Keeping Up with Tax for Insurance

June 2022

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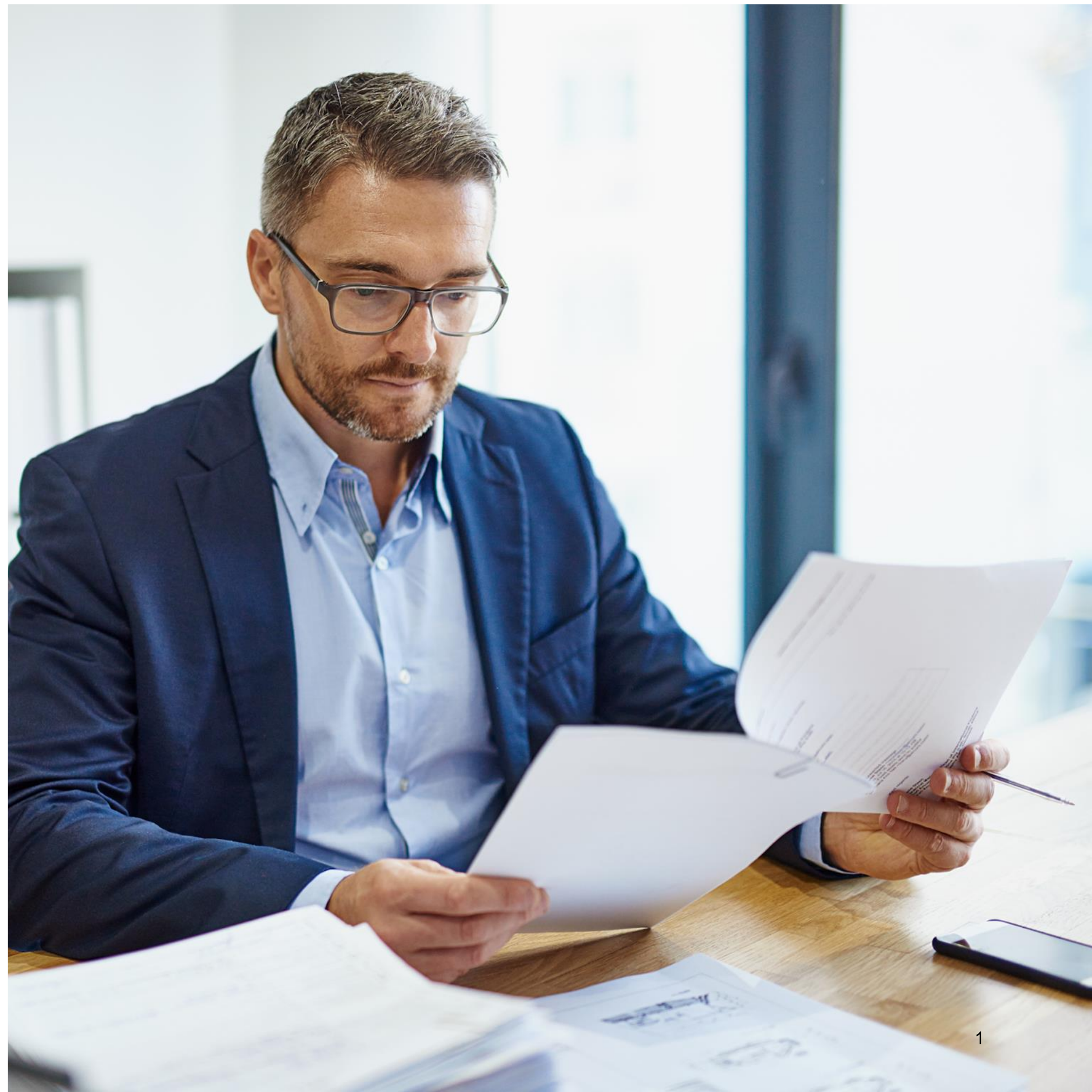

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Introduction

After a short hibernation, we are back and delighted to share with you another edition of Keeping Up with Tax for Insurance.

There have been a number of well trailed developments whilst we have been away. Our latest edition of **Talking Tax**, published 20 June, covers exactly how to get ready for Pillar 2, the impact Pillar 2 will have on deals, as well as how to enrich the wider tax accounting and compliance process and how to build Pillar 2 into technology planning.

As a latest update, **HM Treasury has confirmed** that the implementation of the UK's Pillar 2 rules will be pushed back, the rules will now first apply to accounting periods beginning on or after 31 December 2023. A formal response to the comments received during the consultation process will be provided in the summer, as will draft legislation. However, as detailed **here**, EU Finance Ministers have failed once again to reach a political agreement on the proposed EU Pillar 2 Directive.

We also hosted a **client webinar** on 24 June to outline some of the operational impacts that the Pillar 2 rules could have on your organisation and the steps you can take to manage the initial adoption and embed into business-as-usual. The recording can be found at the link provided.

In this month's edition, we have included the following articles:

- **Hybrid Disclosures – new requirements**
- **Withholding taxes and Pillar 2**
- **Temporary Customer Compliance Manager ('tCCM') scheme**
- **Short Term Business Visitors ('STBVs')**
- **General Court Decision on UK CFC State Aid**
- **Substantial Shareholding Exemption and Joint Ventures**
- **Introduction of a federal corporate tax in UAE**

I hope you enjoy the articles that we have put together, and as always please get in touch with me or your PwC team if there is anything that you would like to discuss further.

Andrew Rosam
Partner, Insurance Tax Market Leader

M: +44 (0)7718 339569
E: andrew.c.rosam@pwc.com

Hybrid Disclosures – new requirements

HMRC has recently added a **new page** to CT600B to Company Tax Returns, which requires disclosures in relation to the **Hybrid rules**.

We expect this to be a large additional burden for taxpayers. In particular groups will need to determine (and disclose) which UK entities within the group structure are hybrid entities, even if there are not any mismatches or counteractions.

Information required

There are ten questions on the **new form** which include whether the company is a hybrid entity, whether there are any transactions with hybrid entities in the same control group, whether there are any mismatches under Chapters 3, 6 and 8 (phrased as ‘mismatches’, not ‘counteractions’, meaning a mismatch under these chapters would need disclosing even if there was no counteraction), any counteraction under the hybrid rules, and claims/surrenders of dual inclusion income.

Timing

HMRC have confirmed that the updated CT600B is to be included with **all** returns submitted to HMRC for the first time from 6 April 2022. The additional disclosure is **not** required where a return submitted prior to 6 April 2022 is being amended.

Where tax return software has not been updated for the new form, then the form can be attached as a pdf to the filing (if possible) or the information included in a white space disclosure. Also where a company has filed a return since 6 April 2022 without this information, the return should be amended to include the information in a white space disclosure.

As you will note, the initial questions (B40 and B45) are required regardless of whether there is a counteraction under the hybrid rules. This means it will be important to consider whether there are any hybrid entities in the group, even if you are already comfortable that there are no mismatches under the rules.

We note for completeness that should your group not have any hybrid entities or mismatches (within the scope of the hybrid rules) then there is no requirement to complete this form (similar to the position with CFCs).

Should you wish to discuss the impact of these changes to your group please let us or your normal contact know.

Shyam Patel
Senior Manager

M: +44 (0)7483 362044
E: shyam.patel@pwc.com

Joel van Messel
Senior Associate

M: +44 (0)7483 435168
E: joel.van.messel@pwc.com

Withholding taxes and Pillar 2

The OECD's plans for a global minimum tax rate – known as Pillar 2 – represents a major challenge for multinational groups, but with the possibility of additional cash tax exposure, it can represent a good opportunity to look at and reimagine existing processes – especially if this can provide a Pillar 2 benefit.

The core of your top-up tax calculation is the proportion between your GloBE income (roughly based on your consolidated profit before tax) and your adjusted Covered Taxes. The specifics of the calculations are tricky – as much from a data availability perspective as a technical one – but picking each in turn there are actions you can take to streamline existing processes and potentially mitigate a top-up tax charge.

This article takes a closer look at one aspect of Covered Taxes – overseas withholding tax.

Withholding tax

The calculation of 'Covered Taxes' begins by considering the consolidated current tax expense accrued in the period with respect to covered taxes, including 'taxes recorded in the financial accounts of a Constituent Entity with respect to its income or profits…'. Withholding taxes recorded below the line under IAS12 should therefore meet the definition of a covered tax, and may provide a benefit in the top-up tax calculation by bolstering covered taxes.

This prompts the questions; how much withholding tax do I actually suffer, and how am I accounting for it?

Under general IFRS accounting principles, withholding taxes should be considered an income tax under IAS12 unless the withheld amount is in respect of a gross (revenue) balance, and the tax suffered is not creditable to the parent, at which point it may be more appropriate to record the income net in investment income. The base position of IFRS is to present income and expenses separately except when it reflects the 'substance of the transaction', when netting is an acceptable approach.

Therefore, where investment income is currently recorded net of overseas withholding taxes, withholding tax suffered on distributions may be eligible for inclusion within covered taxes by applying IAS12.

It's all in the data

The practical challenge is obtaining a split of gross income and withholding tax suffered, especially if that income is derived from fund structures, which can obfuscate the underlying distributions. Now that the presentation of withholding tax can have a material cash tax impact, it is worth considering how you might get that data, and whether it is preferable to report it under IAS12.

There is further merit in understanding the withholding taxes you suffer - the rate of withholding tax suffered may not be appropriate. The UK double tax treaty network allows for reductions in the standard rate of withholding tax you may suffer on investments, particularly for long-term business.

A review of your withholding tax position is worthwhile regardless of the risk and impact of Pillar 2 on your business; withholding taxes can be a cash cost for your business if incorrect rates are applied, and irrecoverable amounts can be included in your total tax contribution disclosure.

Michael Trigg
Director

M: +44 (0)7715 033786
E: michael.trigg@pwc.com

Stephen Kemp
Senior Manager

M: +44 (0)7483 456286
E: stephen.d.kemp@pwc.com

Temporary Customer Compliance Manager ('tCCM') scheme

Background

HMRC are trialing a new initiative to offer a number of medium sized taxpayers, those dealt with by HMRC's Mid Sized Business team, additional time limited support through the appointment of a temporary Customer Compliance Manager ("tCCM"). A small team of tCCMs will work alongside existing support offerings. The aim of the tCCM model is to provide additional one to one support to medium sized taxpayers who have extra tax complexity or are going through significant growth or key lifecycle events. Once allocated to the taxpayer, the tCCM will act as a nominated point of contact in HMRC. They will work alongside other HMRC tax specialists to progress and resolve any tax issues or queries that the taxpayer may have.

HMRC hopes that this increased level of support will improve the service provided to the taxpayers involved who need it most and support those taxpayers by helping to reduce error, by providing early certainty and ensuring the right response at the right time.

HMRC expects the length of time for tCCM support to differ depending on individual customer needs. A clear exit point will be agreed during the opening discussions with businesses and kept under regular review.

As the tCCM team is small, HMRC will need to prioritise allocation of its support and may not be able to provide a tCCM to every business who requests one. tCCMs will be allocated via:

- Direct requests from taxpayers or their agents;
- Internal referrals from HMRC case workers; and
- Proactively sourcing cases through data analysis to identify appropriate cases.

In essence the taxpayer will either be approached by HMRC and invited to join the scheme but in addition a taxpayer could apply to HMRC to be accepted into the scheme.

How the scheme initially operates

Once a taxpayer joins the scheme questionnaires are issued to the taxpayer and meetings scheduled which are focused on HMRC gaining an understanding of the businesses in question, their operations, how they make money and how this compares to their tax profiles. It is likely that in subsequent discussions once HMRC better understands the nature of the business that their focus would turn to specific issues as well as the governance, risk management and control environment. HMRC will want to learn as much as they can in the time the tCCM arrangement is in place to do a proper risk assessment in the widest sense. It will also be likely that discussions on areas of increased complexity can be expedited on a timely basis. Such areas could cover areas of long term disagreement, areas of increased complexity, and clearance that may be needed on a timely basis.

Why might a taxpayer opt to participate in the scheme?

One may ask the question why would a taxpayer decide to participate - there are a number of valid reasons including:

- Acceleration of long standing issues into HMRC lead initiatives such as accelerated resolution programmes with allocation of HMRC resource e.g. HRCP;
- Access to the Alternative Dispute Resolution mechanisms such as mediation;
- Management of boundary cases and access to Large Business specialists;
- Management of clearance processes; and
- Dealing with complex issues such as proactive disclosures, consequential claims and overpayment relief claims.

If any of the above factors are relevant to a taxpayer then they may consider joining the scheme if the option arises.

HMRC have also indicated that this service can be utilised where groups want to engage proactively with HMRC on the Uncertain Tax Treatment (UTT) regulations which apply to tax returns filed on or after 1 April 2022. This will be helpful to groups who fall within the UTT criteria but have not been allocated a CCM. Early engagement on this issue can help groups seek clarity on any uncertainties, engage with specialists and ultimately obtain a general exemption from the UTT notification if all necessary information is provided to HMRC in advance of the notification deadline.

What are the key points a taxpayer should consider ahead of accepting an invitation to join the scheme?

Ahead of accepting an invitation to join the scheme or applying to join the scheme a taxpayer should consider the following:

- Assess what are the pros and cons for them of joining the scheme;
- What steps should be taken to ensure the taxpayer makes the most of the arrangement;
- Assess its level of preparedness for the questions and reviews that are likely to follow;
- Does it want to have an increased level interest or intervention from HMRC; and
- Is it facing any issues that an increased level of focus and input from HMRC would assist in addressing.

Temporary Customer Compliance Manager ('tCCM') scheme (cont'd)

Key takeaways

Medium sized taxpayers should consider if it would benefit them to apply to join the scheme or if invited to join if they should accept that invitation. Key factors to consider include understanding HMRC's objectives for the scheme and would the taxpayer benefit from participating in the scheme. Those taxpayers who are most likely to benefit are those who are going through significant growth or have key life cycle events in their business, have complex tax issues to deal with, would benefit from additional focus or expertise from HMRC or have open enquiries or need to seek timely clearances on material transactions. Equally, taxpayers should consider the impacts of increased focus from HMRC for their business that may arise from participation in the scheme.

Emmet Bulman
Director

M: +44 (0)7483 417209
E: emmet.bulman@pwc.com

Short Term Business Visitors (‘STBVs’)

With pandemic related restrictions worldwide beginning to end and international borders reopening, attention is now beginning to turn to employment tax issues related to business travel.

From a UK perspective, this has been a common area of risk in HMRC Employer Duties enquiries for some time and we are aware that a number of employers have received a letter from HMRC recently reminding them of their compliance responsibilities and pointing out common pitfalls.

A distinction can typically be drawn between non-resident directors and the employed workforce as a whole.

For directors, most Double Tax Treaties (“DTT”) typically contain a director’s fee article which gives taxing rights to the country of residence of the company with which the individual holds office on directors fees and similar payments. Under UK domestic law, this tax is imposed to the extent that the individual performs their duties in the UK. Liability to social security will depend on the specific facts of the case (for example under the multi state working provisions in the social security coordination protocol adopted by the UK as part of the Trade and Cooperation Agreement with the EU). However, there is also a specific administrative concession for NIC for non-resident directors in the UK which can be in point if certain circumstances are met.

A different challenge lies where the director concerned holds an unremunerated UK directorship, whilst concurrently holding a remunerated employment or directorship overseas. HMRC may assert that the part of the global remuneration is, in reality, consideration for acting or being a director of the UK entity and should be taxed to the extent the individual works here. The strength of HMRC’s arguments here will rest on the specific circumstances. To mitigate the risk of this challenge, and the corollary risk that the home jurisdiction doesn’t allow Double Tax Relief, many employers ensure that there is a specific directors fee reflected in the total remuneration received.

For the rest of the non-resident employed workforce, there is a greater likelihood that the terms of a DTT will prevent the UK imposing taxing rights on the employees’ UK workdays. However, it is important to ensure that:

1. the UK business has an Appendix 4 (STBV) agreement in place with HMRC and is complying with the tracking, reporting and evidence gathering requirements contained in that agreement. In the absence of this, HMRC will assert that the terms are not met and technically, PAYE will apply irrespective of whether the Treaty offers exemption from UK income tax; and

2. any cases where the non-resident employee does not benefit from Treaty Relief (e.g. non Treaty travellers (such as those from Bermuda), employees of overseas branches or representative offices of UK companies, those who have breached 183 days over the relevant period or those economically employed in the UK) are identified and taxed as appropriate. In this regard, the simplified Appendix 8 payroll offers a number of benefits in terms of ease of administration and absolute tax cost.

Sam Moore
Director

M: +44 (0)7483 440171
E: sam.j.moore@pwc.com

General Court Decision on UK CFC State Aid

The General Court of the EU has dismissed both the UK and ITV plc’s applications made in respect of the European Commission’s UK Controlled Foreign Company State aid decision.

On 8 June 2022, the General Court of the European Union dismissed both cases (T-363/19 and T-456/19) in their entirety.

The facts of the case

In April 2019, the European Commission (“EC”) announced that it had found that the Group Financing Exemption (“GFE”) within the UK Controlled Foreign Company (CFC) rules constituted unlawful State aid in certain circumstances.

The UK CFC rules broadly allow the UK to tax the income of overseas subsidiaries controlled by a UK corporate parent where that income is regarded as artificially diverted from the UK.

The provisions in question, relating to the GFE, were introduced as part of the 2012 revision of the UK CFC rules and apply to offshore group financing arrangements with the result that, in certain circumstances, only 25% of the finance income is subject to a CFC charge (and in certain circumstances none at all).

The EC focused on the two ways in which income might be regarded as related to the UK:

1. Where loans are financed with funds or assets which derive from capital contributions from the UK.
2. Where activities relevant to managing the financing operations are located in the UK.

The EC considered that where the GFE provided an exemption for arrangements which fall into the first category above, this was justified since the exemption avoids a complex and burdensome intragroup tracing exercise.

However, where the GFE had been applied to arrangements in the second category, the EC considered that the exemption was not justified and instead constituted unlawful State aid.

The UK and a number of affected groups including ITV plc made applications to the General Court seeking to annul this decision.

As a result of UK amendments effective from 1 January 2019, the EC decision is only relevant to periods up to 2018.

The Judgment of the General Court of the EU

The General Court considered that the reference system was the CFC regime, rather than the UK corporation tax system as a whole. They concluded that the objective of the CFC regime was to tax profits which are regarded as having been artificially diverted from the UK. They further concluded that where any activities relevant to managing the financing activities are located in the UK, then the corresponding profits are, under the CFC rules, to be regarded as profits artificially diverted from the UK. As a result they ruled in favour of the EC and agreed that companies applying the GFE benefited from a selective advantage (to the extent that the relevant activities took place in the UK). The Court also dismissed the arguments made regarding justification, concerning administrative simplicity and compliance with the fundamental freedoms.

Key takeaway

It remains to be seen whether this decision is appealed to the Court of Justice of the EU. In the meantime, affected groups will also need to consider what further action if any to take regarding the ongoing domestic recovery proceedings.

Jonathan Hare
PwC UK

M: +44 (0)7740 968688
E: jonathan.hare@pwc.com

Mark Whitehouse
PwC UK

M: +44 (0)7715 705102
E: m.whitehouse@pwc.com

Peter Halford
PwC UK

M: +44 (0)7946 291684
E: peter.halford@pwc.com

Substantial Shareholding Exemption and Joint Ventures

The Substantial Shareholdings Exemption ("SSE") exempts from the charge to tax gains or losses accruing on the disposal by companies of shares where certain conditions are met.

We would like to provide here a refresh of a helpful update that HMRC made to react to certain consequences of the original legislation.

In brief

Where a group includes an investment of less than 50% in a joint venture company ("JV Co"), the activities of the JV Co can be treated as activities of the group, unless the JV Co is a member of the same group.

Revenue & Customs Brief 29/2011 (the "Brief") clarifies that where a group has an interest in a company that does not fall within the definition of a "joint venture company", rather than the investment automatically being treated as non-trading activity, whether that represents part of the group's overall trading activities or constitutes a separate investment activity will be a question of fact and depend on the circumstances of the case.

Where, for example, the effective management of the joint enterprise is closely integrated with that of the group and it conducts a trade that is similar to or complements that of the wider group, the investment can still be treated as trading activity of the group.

In detail

One of the conditions for the SSE to apply to a disposal of shares is that the company being sold must be a trading company or the holding company of a trading group/subgroup (paragraph 19(2) Schedule 7AC TCGA 1992).

Where a subgroup is being sold, if the subgroup includes an investment of less than 50% in a JV Co, provisions in para 23 allow the shareholding to be 'looked through' and the relevant percentage of the activities of the JV Co to be treated as activities of the subgroup.

However, there is an exclusion within para 23 that prevents this treatment if the JV Co is a member of the same worldwide group as the company being disposed of. The Brief (now incorporated in **CG53114** and **CG53116E**) was introduced to respond to certain unintended consequences of the legislation.

The Brief covers two scenarios:

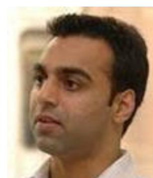
- Scenario #1 – Where a company has an investment in an entity that does not meet the definition of a qualifying joint venture company; and
- Scenario #2 – Where a company has an investment in a wholly owned entity that does not have ordinary share capital.

Before the Brief was issued there was always some doubt as to whether holding such investments should automatically be treated as a non-trading activity. The Brief confirmed that, with the right facts and circumstances, such an investment can be considered a good trading activity when assessing whether a group/sub-group/company is a trading group/trading sub-group/trading company.

In the situation where a valuable JV Co is 100% held within a group, say, 40% by subgroup A and 60% by subgroup B, there's always been doubt whether the SSE can apply when selling subgroup A. The issue arises because the value of the 40% interest in the JV Co could taint the trading status of the A subgroup if it is counted as a non-trading investment activity.

However, the Brief and **the amended online Guidance** explain that '*where, for example, the effective management of the joint enterprise is closely integrated with that of the group and it conducts a trade that is similar to or complements that of the wider group then that would suggest that the group's involvement in the enterprise does not represent a separate non-trading activity.*'

As such, provided that the JV Co is a trading entity and its activities are closely aligned to the activities of the main group, the investment in the JV Co should be able to be treated as good trading activity of the group.



Shezad Aleem
Director

M: +44 (0)7718 978976
E: shezad.aleem@pwc.com

Joel van Messel
Senior Associate

M: +44 (0)7483 435168
E: joel.van.messel@pwc.com

Introduction of a federal corporate tax in UAE

On 31 January 2022, the UAE Ministry of Finance ('MoF') announced the introduction of a federal corporate tax ('CT') in the UAE that will be effective for financial years starting on or after 1 June 2023.

The UAE CT regime will be based on international best practices, with a low / minimal compliance burden on businesses.

High level details on the proposed CT regime are set out in the **press release** and the **Frequently Asked Questions (FAQs)** published on the website of the MoF and the **Federal Tax Authority**. Further information is expected to be released by mid 2022.

In detail

Type of corporate tax system

The UAE CT system is expected to be a residence-based CT regime that taxes the worldwide profits of UAE resident businesses, and only the UAE-sourced business income of non-residents.

Where a business is resident for CT purposes would typically be determined based on the place of incorporation / registration (legal seat), or the place of effective management and control of the business.

Effective date

UAE CT will apply to financial periods beginning on or after 1 June 2023. As most businesses have a calendar financial year (1 January - 31 December), the majority of UAE businesses would become subject to UAE CT from 1 January 2024 onwards.

Tax rate

A statutory tax rate of 9% coupled with an exemption for qualifying dividends and capital gains and other measures to prevent double taxation are expected to be implemented. The UAE would have the lowest CT rate of all Middle East countries, with the exception of Bahrain which thus far has not announced any corporate tax regime changes in response to the call for a global minimum effective tax rate.

A 0% CT rate for taxable income up to AED 375,000 should apply for small & medium sized businesses, and start ups.

Takeaway

The introduction of a UAE CT regime should enable the UAE to adopt and implement the OECD BEPS 2.0 measures to address the tax challenges arising from the digitalisation of the global economy, and the introduction of a global minimum tax rate for large multinationals.

Whilst the press release and FAQs provide helpful information on the expected key features of the proposed UAE CT regime, further specifics and technical details will be needed for businesses to assess the impact and their readiness for the new UAE CT regime.

We understand that further information is expected to be made available by mid 2022, which would give UAE businesses at least 12 months to get ready.

Next steps

The introduction of UAE CT will have an impact on the tax and compliance costs of most UAE businesses. Businesses will require clear identification of the tax implications and available optimisation / mitigation strategies, and any required changes to their corporate structure, operating model(s), finance / tax function, reporting systems, legal agreements, and TP policies to ensure compliance with the new UAE CT regime.

It is important that businesses evaluate the impact of the introduction of UAE CT early on and proactively plan for a smooth implementation.

Andrew Rosam
Partner, Insurance Tax Market Leader

M: +44 (0)7718 339569
E: andrew.c.rosam@pwc.com

Contacts

For additional information please contact

Stuart Higgins
Partner, UK Tax Clients and Markets Leader
M: +44 (0)7725 828833
E: stuart.higgins@pwc.com

Andrew Rosam
Partner, Insurance Tax Market Leader
M: +44 (0)7718 339569
E: andrew.c.rosam@pwc.com

Jonathan Howe
Partner
M: +44 (0)2072 125507
E: jonathan.p.howe@pwc.com

Rob Gooding
Partner
M: +44 (0)7815 643891
E: robert.gooding@pwc.com

Susie Holmes
Partner
M: +44 (0)7841 561428
E: susie.holmes@pwc.com

Richard Mander
Director
M: +44 (0)7740 242198
E: richard.c.mander@pwc.com

Katharine Adlard
Director
M: +44 (0)7725 706688
E: katharine.s.adlard@pwc.com

Mike Trigg
Director
M: +44 (0)7715 033786
E: michael.trigg@pwc.com

Stephen Kemp
Senior Manager, Editor
M: +44 (0)7483 456286
E: stephen.d.kemp@pwc.com

Colin Graham
Partner – Global Financial Services Tax Leader
M: +44 (0)7764 132271
E: colin.graham@pwc.com

Ben Flockton
Partner
M: +44 (0)7968 241792
E: benjamin.flockton@pwc.com

Hazell Hallam
Partner
M: +44 (0)7711 562076
E: hazell.hallam@pwc.com

Lindsay Hayward
Partner
M: +44 (0)7702 678458
E: lindsay.hayward@pwc.com

Brent Hadley
Director
M:+44 (0)7730 147650
E: brent.c.hadley@pwc.com

Sharon Blain
Director
M: +44 (0)7590 352384
E: sharon.blain@pwc.com

Andrew Molloy
Director
M: +44 (0) 7808 105921
E: andrew.b.molloy@pwc.com

Sarah Robinson
Director
M: +44 (0)7715 034006
E: sarah.robinson@pwc.com

Joel van Messel
Senior Associate, Editor
M: +44 (0)7483 365546
E: joel.van.messel@pwc.com

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