

## BREXIT – ITS CONSEQUENCES FROM THE POINT OF CUSTOMS AND VALUE ADDED TAX



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**In the referendum of 23 June 2016, a majority of the UK decided that their country should leave the EU. However, the exit will not take place immediately. Both sides look forward to lengthy and wearisome treaty negotiations before they can put their legal and economic relations on a new basis. Due to the impending exit of Great Britain from the EU, it is advisable for businesses to keep an eye on the development of the tax and legal issues and/or to make corresponding preparations.**

Some weeks and months have now passed since the vote by the British people on 23 June 2016. The first cry of horror has died away, the aftermath has not yet begun. It is not yet definite when the present British government will hand over its request for exit to the European Commission. At the moment this is expected to happen in March 2017. As from that date, the negotiations regarding the new nature of the relations between the European Union (EU) and Great Britain will begin. Up to that date, all parties will have taken up their (verbal) positions. Up to the present, no legal changes have taken place; the general conditions remain completely unchanged. The concrete legal implications of Brexit are thus not yet defined, and the likely consequences of the UK's withdrawal from the EU will be decided during the months ahead.

It must be emphasised that the Brexit referendum affects all enterprises having their legal seat or a branch in an EU country, provided that they have some kind of business relations with Great Britain. Further, the referendum also affects enterprises having their legal seat outside the EU (for example, in Switzerland) that have special trade relations with the EU and sell goods in the UK or purchase goods from the UK. For this reason it is essential for these enterprises to start considering the likely changes in good time: in particular, it can be assumed that there will be serious implications in connection with value added tax and customs duties in the area of the trading of goods and services with Great Britain. Changes will be required (inter alia) with regard to the processes (for example, amendment of supply chains), IT (in

particular tax codes), price structuring and invoicing (including the price and the invoice text).

### **1. The EU single market and its fundamental freedoms**

One of the cornerstones of the EU is free access to the single market. This means a common economic area which guarantees all EU citizens four basic freedoms:

- Free movement of persons: within the EU, all EU citizens can move freely and without border controls, reside and work.
- Free movement of goods: within the EU, goods can be freely imported and exported across state borders without customs controls.
- Freedom to provide services: services can be offered in all EU countries.
- Free movement of capital: EU citizens can decide freely where they would like to invest their money within the EU.

A country can only have free access to the single market if all four above-named basic freedoms can be guaranteed. Great Britain has decided that it no longer wants to guarantee the free movement of persons, i.e. unrestricted access for EU citizens to the British labour market. Provided that the new British government under Theresa May actually adheres to this restriction of the single market principle and actually closes the labour market for non-Britons, then Great Britain would no longer be able to participate in the single market. The grant of an

exception can be excluded; this has already been reiterated several times. This attitude of the EU is completely understandable, given that according to art. 26 of the Treaty on the Functioning of the EU (TFEU) “the internal market shall comprise an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of the Treaties”.

It must thus be assumed that Great Britain will no longer belong to the single market. The single market will consequently afterwards no longer consist of 28 members, but of 27 members. Apart from the currently applicable border controls of persons between the EU and Great Britain (Great Britain never entered into the Schengen Agreement of 1995 for, in particular, the abolition of stationary border controls at the internal borders of the participating states), customs controls will apply as from the exit date.

### **2. Value added tax and Brexit**

As in all other countries which have a value added tax system, value added tax is one of the most important taxes. It can thus be assumed that, by and large, the system will remain in force after Brexit. However, when interpreting the corresponding regulations, the British authorities and courts would no longer be bound by European law (in particular the directive on the common system of value added tax) and/or to the decisions by the Court of Justice of the European Union. Great Britain would thus be

able to be more flexible in implementing certain regulations; certain additional exemptions of goods and services, aimed at supporting particular industrial sectors, are conceivable. The complete abolition of British value added tax is however unlikely, given that it represents a share of around 20% of the entire fiscal revenue.

Apart from the periodic VAT returns, the crucial matter is the additional VAT declarations that are necessary in the EU, like the Intrastat declarations and the recapitulative statements, which are connected to participation in the single market. These obligations would no longer apply in respect of Great Britain, based on the new status as a third country.

### **3. Customs duties and Brexit**

European customs legislation is a central part of EU law and makes it possible to achieve the fundamental freedom of the free movement of goods: the customs legislation in the EU member states is no longer based on national and local provisions, but has been based since 1994 on the Community Customs Code. The basis for this is the EU Customs Union, which forbids the levying of customs duties and charges in connection with the trade in goods between member states, and which also introduced a uniform customs tariff in relations with third countries.

As already mentioned above, the exit from the EU would also mean the exit from the European Customs Union, meaning that Great Britain would again have the status of a third country. Great Britain would then no

longer be bound by the uniform customs provisions of the EU, but would be entitled to give itself its own national customs regulations – and to levy customs duties. On the other hand, the EU will no doubt also levy customs duties on the import of British goods.

In the last analysis, the negotiations between the EU and Great Britain will determine whether customs duties will actually be charged in future. It is also possible that the United Kingdom could become a member of the European Economic Area (EEA), joining Norway, Iceland and Liechtenstein. Great Britain would then still have to harmonise its laws in relation to the free movement of persons, services, goods and capital and to recognise EU requirements with regard to sovereign rights. A further possibility would be the conclusion of a free trade agreement with the EU. In this case, the European regulations and the decisions of the Court of Justice of the European Union would not have to be recognised.

### **4. The concrete indirect tax implications**

#### **4.1. Shipment of goods**

After exit from the EU, the shipment of goods to Great Britain must be declared as an export – and no longer as an intra-Community supply. The corresponding regulations of an EU member state must consequently be complied with – in particular the burden of proof in the case of a supply which is exempt from tax. In future, however, it will no longer be necessary to make Intrastat declarations and recapitulative

statements when shipping goods to Great Britain.

#### 4.2. Purchase of goods

After Great Britain's exit from the EU, where goods are purchased out of Great Britain to the EU, this will no longer be an intra-Community acquisition, but an import into the EU. In future it is important to note that import taxes as well as customs duties may be levied. Import taxes can basically be deducted as input VAT, but customs duties cannot be so deducted. The enterprises must make a new calculation to take this new burden into consideration, provided that Great Britain does not conclude new customs agreements with the EU or other countries (EEA or free trade agreements). It would then be important to check whether the additional burden would be reduced, for example by using duty-free warehouses or an amended tariffing.

#### 4.4. Services

Where the recipient of a service has its legal seat in Great Britain, it will be necessary to check locally what evidence is needed in connection with this provision of service abroad. It would no longer be possible to give the VAT identification number as proof of the entrepreneurial status.

#### 4.5. Input tax refund procedure

For enterprises resident in the EU, the time limit for input tax refund applications is currently nine months (30 September of the following year). On Great Britain's exit from the EU, the legal requirements for third

countries would apply, so that the application period would be reduced to six months.

### Summary

Several months have elapsed since the British people voted on the exit from the EU. The UK's request for exit has not yet been presented: this is expected to take place in March 2017. The EU and Great Britain would then have a period of two years in which to settle the exit procedure. If we consider the procedures applying in connection with the Comprehensive Economic and Trade Agreement between Canada and the EU (CETA), it becomes clear that it will not be easy for Great Britain to impose its own ideas here. It is not only that the EU institutions (EU Commission, Parliament and Council of Ministers) have to approve any treaty with Great Britain, but also that all the remaining 27 member states have to accept the negotiated treaty. Only if all of them agree can the exit take place according to the result of the negotiations. This will not be an easy task, either for the British government or for the EU. It cannot however be expected that Great Britain will succeed in cherry-picking, such as e.g. participation in the single market without a guarantee of free movement of persons.

Provided that the government of Great Britain does not change its attitude towards the guarantee for free movement of persons, it appears certain that the United Kingdom will not be granted access to free movement of goods. Great Britain will thus no longer be a member of the single market, but will act in

relation to the EU as a third country – like Switzerland, Iceland or Norway. This entails serious consequences at the level of indirect taxes: economic frontiers will be erected between the EU and Great Britain. There will be implications for supplies of goods on both sides at the level of customs duties as well as import VAT. When the Swiss electorate voted against joining the EEA on 6 December 1992, the Swiss federal government declared in January 1993 that it would like to build up its relations with the European Community on a bilateral basis. Negotiations lasted for six years, until on 21 June 1999 the first bilateral agreements were signed and they came into force on 1 January 2002 after the referendum in Switzerland accepted them. If the negotiations between Great Britain and the EU drag on equally long, the enterprises should be prepared for a long transition period of uncertainty with regard to the economic relations between the two economic areas.

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