Slaughter and May Podcast
Tax News Highlights: May 2021

Zoe Andrews	Welcome to the May 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 provide an update on the progress of the Finance Bill, look at HMRC's updated stamp duty guidance and discuss three recent cases, the First-Tier Tribunal decisions in *Euromoney* and *Aozora*, and the High Court decision in respect of the Danish tax authority SKAT's attempt to reclaim Danish withholding tax refunds. We will also cover some international tax topics, including the adoption of a new Article 12B for the UN's Model Tax Treaty. This podcast was recorded on the 11th of May 2021 and reflects the law and guidance on that date. Shall we start with the Finance Bill? Where are we with that?
Zoe Andrews	Well, the Committee Stage has concluded. The Report Stage and Third Reading have yet to take place, and will fall during the new Parliamentary session following the prorogation of Parliament from the 29th of April to the 11th of May.
Tanja Velling	During the Committee Stage, a number of Government amendments were passed. Amongst others, these confirm that the extended loss carry-back is not available to a furnished holiday lettings business that is treated as a trade under the Income Tax Act 2007.
Zoe Andrews	Amendments were also made to Schedule 7 on hybrid mismatches. In particular, the proposed changes to the definitions of "hybrid entity" and "investor" have been deleted from the Finance Bill 2021 – apparently, the drafters have been struggling to get the wording right and what was proposed might have produced some unintended consequences. The changes are now planned to be included in Finance Bill 2022, but they would still take effect from the 1st April 2017 – a recipe for continued uncertainty around the application of the hybrid rules.
Tanja Velling	On stamp duty, we wanted to highlight certain changes to the guidance entitled "Completing a stock transfer form". As anyone with experience of private M&A involving a UK target will know, the UK's paper-based process for paying stamp duty is unduly cumbersome and time consuming. The original stock transfer form is sent to HMRC and, once stamped, returned by second class post.

	I recall many a conversation where this description of the process would have been met with a horrified exclamation of "but what if the original gets lost in the post?" My only answer was an exasperated shrug paired with the observation that, fortunately, stock transfer forms don't seem to get lost all that often.
Zoe Andrews	The practical challenges associated with the paper-based process have been raised with HMRC on numerous occasions. Yet, nothing changed until the pandemic. But, as the lockdown arrived, stamp duty went paperless. HMRC updated its guidance to ask taxpayers not to send hardcopy documents. Instead, pdf copies were to be submitted by email and HMRC would send an email confirmation that stamp duty had been paid. Naturally, there were teething issues. Questions arose whether a company's registrar could rely on the electronic confirmation to update the share register. The answer is "yes". And whether, once restrictions were lifted, hardcopy documents would have to be re-submitted for stamping.
Tanja Velling	HMRC's recent update to its guidance finally answers this latter question. And the answer is "no". Stock transfer forms do not have to be re-submitted to actually be stamped, if the electronic replacement process for stamping was followed. Indeed, under the updated guidance, the electronic replacement process has become the default stamping procedure. Hardcopy documents should be submitted only where an electronic notification cannot be made – and it is envisaged that these would no longer be sent to the Birmingham stamp office, and would include only a copy of the stock transfer form (and not the original). The guidance states that taxpayers "must not post original[s] as [HMRC] will not retain or return them". So, that's quite a change. And it is certainly welcome, but you know what would have been even better, apart from finally abolishing stamp duty?
Zoe Andrews	Go on – tell me.
Tanja Velling	If the change was not just made through guidance. The stamp taxes legislation should really be updated to properly underpin the changed procedure, and I hope that a proposal for that will be published as part of any follow-up to last July's call for evidence on the modernisation of the stamp taxes on shares framework – unless the follow-up is a proposal to abolish stamp duty altogether which would, of course, be even better. But let's move on to look at some cases.
Zoe Andrews	The First-Tier Tribunal's decision in *Euromoney* is, at heart, a relatively simple case, reflected in the First-Tier Tribunal's relatively short 15 page judgment. The factual background can be boiled down to this. Economically, Euromoney's aim was to dispose of part of its investment in a joint venture. To this end, Euromoney agreed with a private equity house

	to sell all of its shares in the JV in exchange for cash and shares in the entity that would become the JV's parent.
Tanja Velling	At this point, the tax director became involved and, presumably, spotted that, on the sale of the JV shares, Euromoney would not be able to benefit from the substantial shareholding exemption.
Zoe Andrews	This may sound surprising. The JV was a trading company and Euromoney held a large portion of the share capital. So, one would normally expect SSE to apply. The issue seems to have been that Euromoney's stake did not carry a right to dividends and that, therefore, its stake could not count as a substantial shareholding for SSE purposes.
Tanja Velling	So, prior to the tax director's involvement, the transaction would have been part share exchange, which would have qualified for rollover treatment, and part cash sale, which would have triggered a gain and a corporation tax liability. In respect of the cash element, the tax director then proposed a flip to preference shares which would be turned into cash a year later. The intention was that this should secure rollover treatment for both elements and that SSE would apply on conversion of the preference shares into cash.
Zoe Andrews	The unfortunate result was, however, that HMRC challenged the application of rollover treatment in respect of the whole transaction – including the part which would have been a share-for-share exchange all along. This was on the basis that the exchange formed part of an arrangement with a main purpose of tax avoidance. The FTT disagreed with HMRC and decided the case in favour of Euromoney on the basis that there was no main tax avoidance purpose.
Tanja Velling	So, this is another high profile purpose test case which was decided by the FTT in favour of the taxpayer. The other one was *Blackrock* which we covered in the November 2020 edition of our Tax News Highlights podcast. In *Blackrock*, the FTT had found that there was a tax avoidance main purpose, but none of the debits at issue were attributable to that purpose. The difference between the legislative provisions is noteworthy – in *Blackrock*, the FTT had two ways of deciding the case in favour of the taxpayer, either by deciding that there was no tax avoidance main purpose or by deciding that no disallowance resulted from the presence of such a purpose. In *Euromoney*, the legislation did not provide for the latter option; so, deciding the case in favour of the taxpayer necessitated finding that there was no main tax avoidance purpose. With that, shall we move on to two key lessons from *Euromoney*?

Zoe Andrews	Sure. The first is the importance of how the arrangement is defined. If the arrangement had been just the issuance of preference shares as opposed to the payment of cash, Euromoney would have lost. The FTT, however, found that it was right to look at the arrangement as a whole because to do otherwise would give a distorted view and lack reality. The key factor here seems to have been that the preference shares constituted a relatively small portion of the overall consideration.
Tanja Velling	Secondly, witness evidence is key. Like Blackrock, Euromoney called one tax and one business witness, and their testimony led the FTT to find that "the potential tax saving…was not important to Euromoney" and that "tax was not a main driver of the transaction". Noting that a purpose can be more than trivial without being a main purpose, the FTT concluded that Euromoney's main purposes were commercial.
Zoe Andrews	In *Aozora GMAC Investments Limited v HMRC*, Aozora received interest payments on loans it made to its US subsidiary and sought relief from the double taxation of those interest payments being subject to corporation tax in the UK, but also being subject to US withholding tax. The US/UK tax treaty normally provides relief in this situation by permitting a refund of the US withholding tax, or allowing a credit of the US tax against the UK tax on the interest. But the Limitation on Benefits article was triggered which meant that Aozora was denied treaty benefits because lowering the group's overall tax liability was critical to the way the loans were structured (the loans were made from the UK rather than directly from Aozora Japan because the rate of tax on interest received in Japan was 41%). Aozora was therefore unable to obtain a refund of the withholding tax under the treaty and so applied to the US competent authority for discretionary treatment under the Limitation on Benefits Article 23(6), but this was refused as it could not be determined that the establishment, acquisition or maintenance of Aozora and the conduct of its operations did not have as one of its principal purposes the obtaining of benefits under the treaty.
Tanja Velling	Having been denied treaty benefits, Aozora made claims in its tax returns for unilateral relief by way of credit against the UK tax due on the interest which brought the amount of corporation tax self-assessed to nil. The credit was claimed under section 790 of the Income and Corporation Taxes Act 1988 which has now been rewritten as section 18 (and various other sections in Part 2) of the Taxation (International and Other Provisions) Act 2010. But HMRC assessed Aozora to tax of nearly £4.5 million on the basis that section 793A of ICTA applied to prevent unilateral relief under section 790. HMRC calculated the tax for the relevant accounting periods on the basis that Aozora were entitled to relief under section 811 of ICTA and suffered UK corporation tax on the net amount received (after deduction of the US withholding tax).

Zoe Andrews	Where treaty relief is unavailable to a taxpayer, section 790 gives unilateral relief in certain circumstances and subject to section 793A which applies to limit the availability of unilateral relief. Section 793A(3) (which has been rewritten as section 11(3) of TIOPA) denies unilateral relief where a tax treaty contains "express provision" to the effect that relief by way of credit shall not be given under the treaty. The key issue in this case was whether section 793A(3) denied Aozora entitlement to unilateral relief. HMRC argued that section 793A(3) applies where the terms of a double tax treaty have the effect that credit relief "shall not be given".
Tanja Velling	But the FTT found that, in order for section 793A(3) to have effect to exclude credit relief, the terms of the double tax treaty must be explicit as to the cases and circumstances in which the credit relief is not available. The FTT found that the US/UK tax treaty is not explicit on this, and in particular the Limitation on Benefits article is not "an express provision to the effect that relief by way of credit shall not be given". Consequently, section 793A(3) did not apply to prevent unilateral relief in respect of the US withholding tax imposed on the interest received by Aozora. This is a helpful case for taxpayers in similar scenarios who find that they are prevented by a Limitation on Benefits article from getting treaty benefits and wish to claim unilateral relief.
Zoe Andrews	The final case we wanted to mention is the High Court case brought by the Danish tax authority, SKAT, and this takes me right back to the constitutional law module of my university days. This case is important in terms of public profile, the amount of money at stake and the principles of the case. SKAT had brought civil litigation proceedings to, in substance, indirectly enforce Danish tax law although SKAT argued it was a private law action.
Tanja Velling	The case concerns thousands of Danish withholding tax refund claims over a three year period totalling around £1.5 billion which SKAT maintains were paid in error because misrepresentations had been made to SKAT inducing the approval and payment of the claims. In total, 114 defendants are named in the proceedings. This meant that, at the time of the preliminary issue trial, 21 separate legal teams from 18 firms of solicitors had responded to SKAT's various claims – and that just accounts for 74 of the defendants!
Zoe Andrews	The High Court held that SKAT's claims fell foul of Dicey Rule 3, which requires English law courts to dismiss claims that ask the court to enforce a foreign state's sovereign authority. The High Court identified the central issue in the case as the Kingdom of Denmark's sovereign right to tax Danish company dividends. The Danish Tax Authority has already said that it will appeal the decision.

Tanja Velling	After this UK case with an international flavour, our other international tax topics shall follow quite naturally. Zoe, what are your thoughts on the potential impact of President Biden's US tax reform proposals on the OECD's international tax reform project?
Zoe Andrews	I watched a seminar last week hosted by the Oxford University Centre for Business Taxation in which various speakers were invited to discuss the OECD's international tax reform project in light of the renewed interest and support from the US under the Biden/Harris administration. The Made in America Tax Plan proposes changes to the US tax system to discourage offshoring and bring activities and jobs back to America. So why is this of interest to the OECD's project? The proposals include changes to the US GILTI rules which impose a minimum rate of tax on foreign income. If the proposals get enacted, it will make it easier for the US GILTI rules to co-exist with the OECD's global minimum tax proposals under Pillar 2 of the project. At the moment, GILTI permits global blending of tax rates which encourages tax planning to mix the high and low tax rates, whereas the proposal is to move this to jurisdictional or country by country blending – which is where Pillar 2 is currently at.
Tanja Velling	The rate of GILTI is currently 10.5% but the Tax Plan proposes an increase to 21%. So, it will be in the interest of the competitiveness of the US for other countries to adopt a minimum tax, too, which is why Janet Yellen, the US Secretary to the Treasury, has spoken out in support of a global minimum tax rate. What such a minimum rate will be is hard to predict – Ireland will obviously not want it set above 12.5% but at the other end of the spectrum, the US will be keen on a higher rate of up to 21%, comparable with whatever the increased GILTI rate ends up being.
Zoe Andrews	Another point of contention is that the US does not want a substance-based carve out from the minimum tax rate (and, indeed, one of the proposed changes to GILTI removes the exemption for 10% of tangible assets). A substance-based carve out is being discussed, however, and was included in the blueprint for Pillar 2. In the absence of a substance-based carve out the minimum tax rate would simply be limiting tax competition rather than, as was the OECD starting point, putting in a safety net to address remaining base erosion and profit shifting risk.
Tanja Velling	As the global minimum tax is part of a package with a new taxing right and profit allocation to market jurisdictions under Pillar 1 of the project, the US realises that, to get a deal done, it needs to be on board with Pillar 1, too. But the scope of Pillar 1, as shown in the blueprint from October 2020, is too broad for the US and the US has proposed to narrow it, so that it targets just the biggest 100 companies globally. Whether this is acceptable to the OECD Inclusive Framework members remains to be seen. Certainly, the position of the UK has consistently been that the issue of how to tax digitalised businesses fairly and without creating distortions has to be

	solved, meaning that, if the scope of the new taxing right is narrowed so much that it does not catch the main digital players, this is unlikely to be acceptable to the UK.
Zoe Andrews	The change in US administration is significant and there is, in the words of Pascal Saint-Amans a desire for "tax peace". So there is certainly an increased momentum to get global consensus. The forever optimistic Pascal Saint-Amans is hopeful that, by October of this year, there will be a package agreed. But with so many competing ideas and requirements I still find it difficult to see a satisfactory compromise being reached which ticks enough boxes for enough people. And even if something is agreed and implemented, further reform is likely to be required in the future to deal with issues "too difficult" to resolve right now.
Tanja Velling	The OECD is not the only player in international tax. The United Nations have adopted a new Article 12B for their Model Treaty which is what most developing countries' tax treaties are based on. The new Article comes at the issue of allocating taxing rights to market jurisdictions from a bilateral treaty perspective. It does not give a new taxing right, but rather removes the requirement for physical presence in order for taxing rights over payments for automated digital services to arise. It is much simpler than Pillar 1, but it does not have its own dispute resolution system and requires underlying domestic law to apply it.
Zoe Andrews	The OECD is consulting until the 28th of May on proposed changes to the commentary on the OECD's Model Treaty to clarify the application of Article 9 (Associated enterprises), especially as it relates to domestic laws on interest deductibility. Consequential amendments are also proposed to the commentary on articles 7 (Business profits), 24 (Non-discrimination) and 25 (MAP). The changes put forward in the discussion draft are expected to be included in the next update to the OECD Model Tax Convention.
Tanja Velling	This work is closely linked to the Transfer Pricing Guidance on Financial Transactions published on the 11th of February 2020 and to the BEPS Action 4 report recommendations on interest deductibility.
Zoe Andrews	I'd like to highlight three points in particular. First, the changes clarify that the setting of an arm's length price and domestic restrictions on the deductibility of that price (for example through interest restriction rules) are two different things; article 9 is not concerned with domestic restrictions on the deductibility of expenses. Secondly, the changes delete references to domestic thin capitalisation rules and insert commentary concerning the need to consider whether the interest amount can be regarded as the arm's length amount and whether a

	loan should be regarded as a contribution to equity capital, referring to both domestic law and the OECD Transfer Pricing Guidelines. Thirdly, the changes also clarify that a state has to make a corresponding adjustment only to the extent that it agrees that another state's adjustment is in line with the arm's length principle.
Tanja Velling	As for important dates during the next few weeks, the consultation on changes to the commentary on Article 9 of the OECD's Model Tax Convention closes on the 28th of May, and a number of consultations in the UK close at the start of June. Most of them close on the 1st of June, including those on notification of uncertain tax treatment by large businesses, transfer pricing documentation and clamping down on promoters of tax avoidance. The closing date for the consultation on reforming the taxation of securitisation companies is the 3rd of June. And, going back to the nearer future, two important UK Supreme Court decisions are due to be released this Friday, the 14th of May. They are the decisions in *Hurstwood Properties v Rossendale Borough Council* where the Council sought to apply the *Ramsay* principle in respect of non-domestic rates, and in *Tooth*, which raised questions around concepts of staleness and deliberate conduct in respect of discovery assessments.
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