CHANGING THE UK TAX LANDSCAPE

The recently filed Brexit application letter made it into the major news, and not only once. Highly complex items will need to be addressed, and discussions around the topic are everywhere, from the London tube to the pub of your choice. Far less within the public, but nonetheless of substantial importance, are the tax reforms the UK government has initiated to come into force over the next years, in particular for businesses with cross-border activities. Some of the changes are driven by the intention to increase competitiveness, others in response to international initiatives such as the programme against base erosion and profit shifting ("BEPS") shaped by the OECD. Probably most visible: A commitment to reduce the corporate income tax rate to 17% (just reduced from 20% to 19% as of 1 April 2017) by 2020. This rate reduction is tied together with an effort to increase attractiveness for R&D focussed businesses. A "patent box" had been introduced several years back already, but has now been renewed substantially due to increased substance and activity requirements set out by the OECD in the BEPS project. It offers tax benefits if intellectual property is held within the UK (rather than being put into an offshore jurisdiction). The major benefit is offered through a substantial tax rate reduction for profits that arise out of such intellectual property. It is now compliant with international standards agreed within the OECD, so it can be expected by businesses to be available in the future. Addressing the other side of the same coin, businesses are being charged with a so-called "diverted profits tax" if they operate through structures that can be viewed as intentionally avoiding a taxable presence in the UK. The goal of this tax, however, is less to gain additional tax revenue and more to increase transparency of cross-border value chains for UK tax authorities. Highly complex rules had also been introduced to deal with abusive tax structures, such as those that allow taking a deduction (e.g. for an interest expense) in two countries.

From a German viewpoint, other significant measures will appear very familiar to cross-border business – in particular, at least from a high-level point of view, the newly implemented rules that limit interest deductions: Interest in the amount of 30% of, broadly speaking, adjusted profits (so-called "taxable EBITDA") will be able to be taken into account, with various further thresholds and carry-forward rules being put into place, as well. This, again, follows the recommendation of the OECD project, which calls for countries to implement similar rules. Another shift will reform the treatment of tax losses and tax-loss carry-forwards that have been produced by loss-making entities in the UK. Whereas from a German viewpoint, the UK system has been very complicated and difficult to comprehend (as it focused on factors different to those of the German system), the new system should be more easily comparable. Now, losses may – if conditions are met – be considered throughout a corporate group. In addition, a minimum taxation rule has been introduced. Variants of both measures are found in the German system.

Further measures are being taken to deal with internal UK problems the government feels are best solved through the introduction of new taxes, such as the sugar tax, which will be levied – likely from 2018 onward – to increase the price of sugar-rich products, and thus contribute to mitigating troublesome health issues such as obesity.

That being said, another factor that will play a major role in the transition period to come should not be disregarded. The very likely loss of access to benefits from EU tax directives and the loss of eligibility with respect to German rules requiring "EU entity status" will create another area in which careful planning of UK-German cross-border activities from a tax perspective is required.

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