TRAVERS SMITH

Brexit:
Tax Implications

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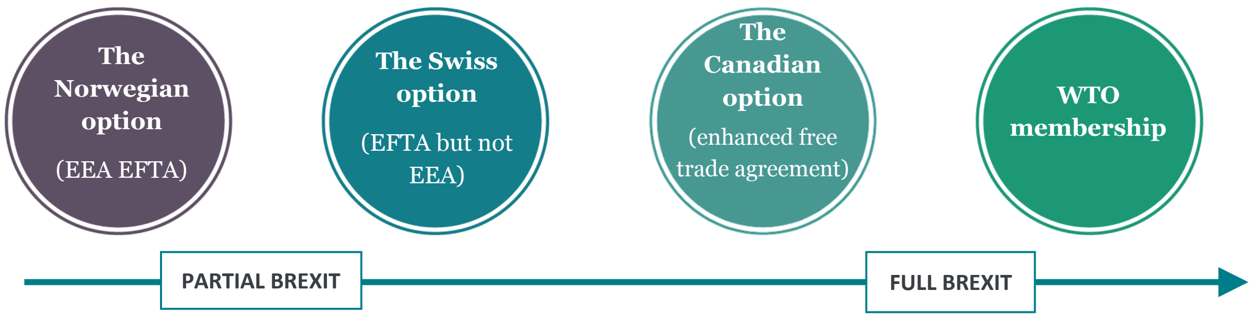
Brexit: High level UK tax implications

The tax consequences of Brexit will depend to some extent on the new relationship negotiated between the UK and the remaining EU Member States. Several different options have been mooted in recent weeks, ranging from membership of the European Economic Area (EEA) (partial Brexit) to merely relying upon World Trade Organisation (WTO) membership (full Brexit).

Our initial thoughts are that Brexit will have direct implications in the following areas of UK tax law: VAT, customs duties, EU tax directives and state aid. The nature of Brexit may also result in changes in the extent to which UK tax law is required to be consistent with the rights to freedom of establishment and free movement of capital. It is also likely that Brexit would have indirect consequences on taxation policy and legislation, as the UK responds to the altered economic and commercial position outside the UK. This note only considers the first four areas of tax impact.

Options for relationship between the UK and the EU



What is the EEA?

The EEA is made up of the EU Member States and the three EEA EFTA states (Norway, Iceland and Liechtenstein). The EEA EFTA states are the countries which are members of the European Free Trade Area (EFTA) which have opted to be members of the EEA.

The EEA Agreement provides that the EEA EFTA states must adopt EU legislation covering the four fundamental freedoms: free movement of goods, services, capital and persons. The EEA agreement also covers certain other complementary areas, but does not cover direct or indirect taxation.

COVERED BY THE EEA AGREEMENT

- Free movement of goods, persons, services and capital
- Competition and state aid rules
- Consumer protection, company law, environment, social policy statistics

NOT COVERED BY THE EEA AGREEMENT

- Common agriculture and fisheries policies
- Customs union
- Common trade policy
- Common foreign & security policy
- Justice and home affairs
- **Direct and indirect taxation**
- Economic and monetary union

There are four joint EEA bodies:

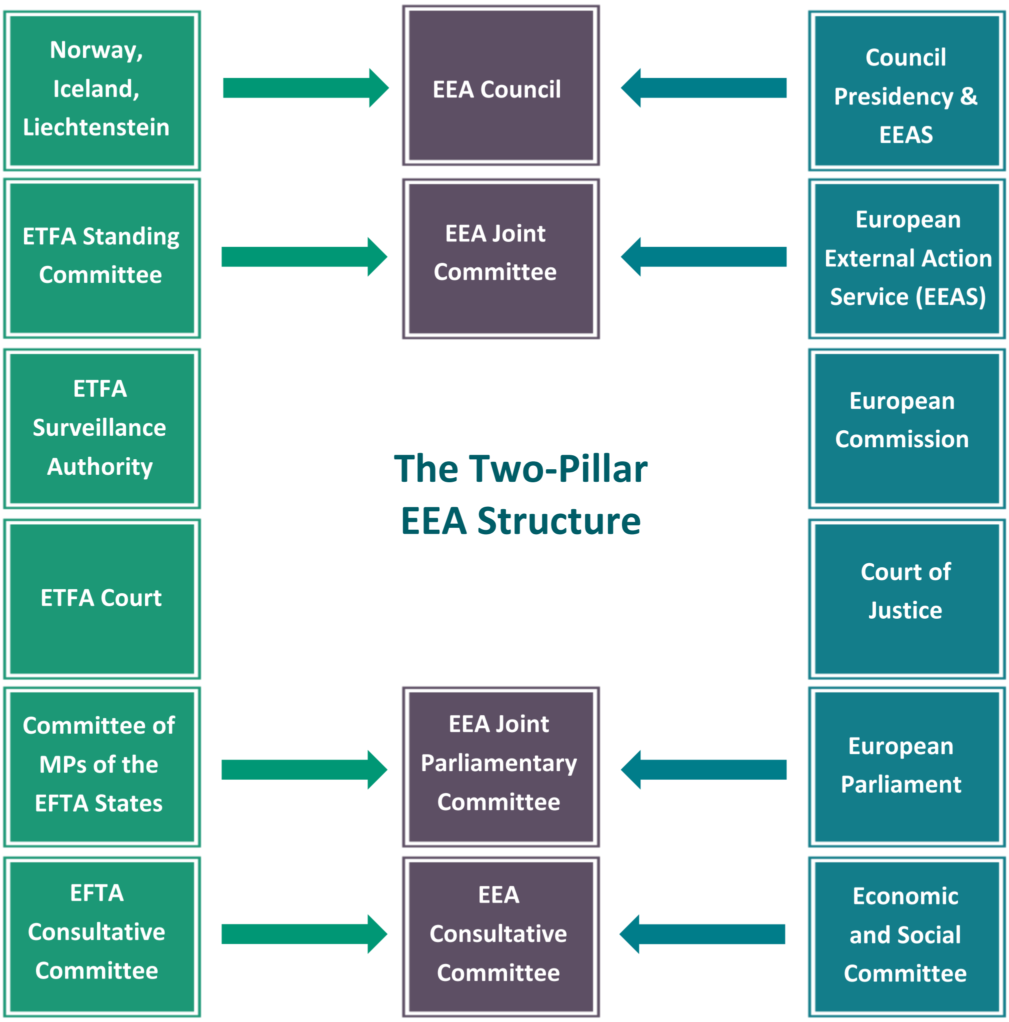
1. **The EEA Joint Committee:**
responsible for management of the EEA Agreement and decisions relating to the incorporation of EU legislation into the EEA Agreement.

2. **The EEA Council:**
provides political impetus for the development of the EEA Agreement.

3. **The EEA Joint Parliamentary Committee:**
debates and discusses the content of the EEA Agreement.

4. **The EEA Consultative Committee:**
a forum for cooperation and consultation between the EEA EFTA countries and the EU.

As the EEA EFTA countries have not transferred any legislative powers to the joint EEA bodies and are constitutionally unable to directly accept decisions made by EU institutions, a set of EEA EFTA bodies mirroring the EU institutions were established under the EEA Agreement, giving rise to a **"two-pillar structure".**



If the UK wishes to join the EEA, its accession would need to be agreed to by all 30 EEA members, and also by Switzerland as the fourth EFTA country.

The Swiss Option

Switzerland is a member of EFTA, but not of the EEA. Instead, Switzerland has entered into a framework of bilateral treaties with the EU. These treaties give Switzerland partial access to the single market, in exchange for accepting the principle of free movement of persons.

Tax implications of Brexit

1. VAT
2. EU Tax Directives
3. State Aid
4. Customs Duty

Depending upon the nature of the UK's relationship with the EU following the time of actual exit, there also may be wider tax implications. This is because the UK may no longer be required to legislate in accordance with the rights to freedom of establishment and free movement of capital. To date, these EU law principles have required the UK to make changes to its CFC rules and its group relief rules, to name but a few. Detailed consideration of this area is outside the scope of this note.

VAT

Introduction

VAT is a European tax which has been implemented into UK domestic law. From the time of actual exit from the EU, the UK government will be free to decide whether to retain or repeal existing VAT legislation. This will be the case even if the UK joins the EEA, as VAT is not covered by the EEA agreement.

As VAT represented 22% of the UK's annual tax revenue for 2015-16, it is extremely unlikely that the UK government will abolish VAT. It is also unlikely that the UK government will replace VAT with a new goods and services tax, since it would be too disruptive and expensive to introduce a new tax.

However, the UK government will have the opportunity to tinker around the edges with VAT, reforming illogical areas and departing from CJEU decisions that are contrary to HMRC's practice or the UK's preferred policy outcomes. For example, the government might choose to make changes to the rules on input tax recovery on deal fees, amend the VAT rules relating to construction or to alter the rules relating to VAT on fund management fees. The government would also have the full freedom to set the standard rate of VAT (under EU law the standard rate must be between 15% and 25%), or to introduce new categories of zero rated products. However, the government would have to balance any cut in the standard rate or new zero-rated categories with the need to preserve current levels of VAT revenue.

Impact on Cross-Border Supplies

From the time of actual exit from the EU, the UK will be a non-Union country. This may result in some changes to the place of supply rules. It also may result in changes to the time at which VAT is payable. Any changes to excise duty are outside the scope of this note.

Cross-border supplies of services

Business to business supplies

Under the default place of supply rule, services supplied to a business are supplied in the country in which the recipient is established. In Example 1, the services would be regarded as being supplied in the UK because the recipient of the services (UK Co) is established in the UK. This means that UK VAT is chargeable.

Example 1:

UK Co must account for the UK VAT chargeable on the supply under the reverse charge mechanism. In its VAT return, UK Co must

- credit its account with output tax chargeable on the supply (as if UK Co had supplied the service itself) and
- debit its account with any allowable input tax.

The default place of supply of services rules apply to transactions with both EU and non-EU business counterparties. Assuming the current place of supply rules stay the same (under both the VAT Directive and UK domestic law), following the UK's departure from the EU, Example 1 would result in the same VAT consequences as those outlined above.

Business to customer supplies

Different place of supply rules apply to supplies to non-business customers, and to special categories of supplies. Where the recipient is a not carrying on an economic activity (as defined by the VAT Directive), the recipient is a non-taxable person or non-business person. Under the default place of supply rule, services supplied to a non-business are supplied in the country in which the supplier is established.

However, supplies of certain services – including legal, consultancy and electronically supplied services – to non-business customers who are established or resident outside the EU are treated as supplied in the place where the customer is established or resident.

In Example 2, UK Co is a holding company that doesn't supply any management services or carry out any activities other than the holding of shares. As a result, UK Co is not carrying on an economic activity and is a non-taxable person or non-business person.

Example 2:

Until the UK leaves the EU, the supply of services will be governed by the default rule for supplies of services to non-business persons; the supply of legal services will be in the Netherlands and Dutch VAT will be chargeable. (This would remain the position after the UK left the EU for supplies of services that are not in the category of specified services referred to above.)

Assuming the current place of supply rules remain the same, when the UK leaves the EU, the special rule for legal supplies to non-EU non-business persons will apply and the supply will be treated as being made in the UK of legal services rather than the Netherlands. However, as UK Co is not a business person, it will not be required to account for UK VAT on the supply under the reverse charge mechanism. As a result, no VAT would be payable in Example 2.

Mini-one stop shop

Cross border supplies of digital services to non-business customers are supplied in the EU Member State in which the customer is located. Rather than registering for VAT and filing VAT returns in each Member State in which the business has customers, suppliers of digital services can register for VAT in one Member State and use the mini-one stop shop (MOSS) to discharge their VAT liability in other Member States. Under MOSS, a single VAT return and payment is filed with the tax authority in the Member State where the business has registered for VAT and that tax authority sends the relevant parts of the return and VAT payments to the Member States in which the customers of the business are located.

Unless specifically preserved in any agreement entered into between the UK and the EU, from the time of actual exit, UK businesses and UK VAT will no longer be covered by MOSS. This means that UK and other non-EU businesses will no longer be able to use a UK VAT registration to deal with its EU-wide VAT liabilities under MOSS. It also means that businesses registered for MOSS in an EU Member State will not be able to use MOSS to deal with their UK VAT liability.

Cross-border supplies of goods

The place of supply rules for goods depend upon whether the customer is a taxable person and whether the supplier is located in an EU Member State or a non-EU country.

Acquisition VAT

Inbound transfers of goods from one EU Member State to another are called acquisitions. Acquisition VAT is chargeable in the Member State where the customer is established where there is an intra-EU movement of goods and both parties to the transaction are VAT registered.

In Example 3, the goods start off in a German warehouse and are delivered to UK Co's UK factory. German Co is registered for German VAT and UK Co is registered for UK VAT. UK acquisition VAT will be chargeable on the supply of goods.

Example 3:

UK Co must account for the acquisition VAT as output VAT in its VAT return, but can set off any allowable input VAT in respect of the supply in the same return.

Following actual exit from the EU, the supply of goods would no longer be an intra-EU supply and acquisition VAT would no longer be applicable. Instead, import VAT (covered below) would be applicable as regards the position of UK Co.

Intra-EU cross-border supplies by a VAT registered supplier to non-taxable / non-registered persons are usually subject to VAT in the country in which the supplier is established. However, once the value of supplies into the customer Member State exceeds the local distance selling threshold (the UK annual threshold is £70,000), the supplier must register for and charge local VAT on future supplies to customers in that Member State.

Import VAT

Goods imported into the UK from non-EU countries are subject to UK import VAT, whether or not the person importing the goods is registered for UK VAT. Import VAT is due at the time of importation unless the importer has been approved by HMRC for deferment. Import VAT can be claimed as input tax by UK taxable persons if it is allowable under normal rules.

From the time of actual exit, the UK will be a non-Union country. This means that all inbound cross-border supplies of goods will be subject to import VAT rather than acquisition VAT. This will result in UK VAT registered businesses (that have not been approved for deferment) paying VAT on supplies of goods from remaining EU countries at an earlier time – the time of import – than would currently be the case, giving rise to a cash flow disadvantage.

Tax Directives

Introduction

From the time of actual exit from the EU, the UK would no longer give effect to any of the EU Tax Directives (save to the extent implemented into UK law and that the law hasn't been amended or repealed). The main EU Tax Directives (apart from the VAT Directive) are as follows:

1. Parent-Subsidiary Directive
2. Interest and Royalties Directive
3. Cross-border Mergers Directive
4. Directive on Administrative Cooperation
5. Capital Duties Directive

The Council approved the Anti-Tax Avoidance Directive on 12 July 2016. It remains to be seen whether the UK will implement the provisions of the Anti-Tax Avoidance Directive, given that the deadline for implementation is not until 31 December 2018 (31 December 2019 in relation to the exit taxation rules).

Of these, the key directives from a day-to-day perspective are the Parent-Subsidiary Directive and the Interest and Royalties Directive.

Parent-Subsidiary Directive

The Parent-Subsidiary Directive provides for the elimination of withholding tax on intra-EU cross-border dividend payments where the parent company holds at least a 10% interest in the subsidiary. It also provides that the receipt of dividends must either be exempt from tax in the hands of the parent company, or that the parent company jurisdiction must give credit for tax on the underlying profits in the subsidiary jurisdiction.

Other than in relation to REITs, the UK does not impose withholding tax on dividend payments.

The UK currently complies with the second limb of the Parent-Subsidiary Directive by exempting the receipt of dividends from corporation tax provided the dividend satisfies the conditions of the dividend exemption. It is not envisaged that the UK will make any changes to its dividend exemption following its exit from the EU, since this would damage the UK's competitiveness as a holding company jurisdiction. However, remaining EU Member States would be able to charge withholding tax on dividend payments to UK parent companies (subject to the rates agreed in double tax treaties entered into with the UK – see below). Remaining EU Member States could also tax EU parent companies on the receipt of dividends from UK subsidiaries.

Interest and Royalties Directive

The Interest and Royalties Directive provides for the elimination of withholding tax on intra-EU cross-border interest payments and royalties payments between 25% associates. 25% associates are companies where one company holds at least a 25% interest in the other company, or sister companies where a third company holds at least a 25% interest in each company. Following actual exit from the EU, remaining EU Member States would be able to charge withholding tax on interest and royalty payments to UK associate companies. The UK would be free to repeal domestic legislation implementing the Interest and Royalties Directive, but it is unclear whether it would choose to do so. If the UK repeals this legislation, outbound payments of interest and royalties would (subject to other exemptions, such as the Quoted Eurobond Exemption) attract UK withholding tax at the rates set out below in the table.

Double tax treaty withholding rates

The UK has entered into double tax treaties with each of the remaining EU Member States. (Double tax treaties stand separate from the EU treaties and so, without more, would remain in effect as currently.) However, not all of the treaties provide for the 0% withholding tax rate provided for by the Parent Subsidiary Directive and the Interest and Royalties Directive.

The rates are set out below. Where several rates are shown for a jurisdiction, the different rates will depend on the nature of the payment in question (for example, whether or not the dividend is funded by immoveable property income) and the nature of the recipient (for example, whether or not the recipient holds a significant interest in the payer). Please note that in several cases the lowest dividend withholding tax rate is only available to pension fund recipients.

It is also possible that some or all of these tax treaties will be amended as a result of the OECD BEPS project to include anti-treaty abuse provisions. Such provisions would restrict treaty benefits either to (i) persons falling within one of a set of tightly defined categories; or (ii) persons who do not fall foul of a purpose test.

COUNTRY	DIVIDENDS	INTEREST	ROYALTIES
Austria	5% / 15%	0%	0% / 10%
Belgium	0% / 10%	10%	0%
Bulgaria	0% / 5% / 15%	0% / 5%	5%
Croatia	0% / 5% / 10% / 15%	0% / 5%	5%
Cyprus	0%	10%	0% / 5%
Czech Republic	5% / 15%	0%	0% / 10%
Denmark	0% / 15%	0%	0%
Estonia	5% / 15%	10%*	5% / 10%
Finland	0%	0%	0%
France	0% / 15%	0%	0%
Germany	5% / 10% / 15%	0%	0%
Greece	No treaty rate. Domestic WHT = 10%	0%	0%
Hungary	0% / 10% / 15%	0%	0%
Ireland	0% / 15% / 15%	0%	0%
Italy	5% / 15%	0% / 10%	8%
Latvia	5% / 15%	10%	5% / 10%
Lithuania	5% / 15%	10%	5% / 10%
Luxembourg	5% / 15%	0%	5%
Malta	0%	10%	10%
Netherlands	0% / 10% / 15%	0%	0%
Poland	0% / 10%	0% / 5%	5%
Portugal	10% / 15%	10%	5%
Romania	10% / 15%	10%	10% / 15%
Slovakia	5% / 15%	0%	0% / 10%
Slovenia	0% / 15%	0% / 5%	5%
Spain	0% / 10% / 15%	0%	0%
Sweden	0% / 5% / 15%	0%*	0%

* Estonia and Sweden do not levy domestic withholding tax on interest payments.

State aid and taxation

EU competition rules on state aid generally prohibit any advantage granted by a Member State on a selective basis to an undertaking, category of undertakings or category of goods, where this could distort competition and affect trade between Member States (article 107 of the Treaty on the Functioning of the European Union (TFEU)).

Whilst Member States have sovereignty over their tax systems, each Member State must also comply with the state aid provisions in the TFEU. In the context of taxation, the European Commission has challenged legislative reliefs and discretionary rulings or settlements which favour particular undertakings or sectors. Recent examples include the European Commission's ongoing investigations into the transfer pricing rulings given by the Netherlands to Starbucks and Luxembourg to Fiat (amongst others).

If a Member State wants to provide state aid, it must apply to the European Commission for approval, although there are a number of circumstances in which the Commission's approval is not necessary. The EU permits *de minimis* aid (not more than €200,000 to an undertaking over three fiscal years). There are also block exemptions (under the General Block Exemption Regulation (GBER)) for certain categories of aid, where it is recognised that there is a market failure.

The UK's Enterprise Investment Scheme (EIS) and Venture Capital Trusts (VCT) scheme are examples of authorised state tax relief (from Income Tax and Capital Gains Tax) for private individuals to encourage investment in small & medium enterprises (SMEs). The GBER contains a number of conditions that the SME and the investor must meet in order for the tax relief to be exempted from state aid approval by the Commission. These conditions are reflected in the conditions for the tax relief under the UK's legislation. In the past, when the UK has wished to relax or amend the conditions under its domestic legislation, it has been required to obtain the Commission's prior approval.

Once the UK leaves the EU, it should have greater freedom to provide state aid (including in the form of tax incentives), although this will depend upon the exact model adopted by the UK. However, the UK has historically been a strong supporter of EU state aid rules, and still has its commitments under the OECD BEPS project to counter harmful tax competition, so it may be politically difficult for the UK to offer very generous tax breaks. Given that the UK's initial response to the Brexit vote has been to embark upon more aggressive tax competition (by announcing an intention to reduce the Corporation Tax rate), it will be interesting to see if the UK continues to be in the vanguard of BEPS implementation.

Norway model

- State aid rules are still relevant for EEA members by virtue of the EEA Agreement.
- EEA members must get prior permission from the EFTA Surveillance Authority for fiscal state aid that could distort the internal market.

Switzerland model

- Whilst Switzerland is not bound by the TFEU or the EEA Agreement, the FTA between Switzerland and the EU does contain a provision (article 23) which prohibits "public aid" that distorts the level playing field.
- However, this provision has proved problematic to interpret - Switzerland and the EU recently had a 6 year debate about whether the EU could challenge a Swiss tax regime for breaching the state aid provision in the FTA.
- There are also uncertainties about the exact consequences for Switzerland of a breach of article 23.

Canada- style FTA or WTO membership

- The UK would not be bound by EU state aid rules (but would not be able to complain about state aid provided by EU members to the detriment of UK businesses).

Customs Duty

Introduction

The UK is currently part of the EU's Customs Union. Customs duty (imposed on goods entering the EU and collected by the Member State of import) is imposed by directly effective EU legislation and the majority of revenue that the UK collects from customs duty is remitted to the EU. Following Brexit, the UK will need to implement its own legislation on customs duty, although the nature of this legislation, and the tariff rates, will depend upon the type of trade agreement that the UK negotiates with the EU and third countries.

Half of the UK's goods exports go to the EU, although the UK ran a trade deficit in goods of £88.7 billion with the EU in 2015, reflecting the fact that the UK economy relies heavily upon its services exports. However, businesses with complicated cross-EU product supply chains will need to start considering the impact that changes to import/export duties and, equally importantly, additional customs clearance procedures will have on their businesses. We have set out, in summary, the current position and the likely post-Brexit options for UK trade and customs tariffs.

The UK's current position: the EU Single Market and Customs Union

FREE TRADE

- No customs duties within the EU's customs territory and very limited non-tariff barriers (such as quotas).
- Goods originating in the EU can move between Member States without attracting customs duty/tariff or undergoing a customs clearance procedure. Free movement of goods, persons, services and capital.

CUSTOMS UNION

- Member States, including the UK, apply the EU's common external tariffs to imports from non-EU countries.
- The Council of the European Union decides the rate of the EU's common external tariffs. The actual tariff depends upon a number of factors, including:
  - the type of product and its value;
  - the country of origin - the tariff rates will depend upon whether the third country exporter has signed a free trade agreement with the EU or is a World Trade Organisation (WTO) member.
- In general, once the initial customs clearance procedure has been concluded in the Member State of import and the EU's external tariff paid, goods originating in third countries can be put into 'free circulation' - they can move between Member States without attracting further duty or undergoing further customs clearance procedures.

The EU's free trade agreements

The EU has negotiated over 30 free trade agreements with third countries, including Mexico and South Africa, which allow for lower or nil rates of customs duty. The EU has recently concluded negotiation of a free trade agreement with Canada (the EU-Canada FTA (CETA)), which is expected to be ratified in 2017 (although, in practice, the process of ratification in each EU Member State could take much longer). The EU is in negotiation with the United States for a free trade agreement (the TTIP), although this is proving politically controversial in many EU Member States and eventual agreement cannot be assumed.

Outside the EU, the UK will not only need to renegotiate its trading position with the EU, it will also lose the benefit of the tariffs negotiated under the EU's FTAs with third countries, so UK exports to these third countries could become more expensive. It will take the UK a significant time to renegotiate these free trade agreements, and it may not be able to secure such preferential tariff rates.

Options for the UK post-Brexit

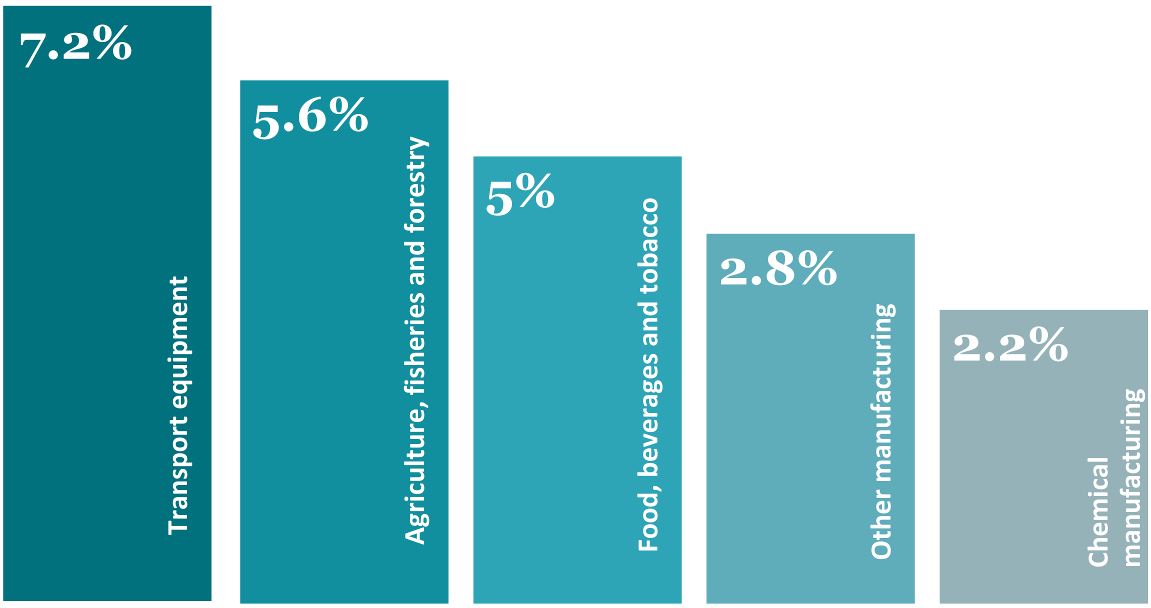
Rely upon trade under the World Trade Organisation rules – the WTO option

The UK (in its own right) and the EU are WTO members and have agreed an international binding framework for trade, including the General Agreement on Tariffs and Trade. The post-Brexit default option for the UK would be to rely upon the WTO rules, although there has been some debate about whether the UK could immediately start to trade under the WTO "most favoured nation" (**MFN**) tariffs without prior negotiation with the other WTO members, due to the UK sharing its WTO 'tariff schedules' with the EU. If the UK is unable to trade under MFN tariffs, the fall-back position would be to rely on the less advantageous tariffs that WTO members apply to imports from non-WTO members.

Broadly, unless WTO members agree preferential tariff rates under a free trade agreement or customs union, each WTO member must apply the same external tariffs (MFN tariffs) to imports from all other WTO members. As the UK would no longer be a member of the EU, the EU's common external tariffs would apply to UK exports to the EU, making it less attractive for EU companies and consumers to source goods from the UK. However, under the WTO's MFN rules, the EU could not penalise UK-source goods with higher tariffs than the EU applies to other WTO members. Therefore, if the UK does not agree a free trade agreement or customs union with the EU, its goods would be subject to the EU's MFN tariffs.

The EU's average external MFN tariff is **5.3%**, however, there are much higher tariffs for certain products, such as sugar and confectionary (over **20%**). The US's average external MFN tariff is **3.5%**.

Examples of the EU's average external MFN tariffs for different categories of product:



On the other hand, the UK would be free to set its own import tariffs on goods imported from other countries and keep all of the revenue generated. One of the main arguments put forward by the Leave campaign for Brexit was the ability of the UK to negotiate free trade agreements with, for instance, Commonwealth countries.

- If the UK wished to keep trade with the EU tariff-free, it would need to unilaterally lower the tariffs for other WTO members.
- Alternatively, the UK could impose tariffs on imports from the EU, which would make it more expensive for UK businesses and consumers who currently source goods from the EU.

Post-Brexit: other trading options

Unless some transitional agreement can be negotiated, the most likely short-term option for the UK will be to rely upon WTO rules. In the longer-term, the UK will likely look to agree preferential trade agreements with its main trading partners. Broadly, there are two types of preferential customs agreement in respect of trade in goods: a free trade agreement and a customs union.

- Countries which sign up to a free trade agreement agree to lower tariffs on trade in goods originating in those countries and the goods are subject to customs clearance procedures to prove the "country of origin" of the goods in order to obtain the preferential tariff rates. Each country maintains the flexibility to set its tariff rates with third countries.

- Countries in a customs union apply a common external tariff to imports from countries outside the customs union. However, the trade in goods within the customs union is tariff-free, regardless of the country of origin of those goods.

There has been much commentary about the different models that the UK could adopt post-Brexit and whilst these options are different in non-tax respects (such as in the level of contribution to the EU's budget and level of single market access for trade in services), from a customs duty perspective, the difference between them ultimately depends upon whether the option is a free trade agreement or a customs union.

The Norwegian option

(EEA EFTA)

- **EEA/EFTA membership:** tariff-free and quota-free trade on most goods between EEA members and the EU (subject to the "country of origin" rules - i.e. the goods need to originate in the EEA or the EU)
- Some EU MFN tariffs apply to agricultural and fisheries imports from EEA members
- Outside the EU's Customs Union
  - EEA members are free to set their own import tariffs, although EFTA has concluded FTA agreements with non-EU countries
  - Customs checks on goods imported from EEA members to the EU (and *vice versa*) to verify the country of origin of the goods and collect tariffs (where applicable)

The Swiss option

(EFTA but not EEA)

- **EFTA membership plus a series of bilateral free trade agreements:** tariff-free and quota-free trade on most goods between Switzerland and the EU (subject to the "country of origin" rules - i.e. the goods need to originate in Switzerland or the EU)
- Some EU MFN tariffs apply to agricultural imports from Switzerland
- Outside the EU's Customs Union
  - Switzerland is free to set its own import tariffs, although EFTA has concluded FTA agreements with non-EU countries
  - Customs checks on goods imported from Switzerland to the EU (and *vice versa*) to verify the country of origin of the goods and collect tariffs (where applicable)

The Turkish option

(Customs Union with EU)

- **Customs Union:** tariff-free and quota-free trade on certain goods between Turkey and the EU (regardless of their country of origin)
- Some EU MFN tariffs apply to agricultural imports
- Within the EU's Customs Union
  - Turkey must align its external tariffs with the EU's common external tariffs
  - Turkey is not party to the EU's FTAs with non-EU countries (so Turkey does not benefit from lower tariffs for "EU-origin" exports)
  - No customs checks on goods imported from Turkey into the EU (but certificates of origin required on import)

The Canadian option

(enhanced free trade

- **Bilateral free trade agreement:** tariff-free and quota-free trade on most goods between Canada and the EU (subject to the "country of origin" rules - i.e. the goods need to originate in Canada or the EU)
- Some EU MFN tariffs and quotas apply
  - e.g. cars exported from Canada to the EU will continue to attract tariffs (10%) until 2024
- No customs union
  - Customs checks on goods imported from Canada to the EU (and *vice versa*) to verify the country of origin of the goods and collect tariffs (where applicable)
- Canada is free to set its own import tariffs with non-EU countries

Employee Incentives and Brexit

- No immediate impact.
- Brexit unlikely to significantly affect incentive plans operated only within the UK and non-EEA countries (EU laws in the employee incentives field are generally uncontroversial).
- Brexit likely to have greatest impact on UK companies which extend their share incentive arrangements to the EEA. EU securities laws may require the publication of a prospectus when offering shares to EEA-based employees.
- Some changes will need to be made to National Insurance rules as EU social security laws currently protect the rights of individuals moving through member states.

Employee Incentives and Brexit: key legal issues

EU LAW	IMPACT ON EMPLOYEE INCENTIVES	BREXIT IMPACT
Employment Laws • Anti-discrimination • TUPE	• Identity of participants in incentive plans • Grant levels • Rights on termination of employment • Rights on business transfers	Unlikely to be any change to the basic principles. These rules are already incorporated within UK domestic law and accepted by employers and employees alike. Brexit would however mean that UK courts can make final decisions on areas of uncertainty (rather than the CJEU).
Securities laws • Prospectus Rules	• Offers of share based employee incentives to employees in the EEA	Could have a significant impact. Companies with shares listed on the LSE or headquartered in the UK currently benefit from an employee share schemes exemption from the need to publish a prospectus when offering share incentives in the EEA. If a prospectus is required this will create an additional administrative burden for companies.
Regulatory rules • Market Abuse Regulations (MAR) • CRD IV	• Dealing restrictions/notification of dealings • Bonus cap • Ratio of share based/cash based remuneration • Deferral • Malus and clawback	Might be changes to the bonus cap (the UK has been resistant to this from the outset). MAR will cease to have direct effect on Brexit but will have been in place for potentially 2 years so may become incorporated within domestic law. Other controls on executive pay are becoming more accepted and widespread so likely to remain.
Data Protection (EU's General Data Protection Regulation due to come into force in 2018)	• Holding/processing information about participants	Brexit will mean that it is not possible to export employee data from the EU to the UK unless the European Commission rules that the UK provides adequate levels of protection. Repeal or amendment of data protection laws unlikely as data protection laws are an international norm.
Consumer Credit	• Employee loans may need to be drafted as regulated agreements or fall within an exemption	Much of the EU consumer credit laws reflected existing UK law. The main changes were to restrict some of the UK's exemptions and introduce new forms for providing standard information.
National Insurance contributions (NICs)	• Aspects of NICs are governed by EU Treaty and EC Regulations • For non-EEA countries, the UK either has a reciprocal agreement or the "rest of the world" rules apply	Within the EEA a person is broadly subject to the social security system in the country in which they work apart from some exemptions (e.g. posted workers can remain insured within their home system for up to 2 years). Obligations exist for non-resident employers to apply host employer social security rules. With Brexit these would cease to apply.
State Aid rules	• Limits the scope of tax relief afforded under Enterprise Management Incentives	Unlikely to be any change although potentially would give UK scope to extend the scope of arrangements currently limited by State Aid rules

Employee Incentives and Brexit: practical issues

Will share based arrangements still be effective incentive tools during a down turn?

- Important for cash-poor companies
- Tax-advantaged plans remain attractive
- Numerical limits within tax-advantaged plans will go further with a lower share price
- Might the government promote the use of share incentives to retain talent within the UK?

Contacts:

Kathleen Russ
Partner, Head of Tax
E: kathleen.russ@traverssmith.com
T: +44 (0)20 7295 3230

Emily Clark
Partner, Tax
E: emily.clark@traverssmith.com
T: +44 (0)20 7295 3393

Jessica Kemp
Partner, Tax
E: jessica.kemp@traverssmith.com
T: +44 (0)20 7295 3040

Elena Rowlands
Partner, Tax
E: elena.rowlands@traverssmith.com
T: +44 (0)20 7295 3491

Simon Skinner
Partner, Tax
E: simon.skinner@traverssmith.com
T: +44 (0)20 7295 3242

Richard Stratton
Partner, Tax
E: richard.stratton@traverssmith.com
T: +44 (0)20 7295 3219

Russell Warren
Partner, Tax
E: russell.warren@traverssmith.com
T: +44 (0)20 7295 3227

Simon Yates
Partner, Tax
E: simon.yates@traverssmith.com
T: +44 (0)20 7295 3414

Mahesh Varia
Partner, Head of Employee Incentives
E: mahesh.varia@traverssmith.com
T: +44 (0)20 7295 3382

10 Snow Hill, London EC1A 2AL
T: +44 (0)20 7295 3000
F: +44 (0)20 7295 3500
www.traverssmith.com