT exemptions or reliefs were repealed post-Brexit
- ✓ Review tax treatment of cross-border EU payments and receipts and consider whether non-EU based reliefs would be available to mitigate any withholding tax costs post-Brexit
- ✓ Consider the impact that increased customs or excise duties could have on your activities
- ✓ Consider the extent to which your charity benefits from both UK and EU donations as charities may need to be flexible in order to help ensure that donors continue to benefit from tax reliefs following Brexit



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