Tax Topics

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Wolters Kluwer

FOCUS ON CURRENT CASES

This is a regular monthly feature examining recent cases of special interest, coordinated by Tony Schweitzer and Gergely Hegedus of Dentons Canada LLP. The contributors to this feature are from Dentons Canada LLP, Montréal, Toronto, Calgary, Edmonton, and Vancouver.

Dow Chemical Canada ULC v. Canada, 2024 DTC 5098 (Supreme Court of Canada) — Supreme Court of Canada Finds That Ministerial Decisions Under Subsection 247(10) of the ITA Belong to the Jurisdiction of the Federal Court

Background

Dow Chemical Canada ULC ("Dow") earned income and incurred interest in the course of a non-arm's length revolving loan agreement with a related Swiss company. The Minister of National Revenue (the "Minister") reassessed Dow under subsection 247(2) of the *Income Tax Act* ("ITA") to account for additional income the company would have received had it been dealing at arm's length. This resulted in a significant increase to Dow's taxable income.

Dow requested that the Minister make a downward transfer pricing adjustment (the "adjustment") under subsection 247(10) of the ITA to account for the additional interest Dow would have incurred under an arm's-length transaction. Subsection 247(10) generally states that certain adjustments shall not be made unless "in the opinion of the Minister, the circumstances are such that it would be appropriate that the adjustment be made." The Minister advised Dow that she would not exercise this discretion.

Issues and Tax Court Decision

Dow appealed the reassessment to the Tax Court of Canada (the "Tax Court"), objecting to the Minister's decision to deny the request under subsection 247(10). The parties to the appeal asked the Tax Court to determine, pursuant to section 58 of the *Tax Court of Canada Rules (General Procedure)*, the question of whether the Minister's discretionary decision under subsection 247(10) of the ITA falls outside the exclusive jurisdiction of the Tax Court.

The Tax Court held that it had jurisdiction to hear Dow's appeal because the Minister's discretionary decision to deny the adjustment was central to the correctness of the assessment, which falls under the Tax Court's exclusive appellate jurisdiction.

Federal Court of Appeal Decision

The Federal Court of Appeal (the "FCA") reversed the Tax Court's decision on the basis that exclusive jurisdiction to conduct judicial reviews of the Minister's discretionary decisions under subsection 247(10) of the ITA lies with the Federal Court. The FCA noted that the Minister's decision is not an assessment and Tax Court remedies all relate to assessments, which are "the product of the process of determining a taxpayer's liability under the ITA and not the process itself".

Supreme Court of Canada Decision

The Supreme Court of Canada (the "Supreme Court") ultimately upheld the FCA's decision, with a 4-3 split between the majority and the dissent. The Supreme Court's decision was released the same day as *Iris Technologies Inc. v. Canada*, 2024 DTC 5099 ("*Iris*"), which also dealt with the distinction between the jurisdictions of the Federal Court and the Tax Court in tax matters.

As in *Iris*, the distinction between discretionary decisions and non-discretionary decisions featured heavily in the majority's reasons. The majority held that the Minister's decision is purely discretionary and stands apart from a tax assessment, and thus Dow's objection should be brought to the Federal Court for judicial review, rather than to the Tax Court for appeal of the assessment. On this point, the majority relied on precedent set by *Okalta Oils Ltd. v. Minister of National Revenue*, 55 DTC 1029 (EC), to affirm that a tax assessment is a non-discretionary decision.

The majority also contrasted the Minister's decision-making powers under subsection 247(10) to the non-discretionary rule in subsection 247(2). When the conditions for subsection 247(2) are met, the Minister has no choice but to issue an upward adjustment of income to the taxpayer to reflect the income they would have earned under an arm's length transaction. The Minister is under no compulsion to exercise her discretion under subsection 247(10), and if she does it may occur before or after the issuance of an assessment. The correct calculation of tax liability under the ITA does not depend on the Minister's exercise of discretion under subsection 247(10) as the default rule set by Parliament is that the Minister shall not grant a downward transfer pricing adjustment (unless she is of the opinion that it would be appropriate under the circumstances). Dow argued that the former Exchequer Court of Canada's jurisdiction to review discretionary decisions of the Minister under the *Income War Tax Act* suggests similar powers held by the Tax Court. However, the majority determined that the Exchequer Court's jurisdiction and the remedial powers that were available to it are of limited relevance to Tax Court principles under modern legislation.

Additionally, the majority distinguished between the standard of reasonableness applied by the Federal Court during judicial review and the *de novo* review for correctness that the Tax Court uses during an appeal. The Tax Court reviews assessments through trials, in which factual questions are determined on the balance of probabilities and fresh evidence can be adduced to support either party. This approach allows the Tax Court to apply tax law to the facts. The majority considered that if the Tax Court were to take on judicial reviews of ministerial decisions, it would have to apply a *de novo* correctness standard as it lacks jurisdiction to apply a reasonableness standard. This undermines the administrative law principle that discretionary decisions are presumptively assessed on a reasonableness standard, and would grant the Tax Court power to appropriate tax policy decisions of the Minister.

Lastly, the majority emphasized the importance of avoiding erosion of the Federal Court's statutory jurisdiction to conduct judicial review of discretionary administrative decisions. Treating the Minister's decision under subsection 247(10) as part of an assessment would bring into question the Federal Court's jurisdiction to review any tax-related discretionary decisions. Furthermore, granting the Tax Court jurisdiction over discretionary decisions by necessary implication would contradict section 18.5 of the *Federal Courts Act*, which requires an express rule to oust Federal Court jurisdiction. Tax litigation is not limited to the Tax Court and it is the Federal Court that holds the power to quash the Minister's discretionary decision.

The dissent disagreed with the majority's position that the Federal Court retained jurisdiction to review the Minister's decisions under subsection 247(10). The dissent maintained that the Minister's decision is inseparable from the subsequent tax assessment, and thus should be reviewed within the scope of an appeal from an assessment. The dissent reasoned that, unlike other discretionary powers of the Minister under the ITA, subsection 247(10) is not permissive as the Minister is obliged to form an opinion on a downward adjustment in order to determine a taxpayer's liability, particularly where subsection 247(2) is engaged. Accordingly, a decision under subsection 247(10) is inextricably linked to the assessment. On this basis, the dissent held that the Tax Court's statutory jurisdiction to review assessments takes precedence, to the exclusion of the Federal Court's jurisdiction, in cases involving the review of the Minister's decision under subsection 247(10).

Conclusion

The Supreme Court dismissed the appeal, concluding that review of the Minister's discretionary decision to deny a downward transfer pricing adjustment under subsection 247(10) belongs to the exclusive statutory jurisdiction of the Federal Court to conduct judicial review of federal administrative decisions.

— *Anitra Bowman, Student-at-Law*

Iris Technologies Inc. v. Canada, 2024 DTC 5099 (Supreme Court of Canada) — Supreme Court of Canada Finds Judicial Review Application To Be Collateral Attack on Correctness of ETA Assessments Beyond the Jurisdiction of the Federal Court

Background

Iris Technologies Inc. ("Iris") claimed tax refunds under the *Excise Tax Act* ("ETA") for a period ending in 2020. The Minister of National Revenue (the "Minister") then commenced auditing the relevant reporting periods, refusing to pay refunds claimed pending completion of the audit. Upon completion of the audit, the Minister issued assessments which disallowed input tax credits claimed by Iris and assessed gross negligence penalties with interest.

Issues and Federal Court Decision

Iris brought an application for judicial review in the Federal Court seeking declaratory relief regarding the Minister's conduct throughout the audit. Specifically, Iris sought three declarations summarized as follows:

(1) the Minister failed to afford procedural fairness in the audit, and failed to provide notice of or an opportunity for Iris to respond to the proposed adjustments;

(2) the assessments were made without evidentiary foundation and contrary to the Minister's findings of fact; and

(3) the Minister made the assessments for the improper purpose of seeking to deprive the Federal Court of jurisdiction in another application by Iris.

In response, the Attorney General of Canada brought a motion to strike on the basis that Iris' application was essentially a challenge to the correctness of the Minister's assessments under the ETA, which is a matter within the exclusive jurisdiction of the Tax Court of Canada instead of the Federal Court. The prothonotary dismissed the Attorney General's motion to strike on the basis that the application was not bereft of any chance of success because Iris' claims all engaged administrative law principles, over which the Federal Court holds jurisdiction in tax matters.

The Federal Court upheld the prothonotary's decision, agreeing that Iris' claims attacked the procedural fairness of the assessment and thus fell under the jurisdiction of the Federal Court.

Federal Court of Appeal Decision

The Federal Court of Appeal (the "FCA") reversed the Federal Court's decision and struck Iris' application. The FCA did so on the basis that the matter underlying the application was fundamentally an attack on the correctness of the Minister's assessment and was thus exclusively within the jurisdiction of the Tax Court. In light of this conclusion and the fact that the declarations sought were of no practical effect, the application was bereft of any possibility of success.

Supreme Court of Canada Decision

The Supreme Court of Canada (the "Supreme Court") upheld the FCA's decision, with two sets of concurring reasons that were unanimous in the result. The Supreme Court decision was released the same day as *Dow Chemical Canada ULC v. Canada*, 2024 DTC 5098 ("*Dow*"), which also dealt with the distinction between the jurisdictions of the Federal Court and the Tax Court in tax matters.

The issue before the Supreme Court was whether Iris' application in the Federal Court was bereft of any possibility of success. In order to determine this issue, the Supreme Court assessed whether Iris' claims fell under the jurisdiction of the Tax Court or the Federal Court by examining their true nature.

The Supreme Court agreed with the Attorney General that the essential nature of Iris' application was a collateral attack on the correctness of the Minister's assessments. Given that there is an "express direction" in the form of a statutory appeal to the Tax Court under the ETA for disputing assessments, section 18.5 of the *Federal Courts Act* precludes judicial review by the Federal Court. In reasons written by Justice Kasirer, the Supreme Court found that, notwithstanding the administrative law language in Iris' application, Iris' procedural fairness claim was grounded in the timing of the Minister's assessment and the consequential failure to provide Iris with an opportunity to respond to the Minister's proposed adjustments. Through a *de novo* review of the matter under the ETA's statutory appeal procedure, a Tax Court proceeding would provide an "adequate, curative remedy" to Iris' claim of procedural unfairness by allowing Iris a chance to respond to the assessments and to present fresh evidence on the incorrectness of the assessments.

Accordingly, Iris' application falls under the exclusive jurisdiction of the Tax Court to hear appeals on the correctness of tax assessments, which are non-discretionary decisions. As in *Dow*, the Supreme Court relied in part on the precedent set by *Okalta Oils Ltd. v. Minister of National Revenue* (55 DTC 1029 (EC)), which found that a tax assessment is a non-discretionary decision. Because Iris' claims ultimately sought to challenge the correctness of an assessment and not the exercise of discretion, the Federal Court had no jurisdiction for judicial review.

As for Iris' allegation that the Minister acted with an improper purpose, the Supreme Court agreed with the FCA that this claim should be struck. The Court acknowledged that the mere involvement of an assessment in an application does not oust the jurisdiction of the Federal Court where the Tax Court lacks jurisdiction to deal with the Minister's conduct or where the application seeks practical relief against the exercise of discretion.

However, in the present case Iris failed to allege facts supporting an improper purpose. The Minister issued an assessment, the contents of which are dictated by the non-discretionary rules of the ETA. The Supreme Court drew a distinction in this regard between this case and *Dow*. Because the appellant in Dow was ultimately seeking relief against the Minister's exercise of discretion, the Federal Court had jurisdiction. In contrast, Iris' application ultimately centred on the correctness of the assessment, a non-discretionary matter within the jurisdiction of the Tax Court. The Supreme Court quoted the reasoning of the FCA, stating that "fulfillment of a non-discretionary statutory responsibility cannot be an improper motive" for issuing an assessment.

Lastly, the Court found that the declarations sought by Iris were not connected to any asserted rights and would have no practical effect. Particularly, Iris' claims did not disclose any live controversy that the declarations would settle or resolve, as a declaration does not quash or vacate assessments. Where declarations would have no practical utility and an adequate alternative remedy exists, the declarations could not be issued.

In a concurring set of reasons written by Justice Côté, a minority of the Supreme Court agreed that Iris' application was a collateral attack on the correctness of the assessments, with adequate and effective relief available in the Tax Court. Noting that a reviewing court must gain "a realistic appreciation" of the nature of the claim, the concurring reasons supported looking beyond the words used, facts alleged, and remedy sought in a claim to determine if a claim may be a "disguised attempt" to attain an otherwise unattainable result in the Federal Court. The reasons also agreed that no recognizable allegation of improper purpose was made out in Iris' application, and that the declarations sought were of no practical effect.

Conclusion

The Supreme Court dismissed Iris' appeal and upheld the FCA's decision to strike Iris' application for judicial review.

— *Anitra Bowman, Student-at-Law*

Barwicz v. The King, 2024 DTC 1073 (Tax Court of Canada) — Departure Tax Applies to a Deemed Resident Trust After Its Departure

Background

In 2001, the spouse of Andrzej Barwicz (the "Appellant") created the Zaba Trust (the "Trust"), a discretionary *inter vivos* personal trust. The only trustee was the Royal Trust Corporation of Canada. There were nine beneficiaries, including the Appellant, designated in the deed of trust, which stipulated that all beneficiaries had the same rights and benefits. On the same day, the Trust acquired a significant number of shares of a corporation (the "Shares").

Shortly thereafter in 2001, the Royal Bank of Canada Financial Corporation, a tax resident of Barbados, replaced the Royal Trust Corporation of Canada as the trustee.

The Minister of National Revenue ("Minister") subsequently reassessed the Trust for its taxation year ended December 31, 2001, on the grounds that the emigration of the Trust to Barbados resulted in a deemed taxation year-end and a deemed disposition of the Trust's property.

After the Trust had generated cash through carrying out certain transactions relating to the Shares in 2003, it made two substantial capital distributions to the Appellant in 2004 ($2,250,000) and 2005 ($830,288), the second of which was the last distribution of the Trust before its liquidation and termination. At the moment of its second transfer in 2005, the Trust's tax liability, according to the Minister, amounted to $1,602,233.35.

In 2016, the Minister assessed the Appellant under section 160 of the *Income Tax Act* ("ITA") for the same amount (the "Assessment").

The Appellant's position was that the Trust did not have a tax liability at the time of the distribution, and claimed to have given consideration to the Trust for the distribution from the Trust to the Appellant for the purposes of subsection 160(1) of the ITA.

Issues and Decision

The issues before the TCC were as follows :

(1) whether the change in the tax residence of the Trust caused a deemed taxation year-end and a deemed disposition of the Trust's property; and

(2) whether the Appellant gave consideration for the distribution for the purposes of subsection 160(1) of the ITA.

Regarding the change of the tax residence of the Trust, the TCC considered whether subsection 94(1) of the ITA, which provides that a trust is deemed to be resident of Canada upon meeting certain conditions, should take precedence over subsection 128.1(4) of the ITA, which provides for a deemed taxation year-end and disposition of the property of a trust immediately before the trust ceases to be resident in Canada.

Referring to *Fundy Settlement v. Canada*, 2012 DTC 5063 (SCC), the TCC indicated that subsection 94(1) of the ITA deems certain trusts to be resident in Canada when they would not otherwise be, so that these trusts are subject to greater tax obligations in Canada. As for subsection 128.1(4) of the ITA, the deemed taxation year-end and disposition of trust property creates a departure tax liability on latent gains, and subsection 128.1(4) of the ITA applies to the entire ITA, without being subject to any contrary express provision provided for elsewhere.

Subsection 94(1) of the ITA does not determine tax residency, but rather deems certain trusts that are non-residents of Canada during a given taxation year to be resident in Canada. The determination of the taxation year of the Trust and its residency status must precede the application of subsection 94(1) of the ITA. Therefore, subsection 94(1) of the ITA cannot take precedence over subsection 128.1(4) of the ITA and the application of subsection 94(1) of the ITA to the Trust does not prevent the application of subsection 128.1(4) of the ITA, the purpose of which is to crystallize the taxable capital gains made by the Trust prior to leaving Canada.

Regarding whether any consideration for the distribution was given for the purposes of subsection 160(1) of the ITA, the TCC referred to *Eyeball Networks Inc*. *v*. *Canada*, 2021 DTC 5011 (FCA) ("*Eyeball Networks*") and stated that the purpose of subsection 160(1) of the ITA is to ensure that the value of existing property in the taxpayer's (transferor's) patrimony is preserved for collection by the CRA.

The notion of "transfer" at subsection 160(1) of the ITA has an ordinary, rather than technical, meaning, and thus should be interpreted in a large and liberal way. In this case, the capital distribution of the Trust's property was indeed a transfer, characterized by an enrichment of the Appellant, and a correlative impoverishment of the Trust. The TCC noted that if one party is enriched and the other is impoverished by the same amount, it is possible to conclude that the enriched party has not offered equivalent consideration.

After the transfer, the Appellant's beneficial rights in the Trust remained the same. Although the Appellant had a right in the Trust to be considered by the trustee for any distribution on the same basis as the other beneficiaries, the TCC found that the value of the right had not been proven, and there was no reason to believe that anyone would have paid even a very small amount for it.

The TCC found that the Appellant's situation could be distinguished from the situation in *Eyeball Networks*, where the transfer was a redemption of shares. The fact that the second distribution preceded the termination and liquidation of the Trust made no difference.

The Appellant submitted that subsection 107(2) allowed for a tax rollover at cost of trust property, resulting in the Appellant being deemed to have given consideration equal to the value of the property he received during the distribution. The TCC rejected this argument, stating that the special treatment of subsection 107(2) of the ITA has no direct application in the context of subsection 160(1) of the ITA. The word "transfer" must be understood in its ordinary, economic sense, and not in the technical or tax sense put forward by the Appellant.

Conclusion

The appeal was dismissed. *Barwicz* provides insight regarding the interpretation of statutory provisions in the ITA that appear to be conflicting, and the concepts of "transfer" and "consideration" in the context of subsection 160(1) of the ITA in matters involving trusts.

— *Victor Qian, Associate*

Entrepôt Frigorifique International Inc. c. Le Roi, 2024 DTC 1081[1] (Tax Court of Canada) — No Additional Due Diligence Required by Taxpayers Claiming ITCs Beyond Statutory Requirements

Background

Entrepôt Frigorifique International Inc. (the "Appellant") operates a refrigerated transport and storage company. From October 1, 2010 to December 31, 2014, the Appellant entered into agreements with various employment agencies for the supply of temporary workers for its refrigerated storage facilities. The various employment agencies ("Agency" or "Agencies") invoiced the Appellant for the services — the invoices included all of the prescribed information provided for in the *Input Tax Credit Information (GST/HST) Regulations* (the "Regulations"). The Appellant paid the invoices, including the GST, to the Agencies, and claimed the GST paid as input tax credits ("ITCs"). The Agencies, however, did not remit the GST collected to the tax authorities.

The Ministère du Revenu Québec ("MRQ") assessed the Appellant ("Assessment") beyond the normal period of four years, disallowing the ITCs claimed by the Appellant and imposing a gross negligence penalty under section 285 of the *Excise Tax Act* (Canada) ("ETA").

Issues and Decision

The issue before the Tax Court of Canada ("TCC") was whether the Appellant made a misrepresentation that was attributable to neglect, carelessness, or wilful default, or whether it committed fraud in its GST return by claiming the ITCs, allowing the MRQ to issue the Assessment beyond the normal period of assessment. Pursuant to subsection 298(4) of the ETA, the onus was on the MRQ.

The MRQ alleged that the invoices issued by the Agencies were false invoices, invoices of accommodation or convenience; that the Agencies were not the suppliers of the services as they did not have the financial, human, or material resources to supply the services; and that the Appellant was part of a scheme, or should have known that there was a scheme, not to remit the GST.

[1] The decision has not yet been translated into English.

The Appellant had a procedure in place to verify that any new supplier was listed on the relevant provincial corporate registry and that it had a valid GST registration. In addition, there was no evidence to suggest that the temporary workers provided by the Agencies did not perform the actual work. This work was essential to the Appellant's business operations, and the Appellant was not denied the deduction from its taxable income for the same services. Moreover, there was no evidence that the Appellant did not act in good faith or follow reasonable business practices.

The MRQ was fully aware that some of the Agencies had not remitted the GST collected and did not alert the Appellant. The MRQ authorized and even required the defaulting Agencies to continue to collect GST on its behalf. The testimony of the MRQ's representatives revealed that the MRQ had revoked the GST registration of one of the Agencies and reinstated its registration on two distinct occasions, even when the MRQ knew that the Agency did not remit the GST it collected.

Furthermore, and of note in this decision, the TCC stated that the ETA and the Regulations cannot be interpreted as imposing an undeclared additional requirement on a recipient to exercise due diligence in respect of its GST registered suppliers which would include, based on the MRQ's position, the examination of the physical establishment of the supplier, the agreements between the supplier and its personnel, the intention of the supplier to use subcontractors to carry out the supply, and more. In the view of the TCC, if the legislator intended to impose those obligations on a recipient, it would have clearly stipulated such in the legislation, but it did not.

Conclusion

The TCC concluded that the MRQ did not meet the onus of proving, on the balance of probabilities, that the Appellant made a misrepresentation that was attributable to neglect, carelessness, or wilful default, or that it committed fraud in its GST return by claiming the ITCs. The TCC allowed the Appellant's appeal and vacated the assessment. The TCC also noted that, even if the MRQ had assessed the Appellant within the normal period, the facts of the case would still support the Appellant's entitlement to ITCs and would not have substantiated the gross negligence penalty under section 285 of the ETA.

The TCC's decision assures that in order to claim ITCs with respect to an expense incurred in the course of a commercial activity, a registrant's sole obligation is to comply with the mandatory requirements of subsection 169(4) of the ETA and section 3 of the Regulations. No additional due diligence is required beyond this compliance where there is no evidence of involvement in schemes involving false, convenient, or accommodation invoices.

— Dragann Mallette, Senior Associate

CURRENT ITEMS OF INTEREST

Capital Gains Inclusion Rate Shortfall

Budget 2024 introduced an increase in the capital gains inclusion rate from one-half to two-thirds for corporations and trusts, and from one-half to two-thirds on the portion of capital gains realized in the year that exceed $250,000 for individuals. This policy is in effect for capital gains realized on or after June 25, 2024. The Parliamentary Budget Officer ("PBO") estimates an increase of $17.4 billion in income tax revenues from 2024–25 to 2028–29 due to these changes, which is less than the $19 billion estimated in Budget 2024. To access the full report from the PBO, visit www.pbo-dpb.ca/en/publications/LEG-2425-010-S--increasing-capital-gains-inclusion-rate--augmentation-taux-inclusion-gains-capital.

SimpleFile Invites Sent Out for Pilot Project

In July, the CRA expanded its SimpleFile services (phone, digital, and paper) to invite more than 500,000 eligible lower-income individuals to file their return. This automatic tax filing national pilot targets individuals who have never filed a tax return or who have a gap in their filing history, and builds upon the small-scale SimpleFile pilots previously undertaken by the CRA.

In early 2024, the CRA invited more than 1.5 million individuals with a lower income or a fixed income and who are in a simple tax situation that remains unchanged from year to year to use SimpleFile by Phone. To date, more than 90% of the invitees have filed their tax return, using a variety of filing methods the CRA offers.

SimpleFile is a Budget 2024 commitment and the CRA is on track to further increase the number of invitations to two million for the 2025 tax season. SimpleFile is an invitation-only service, whereby the CRA invites eligible individuals to file their tax return. When using the phone or digital service, individuals will need to confirm some personal information and answer a series of short questions. For those using the phone service who have already created a personal identification number ("PIN") in My Account, an estimate of their net income, taxable income, and any refund that they may be eligible for will be available at the end of the call.

A tax return can still be automatically filed without a PIN. Individuals will receive a Notice of Assessment either in the mail or in My Account after their return has been processed. SimpleFile services are available for a limited time to assist individuals in automatically filing their 2023 tax return. The phone and digital services are available 21 hours a day, from 6 a.m. to 3 a.m., Eastern time, seven days a week.

2025 Payroll Deductions Formulas Issued

The following document was recently issued: Payroll Deductions Formulas — 120th Edition (Upcoming changes) Effective January 1, 2025 (July 2024) (https://www.canada.ca/en/revenue-agency/services/forms-publications/payroll/t4127-payroll-deductions-formulas/t4127-jan1/t4127-jan-payroll-deductions-formulas-computer-programs.html).

INTERNATIONAL NEWS

EU Seeks Input on Anti-Tax Avoidance Directive Review

The European Commission is seeking input on an ongoing review into the Anti-Tax Avoidance Directive ("ATAD"), with a focus on the interest expense deduction limitation provisions.

ATAD, or Council Directive (EU) 2016/11641 of 12 July 2016, set out minimum standard measures on addressing the most common forms of aggressive tax planning and tax avoidance practices that directly affect the functioning of the internal market, in response to the OECD's BEPS Project. All member states were required to incorporate the provisions into their corporate tax regimes.

ATAD included provisions in five areas: the interest limitation rule, exit taxation, the controlled foreign company rule ("CFC"), the hybrid mismatches rule, and the general anti-abuse rule ("GAAR").

Article 10 of the Directive requires that the Commission evaluate the implementation of ATAD, in particular the impact of Article 4 (the interest limitation rule), and report back to the Council.

The review is to cover three broad themes:

(1) The implementation of ATAD in the Member States and the policy choices made where the Directive allowed the Member State legislator to choose;

(2) The functioning of ATAD, in the form of a qualitative and quantitative assessment of the effectiveness of ATAD's measures as a minimum standard in addressing aggressive tax planning; and

(3) Potential improvements to the measures to ensure they continue to achieve their objectives, especially in light of the adoption of the Global Minimum Tax Directive.

Feedback is being sought by September 11, 2024.

UK Tax-Related Interest Rates Set To Fall

His Majesty's Revenue and Customs ("HMRC") interest rates for late payments will be revised following a decision from the Bank of England to lower the bank rate to 5%.

The Bank of England Monetary Policy Committee voted on July 31, 2024 to lower the rate from 5.25% to 5%, by a narrow margin of five votes in favour and four against. As a consequence of the change in the base rate, HMRC interest rates for late payment and repayment will fall. HMRC will soon confirm that the interest rate on late payments will fall to 7.5%.

Late payment interest is set at base rate plus 2.5%. Repayment interest is set at base rate minus 1%, with a lower limit — or "minimum floor" — of 0.5%.

UK Legislates To Prevent Abuse of Pillar Two CbC Reporting Safe Harbour

The UK tax agency has released guidance on the transitional country-by-country ("CbC") reporting safe harbour anti-arbitrage rule under the territory's Pillar Two minimum tax framework on large multinational enterprises.

The UK has adopted an income inclusion rule and domestic minimum top-up tax rule to implement the Global Anti-Base Erosion ("GloBE") Rules agreed by the UK and other members of the BEPS Inclusive Framework.

The measure is in response to concerns about the use of avoidance transactions designed to exploit differences between the tax and accounting rules to allow groups to qualify for the transitional CbC reporting safe harbour where they would otherwise not have.

The draft legislation provides for the implementation of an anti-arbitrage rule which protects the UK from a loss of tax. It also ensures that UK legislation remains consistent with OECD administrative guidance on the GloBE rules agreed by the UK and other members of the Inclusive Framework.

The transitional CbC reporting safe harbour is intended to significantly simplify compliance with the GloBE Rules for an initial period, enabling multinationals to base their calculations around financial information used for purposes of CbC reporting.

The legislation will have effect from March 14, 2024.

UK Legislates To Remove Tax Breaks for Furnished Holiday Lets

His Majesty's Revenue and Customs ("HMRC") has released guidance and draft legislation on the repeal of the furnished holiday lettings ("FHLs") tax regime.

The draft legislation provides for the removal of specific tax rules and separate reporting requirements for FHLs. Income and gains from an FHL will then:

- form part of the person's UK or overseas property business; and
- be treated in line with all other property income and gains.

The current rules provide beneficial tax treatment for furnished holiday lettings compared to other property businesses in broadly four key areas:

(1) exemption from finance cost restriction rules (which restrict loan interest to the basic rate of income tax for other landlords);

(2) more beneficial capital allowances rules;

(3) access to relief from taxes on chargeable gains for trading business assets; and

(4) inclusion as relevant UK earnings when calculating maximum pension relief.

To qualify as an FHL, properties:

- must be available for short-term letting to the public for 210 days and actually let for 105 days or more in each tax year; and
- should not be used as a long-term let of over 31 days for significant periods.

The distinction for a furnished holiday let was introduced in 1984 and provided different and more beneficial tax treatment for short-term lettings within the property investment sector.

The new UK Government considers that repealing the beneficial tax treatment for FHLs promotes fairness by removing the tax advantages that FHLs let landlords have over other residential property landlords.

The draft legislation provides that the measure will be effective:

- on or after April 6, 2025, for income tax and for capital gains tax; and
- from April 1, 2025, for corporation tax and for corporation tax on chargeable gains.

New UK Government Sets Out Plans To Overhaul Non-Dom Rules

The new UK Government has released a policy paper setting out its plans to reform the tax rules for non-domiciled ("non-dom") individuals.

The Government has said it intends to remove the concept of domicile status from the tax system and implement a new residence-based regime. It intends to implement the four-year foreign income and gains ("FIG") regime announced by the previous government at the Spring Budget. However, certain concessions for non-domiciled individuals will be reined in. For instance, preferential tax treatment based on domicile status will be removed for all new FIGs that arise from April 6, 2025.

To replace the remittance basis of tax, the Government plans to introduce an "internationally competitive" residence-based regime, providing 100% relief on FIG for new arrivals to the UK in their first four years of tax residence, provided they have not been UK-tax-resident in any of the 10 consecutive years prior to their arrival.

From April 6, 2025, the protection from tax on income and gains arising within settlor-interested trust structures will no longer be available for non-domiciled and deemed domiciled individuals who do not qualify for the four-year FIG regime.

The Government has also said it intends to conduct a review of offshore anti-avoidance legislation, including the Transfer of Assets Abroad and Settlements legislation, to modernize the rules and ensure they are fit for purpose. These changes will not be introduced before the 2026/27 tax year, with further details to be published in future.

The Government has also said it will retain a form of Overseas Workday Relief ("OWR"). It said officials will engage with stakeholders on the design principles for this tax relief and further details will be confirmed at the next Budget.

The policy announced by the previous government, providing a 50% reduction in foreign income subject to tax for individuals who lose access to the remittance basis in the first year of the new regime, will not be introduced.

UK resident individuals who are ineligible for the four-year FIG regime (or who choose not to make a claim for a tax year) will be subject to capital gains tax ("CGT") on foreign gains in the normal way. Transitionally, for CGT purposes, current and past remittance basis users will be able to rebase foreign capital assets they hold to their value at the rebasing date when they dispose of them. The Government has said it is considering the appropriate rebasing date and will set this out at the next Budget.

Any FIG that arose before April 6, 2025, while an individual was taxed under the remittance basis, will continue to be taxed when remitted to the UK, as is the case under the current rules. This includes remittances of pre-April 6, 2025 FIG for those who are eligible for the new four-year FIG regime.

A new Temporary Repatriation Facility ("TRF") will be available for individuals who have been taxed on the remittance basis. Individuals that have previously claimed the remittance basis will be able to remit FIG that arose prior to April 6, 2025, and pay a reduced tax rate on the remittance for a limited time period after the remittance basis has ended. The Government has said, "The rate and the length of time that the TRF will be available will be set to make use as attractive as possible."

"The government is also exploring ways to expand the scope of the TRF, including to stockpiled income and gains within overseas structures, and will confirm further details at the Budget," it said.

The Government has also set out plans for a new residence-based regime for inheritance tax.

Inheritance tax ("IHT") is currently a domicile-based system. The Government intends to replace this with a new residence-based system from April 6, 2025. This will affect the scope of property brought into UK IHT for individuals and trusts.

The Government envisages that the basic test for whether non-UK assets are in scope for IHT from April 6, 2025 will be whether a person has been resident in the UK for 10 years prior to the tax year in which the chargeable event (including death) arises, with provision to keep a person in scope for 10 years after leaving the UK.

The Government has said it will engage further with stakeholders on the operation of the new test, so that any refinements can be considered fully. IHT charges arising on deaths occurring before April 6, 2025 will be unaffected by these changes and will be charged according to the existing rules.

The Government will end the use of Excluded Property Trusts to keep assets out of the scope of IHT. It plans to change the way IHT is charged on non-UK assets which are held in such trusts, so that everyone who is in scope of UK IHT pays their taxes in the UK.

The Government said:

> The Government recognizes that trusts will already have been established and structured to reflect the current rules, so is considering how these changes can be introduced in a manner that allows for appropriate adjustment of existing trust arrangements, while ensuring that the treatment of all long-term residents of the UK is the same for IHT purposes. Confirmation of these new rules and their detailed application, including transitional arrangements for affected settlors, will be published at Budget, following external engagement.
>
> The government will not carry out a formal policy consultation on moving to a residence-based system for IHT. Instead, it will review stakeholder feedback provided following the Spring Budget and officials will carry out further external engagement over the summer on IHT policy design.

TAX TOPICS

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