Finding your way

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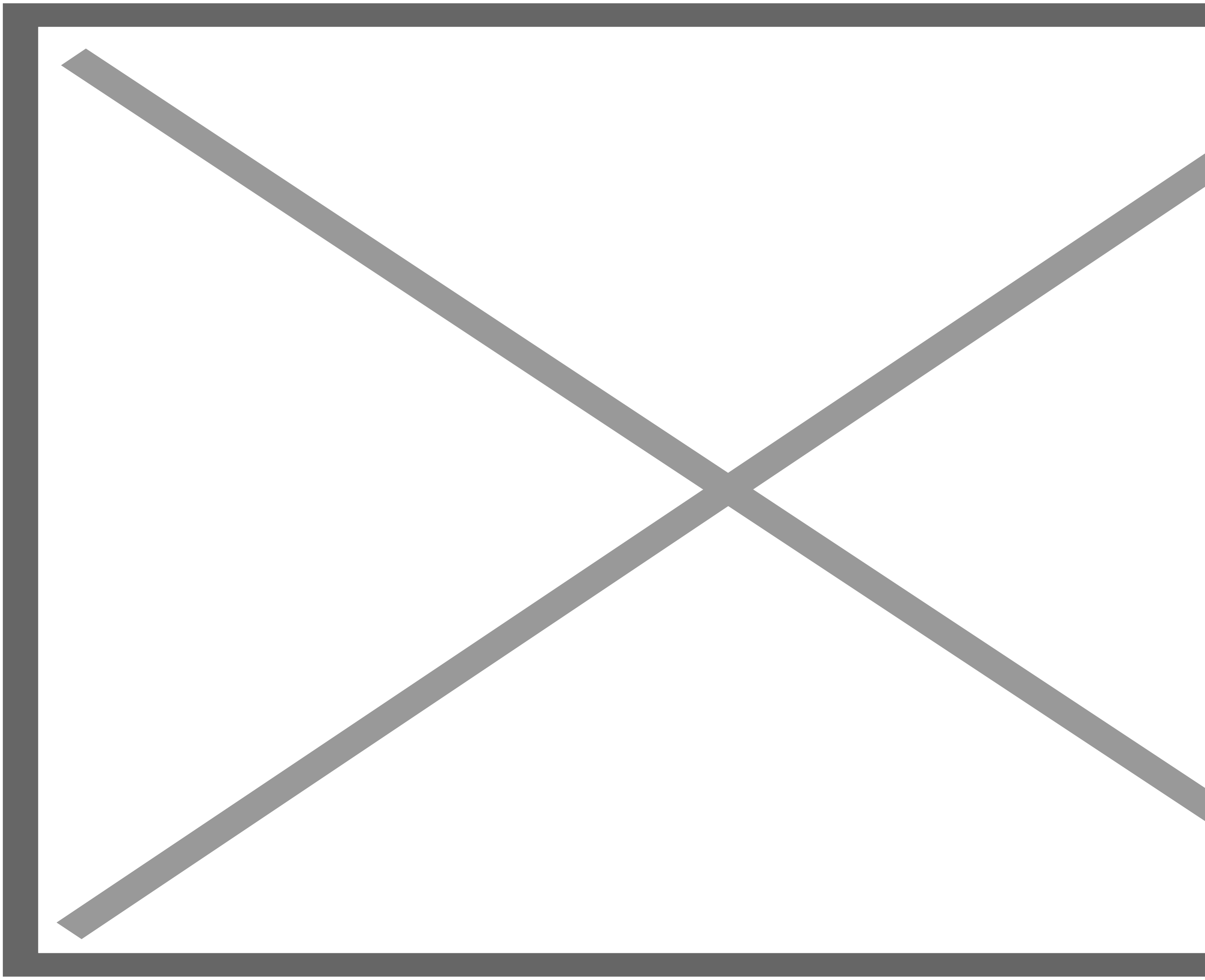

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Panny Loucas and *Matthew Clark* consider some ‘no regret’ actions businesses should be taking, no matter the outcome of the Brexit negotiations

Key Points

What is the issue?

It is critical to understand that no business has the full Brexit picture but certain scenarios are emerging and decisions have to be made.

What does it mean to me?

The continuing political uncertainty has heightened the risk of no deal and as a consequence many more businesses have begun to realise that it is time to act and in particular the importance of taking ‘No Regret’ actions to assess the effects of Brexit on them.

What can I take away?

There are a number of key actions businesses have and should be taking in order to put themselves in a position to address the main tax-related challenges facing them. These are principally in relation to trading arrangements and workforce, but are by no means limited to these areas.

The refrain from many businesses in relation to Brexit has been that there is no point in planning because the landscape remains too unclear. It is also certainly true that the status of the Brexit negotiations at the time of writing this article may well have significantly altered in the short time that elapses before it is read.

However none of that lessens the importance of being prepared for Brexit. The financial services industry and the pharmaceutical sector have been the prime movers in this regard, primarily driven by regulatory issues. But in the second half of 2018 as the clock has been counting down to 11pm on 29 March 2019, many more businesses have been looking to prepare as best they can.

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A quick recap on the most likely outcome of the negotiations between the UK and the EU27 is important to understand what the key issues confronting business are.

Although one can feel as if there are myriad of options in terms of what the post Brexit world will look like, in fact these can be boiled down into three main possible scenarios:

- no deal
- a low alignment deal, and
- a high alignment deal.

A low alignment deal and no deal are very similar in most practical terms, as will be explained below. An example of a ‘high alignment deal’ is the one outlined in the Chequers Agreement and set out in detail in the White Paper issued in July 2018 ‘The Future Relationship between the United Kingdom and the European Union’. This involves the UK in all but name staying in the customs union and single market for goods, but with restrictions on market access for services and free movement of people.

A low alignment deal would be one that builds upon the EU-Canada Free Trade Agreement (CETA), with the UK leaving the customs union and single market, with the introduction of customs, rules of origin, significantly reduced market access for services and the end of free movement of people. As noted above, this from a planning perspective is very similar to a ‘No Deal’ scenario – certainly from a physical trade perspective, as it will require businesses to prepare and implement all the compliance processes to trade across an international border with the EU. We believe it is critical to understand that no business has the full Brexit picture but certain scenarios are emerging and decisions have to be made. Time is limited to effect change, even when focussing on the main business areas likely to be affected: trade and customs (supply chain), people and immigration and regulation and legal. As such, the greater the operational and regulatory complexity in a business, the more urgent it is to take action now.

The other crucial thing for businesses to understand is that even if there is a ‘high alignment’ deal the pre and post business landscape is likely to have changed significantly.

Despite the close alignment in terms of goods that this brings, the UK would still need to seek new arrangements with the 50 plus countries with which the EU has FTAs. And the current position in terms of access to EU/EEA workers and the single market for services will be fundamentally altered. This is because even a high alignment deal is unlikely to cover services in any significant way or grant the same level of free movement of people – as demonstrated by the Chequers proposals. Therefore for those businesses whose main provision is of cross-border services or whose business combines the provisions of goods and services cross-border (e.g. complex equipment which requires installation and/or servicing) things may change significantly.

The continuing political uncertainty has heightened the risk of no deal and as a consequence many more businesses have begun to realise that it is time to act and in particular the importance of taking ‘no regret’ actions to assess the effects of Brexit.

So what are businesses actually doing? These actions are summarised below, all of which we think are key to undertake as soon as practical given the lead time that may be needed to address any issues they bring to light.

Action 1: Clean up data

Whatever the border looks like, data will be key, and will become even more critical if we’re successful in creating innovative solutions for enhanced data sharing and risk profiling to enable the faster movement of goods across the new international border. Investing in clean, well-classified customs data for goods traded with the EU27 today is a prudent first step in preparing for change at the border.

Given that businesses will classify these goods for current VAT intrastat reporting, there is a good starting point to build upon, by enhancing that classification from eight numerical digits to 10 numerical digits fit for a customs declaration. So it’s a good time for businesses to review and ensure their goods data is accurate, appropriately classified and stored now, to make the process simpler from day one.

Action 2: Build ways to capture more data

It’s probable that trade with the EU27 will require declaration of additional data for the processing of customs clearances. In addition to checking existing master data, businesses should plan to capture the customs origin and value of products to take advantage of any Free Trade Agreement we move to with the EU. Systems and process changes take time to implement and embed, and will also have to adapt to accommodate VAT as well as customs duty changes. So, understanding the as-is and planning future systems now means a business will be better positioned to meet the new border requirements.

Action 3: Know supply chains

Businesses should focus on all their UK inbound and outbound movements. They should review their current global movements to and from the UK. Each business needs to understand if they are benefiting from any current Free Trade Agreements, Tariff Suspensions etc. to import or export physical goods (materials, parts and finished goods) with a lower customs duty rate than usual. This is because it is possible that access will be lost to some or all of these agreements for a period of time after Brexit until the UK can enter into its own Free Trade Agreements. In terms of current UK to EU supply chains, each business should model their customs duty, import VAT cashflow and admin charges. Intrastat data can be used as a starting point for this modelling. This will highlight which supply chains are most at risk from either an increase in cost or lead times. This enables a business to identify quickly which supply chains it should prioritise and take action on in the first instance.

Action 4: Take advantage of 'special procedures' where available

Businesses should prepare to apply for the tax approvals that they will need to trade across the international border with the EU27 on day 1, i.e. an EORI (importer of record account) without which it is impossible to import or export from the UK, a duty deferment account to delay the payment of border taxes otherwise cash is required immediately upon the import of goods.

In addition to these basic approvals businesses should take advantage of existing government simplifications to mitigate the cost of Brexit. HM Revenue & Customs approvals designed to support importers and exporters trading outside the EU have historically offered little upside for those trading within the EU. However, post-Brexit, such approvals will be available to all businesses who will then be trading internationally.

Special procedures like Authorised Economic Operator (AEO) should offer the chance of a competitive advantage for a more efficient border clearance, regardless of how the border is managed. The more traditional special procedures like customs warehousing and inward processing could offer competitive advantages by eliminating the potential double customs duty costs dependent on a business's supply chain model. As government resources to manage applications are currently scarce and the process can take months, businesses should be performing an analysis without delay on their need for such procedures and how to put them in place quickly.

Action 5: Review tax structure

It is important for businesses to undertake a wider tax review of their group structure in the EU to be determined whether it is optimal for a post Brexit environment. This should encompass not only customs and VAT implications of the structure (which would complement action 3 above) in terms of which group companies import or export; but also the funds flows in terms of dividends, interest and royalties and whether there is reliance on EU directives in terms of withholding tax mitigation. It will also be important to review the impact of Brexit on the transfer pricing methodology used, given that payment for royalties, intellectual property rights and management fees may be linked to UK to EU supply chains which will have an impact on the customs value of declared goods.

Aligned to tax are the following important additional actions to prepare businesses.

Action 6: Review the workforce composition

It is key for a business to understand the mixture of UK and EU/EEA nationals which make up its workforce – and then to determine how dependent the future conduct of the business is on access to EU/EEA citizens. Businesses need to take time to understand how those people may be affected by Brexit. What is their residency status and how might that change after Brexit? Can they safeguard their position by evidencing their exercise of treaty rights? What will their cross-border social security position be post Brexit? A number of businesses have seen the importance of communicating clearly with their workforce what the businesses strategy is in terms of dealing with the uncertainties of Brexit for their people.

Action 7: Communicate with business partners

No business should underestimate the importance of speaking with their customers, suppliers, third party logistics/customs clearance agents and banks. In fact any type of partner integral to the business.

A business should do this to confirm that their key partners can continue to provide their services on the scale which the business will need post Brexit. These partners should be included in the business's Brexit planning to ensure there is a meeting of minds as to how they and the business will both engage post Brexit. Working with business partners in advance to avoid unwelcome surprises will be key. If these partners have limited resources to support the business, there is a first mover advantage in securing services before competitors can do so.

Action 8: Review legal contracts

It will be important to identify any contract terms that could frustrate the operation of business post Brexit, such as terms which make no sense or are difficult to interpret post Brexit, fulfillment deadlines which may become difficult to satisfy in the short term after Brexit, applicable law of the contract. There may be a number of terms in a business's legal contracts that need to re-negotiated and updated before 29 March 2019.

Undertaking these steps have confirmed for some that the implications of Brexit are not substantial to their business and that only minor further actions are needed. However for others they have been just the beginning of the story as they have revealed that significant further action will be required in order to enable the business to deal with the likely impact of Brexit. As in most business situations, preparedness is key. It is those businesses that are most prepared that are likely not merely to deal most successfully with Brexit but also to spot opportunities in the likely changes ahead more readily than their less prepared competitors.

A final message is to please take action now. Remember timing and resource is key and the longer a business leaves its Brexit preparations, the less time it will have to enable all of its business partners to ensure they can keep trading with the business on same basis and the less time this gives HMRC or EU Customs/VAT Authorities to provide the business with the tax approvals it may need.

The question posed to those running a business is: 'How will I respond to my Board or Shareholders if they ask me to confirm that I do not believe that there will be any adverse implications from Brexit for the business or that I have a plan in place to minimise the impact of any such implications?'