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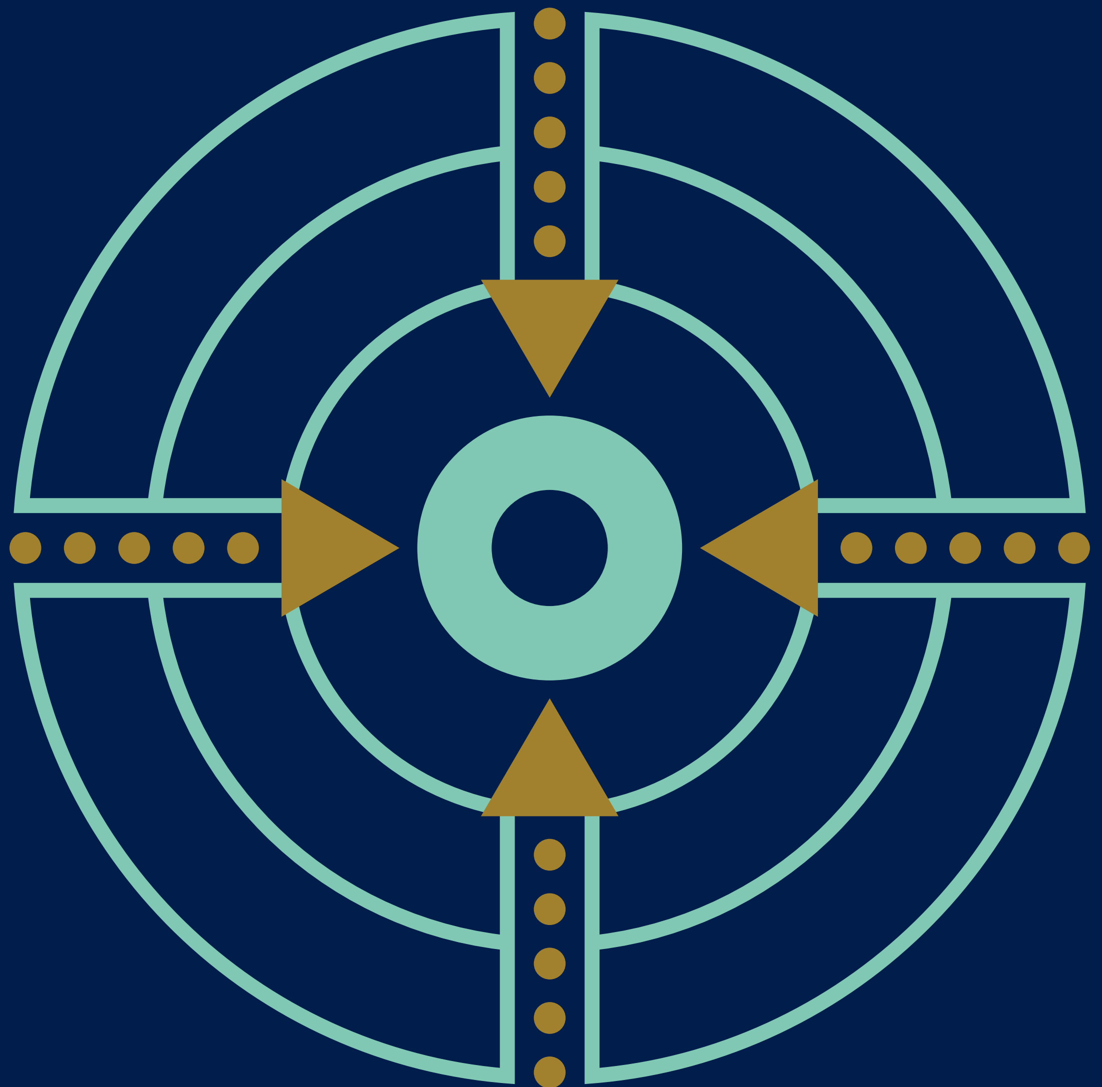
Asset Manager Tax Checklist

What should be on your radar?

October 2020



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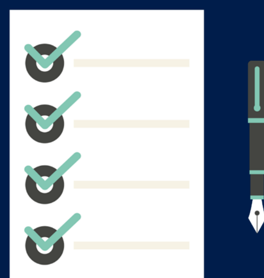
Introduction

Whilst the Covid-19 pandemic and continuing uncertainty over the nature of the UK's relationship with the EU post-Brexit have dominated the political and economic agenda in recent times, there have been a number of important tax developments that asset managers should have on their radar as we approach the end of 2020.

This briefing includes a checklist of the key tax issues that asset managers should be aware of, including both finalised changes as well as potentially significant future developments. We have also set out the actions (including some less obvious ones) that asset managers should now be undertaking in preparation.

How we can help

We advise on all tax aspects of asset management and investment funds. We are currently assisting clients with many of the matters identified in this checklist, and through our membership of industry bodies, are involved in the various consultations highlighted.



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Hot topics

Tax change	Introduction	What does this mean for asset managers?
DAC 6	EU directive 2018/822 (DAC 6) introduces a new tax reporting regime in the UK which came into force on 1 July 2020. These rules catch "cross-border" transactions which satisfy certain "hallmarks". The rules aim to ensure that tax authorities across the EU receive information about matters which may involve tax planning at an early stage, to enable swift challenges or changes to the law to counteract aggressive planning. The hallmarks are, however, widely drafted and are likely to capture certain transactions which do not have a tax avoidance motive, and so will need to be carefully considered in all transactions with a "cross-border" element.	In time for the first reporting dates asset managers should be reviewing all arrangements that have been implemented since 25 June 2018 and assessing whether disclosure is required. If it is, they should consider whether any other party to the arrangement may have a disclosure obligation and consider co-ordinating with them. For future transactions, asset managers should put processes in place to identify and report relevant transactions and communicate these internally. When dealing with third parties, asset managers should consider what (if any) DAC 6 related arrangements they want to make (e.g. in relation to co-ordinating reporting) and ensure that appropriate provisions are included in the relevant documentation.
Off-payroll working rules	New rules relating to off-payroll working come into effect from 6 April 2021 and will apply to medium and large clients in the private sector that have a UK connection. The new rules will affect fee payments made in respect of workers who provide their services through intermediaries such as personal service companies (PSCs). Asset managers engaging such intermediaries will need to decide whether, if the existence of the intermediary were ignored, the worker would be regarded as their direct employee (or office holder) for income tax purposes. If they would, then the client (or the agency paying the intermediary if different) must deduct income tax and NICs from the fees paid to the intermediary and account for employers' NICs (and apprenticeship levy if relevant) as if the fees were payments of salary.	Those in the asset management sector engaging workers through PSCs should be assessing which of these engagements they will have in place as at 6 April 2021. Such firms then need to ensure that contracts governing these engagements provide for the new rules. For example, they should enable tax and NICs to be deducted from payments, (where possible) permit a re-pricing of the arrangement to take account of the additional costs to the firm (such as employers' NICs charges and apprenticeship levy) and contain appropriate indemnities. Firms also need to put in place internal processes for making decisions about whether the new rules apply, issuing "status determination statements" and operating payroll on payments within the rules. The legislation prescribes a disagreement process which firms must follow if the worker or agency challenges its decision on status. Firms should review existing engagements that will continue beyond 6 April 2021 to see whether they come within the new rules. If they take on new workers and think the contract will extend beyond 6 April 2021, firms need to ensure that the contract takes the changes into account. For more information on whether the new rules will apply to you and what needs to be done under them please click here and here.

Social Security for internationally mobile workers from 1 January 2021

There are rules in place for countries in the European Economic Area (EEA) and Switzerland which seek to ensure that social security contributions in respect of an individual are only paid in one country. An aspect of this is that where workers are temporarily assigned from one country to another, contributions should only be payable in the worker's home country for the first two years, provided the relevant conditions are met.

If the UK leaves the EU without an agreement on the issue, social security contributions will potentially be payable both in the UK and the EEA (and Switzerland) unless the UK has entered into an agreement with the other jurisdiction.

Employers should be prepared for a no-deal scenario and should assess their internationally mobile workforce to identify relevant international assignments (as well as those working in different jurisdictions due to Covid-19) and ask the local social security authorities whether the existing rules (and existing Certificates of Coverage) will continue to apply to current assignments between the UK and that country. In addition, employers should consider how to structure new assignments taking place after 1 January 2021.

Employers should get in touch with employees who are likely to be affected by any of the changes and consider who will bear the costs of any increased social security charges and how this might affect any tax equalisation agreements that they currently have in place.

For more on social security and Brexit please click here.

Company residence and permanent establishment in light of Covid-19 travel restrictions

Travel restrictions caused by the Covid-19 pandemic have led to difficulties for directors, who are not tax resident in the same jurisdiction as their company, physically attending board meetings in the company's jurisdiction. If such directors attend remotely or, in the absence of board meetings, make important decisions where they are located, there is a risk that the company could be considered resident where the relevant directors are located.

Similarly, where travel restrictions lead to directors and employees who normally work in one jurisdiction having, instead, to work in another, this can give rise to concerns that the presence of the individual gives rise to a taxable permanent establishment of the company in that other jurisdiction.

Although some jurisdictions have given express comfort that presence in a state caused by Covid-19 travel restrictions will be disregarded for corporate tax purposes, others (including the UK) have, in effect, taken the view that the normal rules should apply but that, in practice, it is likely to be possible to get comfortable that the temporary presence of individuals in the "wrong" jurisdiction should not, under those rules, cause residency or permanent establishment concerns.

As the "temporary" travel restrictions become longer term, it may become difficult for companies to get comfortable on these issues.

Post-Covid 19, workers may want to remain in their home jurisdictions, in which case companies will not be able to rely on any Covid-19 related comfort given by jurisdictions.

Changing corporate tax residence or creating a permanent establishment can have a significant tax impact.

Asset Managers should monitor the situation carefully and consider taking appropriate steps, for example, appointing new directors resident in company's intended jurisdiction of residence and providing directors and employees with clear policies of what actions they can take and decisions they can make from their home jurisdictions without generating corporate residence or permanent establishment concerns.

Covid-19 travel restrictions – tax issues for individuals

The increasing length of time for which many travel restrictions have been in place due to Covid-19 is generating various tax concerns for individuals and their employers, including that employees will become tax resident in the country in which they are "temporarily" located (e.g. if they have stayed with family during the pandemic, the country in which their family is located). Residence tests in many jurisdictions are linked to time spent in those jurisdictions. Some jurisdictions (including the UK) have introduced relaxations to their usual rules but these relaxations may be time limited.

Asset managers should review the position of their team members and consider the extent to which their working arrangements could trigger tax obligations in the jurisdictions in which the individuals are located. Contractual provisions should also be reviewed to establish who bears the cost of any increased tax burden.

Blackrock VAT decision

The width of the VAT exemption for "management" of investment funds was recently considered by the Court of Justice of the European Union (CJEU) in case of Blackrock Investment Management.

The exemption only applies to management of certain types of fund (special investment funds (SIFs)). Blackrock had been arguing that a supply of a management platform that had been used for both SIFs and non-SIFs should be treated as within the exemption insofar as the supply related to SIFs. However, the CJEU disagreed.

There is concern that the CJEU decision may have indicated that for a service to constitute "management" it must be of a type that can only be made to SIFs. This would narrow the scope of the exemption a great deal as most management services can be provided to all types of fund (e.g. investment advice). We do not think that the exemption should be interpreted in that way but the position is not free from doubt.

Where supplies of potential "management" services are made to SIFs and non-SIFs, the parties should consider the arrangements and the extent to which they can legally and economically separate the services relating to SIFs from those relating to non-SIFs (e.g. through separate contractual and billing arrangements).

Such an approach will not help address the concern raised by the case that the exemption is limited to services that can only be made to SIFs. On that point, asset managers will want to see how the industry reacts to the decision, whether the CJEU takes a similar approach to Blackrock in the upcoming fund management exemption case of DBKAG and what emerges in relation to the issue from the expected Government review of the VAT treatment of fund management fees (discussed further below).

Increased VAT recovery for supplies to EU members states

Currently input tax associated with most VAT exempt supplies of financial services can be recovered where the supply is made to a person belonging outside the EU. Relevant exempt supplies include making loans and transferring shares but do not include exempt fund management.

It is expected that after the end of the Brexit transition period, (due to be 31 December 2020) this ability to recover input VAT will be extended so that it applies to supplies made to persons belonging outside the UK (i.e. it will apply also to supplies to the EU).

Asset managers should consider the extent to which they and the funds they manage will be able to, from I January 2021, recover increased amounts of input VAT on supplies to the EU.

What to look out for in the future – macro changes

Tax change	Introduction	What does this mean for asset managers?
Introduction of revenue raising measures in response to Covid-19	The UK Government's response to Covid-19 is likely to include tax increases and there has been a lot of speculation about what measures may be introduced. Perhaps the most likely is a change in the tax treatment of the self-employed as the Chancellor alluded to this in his announcement of the Self-Employment Support Scheme. This would likely be in the form of paying NICs at a rate more equal to employees. Other areas of speculation have included increasing the rates of capital gains tax to the income tax levels, increasing corporation tax and introducing a new net wealth tax.	With the Autumn Budget cancelled it seems unlikely (but not impossible) that any major proposals will be announced this year but tax increases are probably not too far away. Businesses should monitor the position going forward.
OECD Pillar One and Two	Building on its original BEPS project, the OECD is working on two proposals that could have huge consequences for international taxation. "Pillar One" seeks to introduce a new taxing right for countries in relation to non-resident companies that do not have a permanent establishment there and "Pillar Two" seeks to introduce a global minimum tax rate. Pillar One is aimed at "consumer" facing businesses and those providing automated digital services so it is hoped and expected that alternative investment funds and their managers will not be within scope. The asset management sector will not want Pillar Two to cut across national regimes designed to ensure that fund structures are tax neutral. Both pillars have an ambitious timeline of reaching consensus by mid-2021.	Asset managers should monitor the progress of these projects. Even if consensus is reached by mid-2021, the timetable for implementation is unclear and we would expect it to take at least two to three further years for reforms as fundamental as those being considered to be implemented internationally.
CGT review	In July the Office of Tax Simplification launched a call for evidence for a review of capital gains tax (CGT). The review is to develop recommendations for simplification including reducing distortions from both an administrative and technical standpoint. Whether the review is a precursor to the introduction of revenue raising measures to fund the Government's Covid-19-related expenditure is currently unclear. However, asset managers will be very interested in the scope of any resultant changes to CGT.	Asset managers should monitor this issue. Those wishing to provide comments must act soon as the call for evidence closes on 9 November.

What to look out for in the future – specific issues

Tax change	Introduction	What does this mean for asset managers?
Changes to the UK's "hybrid" anti-avoidance rules	The Government recently consulted on three particular problem areas with the UK's "hybrid" anti-avoidance rules. For more information please click here.	The consultation closed on 29 August 2020 and the Government is currently considering its responses. Asset managers should monitor the situation. The impact will depend on how (if at all) the hybrid rules are amended. Ideally the changes would be included in the next Finance Act and have effect from April 2021. However, with the cancellation of the Autumn Budget and the Government's attention likely to be focused on Covid-19 and-Brexit related issues in the near future, this may be too much to hope for.
Tax treatment of Asset Holding Companies	The Government recently consulted on how to make the UK a more favourable location for asset holding companies in alternative fund structures.	The consultation closed on 19 August 2020 and the Government is currently considering the responses. Again, asset managers should monitor the situation.
VAT treatment of fund management fees	The Government announced in the 2020 March Budget a review of the VAT treatment of fund management fees. Whilst no details have been announced, the current scope of the VAT exemption for fund management services is unclear. Brexit should provide the UK with the opportunity to consider this area afresh, allowing it to adopt a more coherent approach than its European competitors, and it is hoped that this is what the fund review will address. (See also "Blackrock VAT decision" above).	The review has been delayed due to Covid-19 so the start of the review is something to look out for as we expect that it will involve a process of consultation with the asset management industry.
Call for evidence on VAT grouping	HM Treasury has issued a call for evidence relating to VAT grouping. The review includes views on potential changes to the current rules which would, if adopted, significantly recast the UK's VAT grouping framework. Of particular interest to asset managers will be the review of VAT grouping rules for limited partnerships and the impact of any changes to the VAT treatment of management fees.	Asset managers will want to track the development of this issue. Those wishing to provide comments must act soon as responses must be provided before 20 November 2020.
Economic crime levy	The Government is planning to introduce a levy (from the AML regulated sector) to fund combatting economic crime. If introduced it is likely to apply to many within the asset management sector including portfolio managers, collective investment undertakings and investment advisers. The government intends for the first set of levy payments to be made in the Financial Year 2022/23. However, this timeline is subject to the findings of the consultation it launched on the levy.	The HM Treasury consultation on the design of the levy closed on 14 October 2020 and asset managers should monitor this issue.