



Brexit - What to do?

On 29 March 2019, the UK will officially leave the EU. Irrespective of the shape of the future relationship between the EU and the UK, a customs border will be created. Whether the outcome of the negotiations leads to a Free Trade Agreement, a customs union, or whether no deal will be reached, in all scenarios a customs border will exist where this was previously not the case.

Without taking appropriate measures, businesses trading with the UK will be confronted with significant delays at the UK and EU customs borders. In the Netherlands alone, approximately 77,000 companies are trading goods with the UK and over 35,000 of these companies never dealt with customs before, and hence have no customs management in place. Appropriate measures should be taken now to prevent goods being stopped at the border post-Brexit. Because one thing is clear: Brexit will force businesses trading with the UK to deal with customs formalities.

On the long-term horizon, it is likely that the UK and EU will either agree on a Free Trade Agreement ("FTA"), or that the UK would form a customs union with the EU-27 ("Customs Union"). Either way companies will face a significant additional administrative burden and potential supply chain disruption.

Customs Union	Free Trade Agreement
	
<ul style="list-style-type: none"> No customs duties Additional customs formalities Import VAT, VAT formalities and VAT cash flow 	<ul style="list-style-type: none"> Additional customs duties Additional customs formalities Import VAT, VAT formalities and VAT cash flow
<p>Example: Turkey</p>	<p>Examples: Switzerland, Norway, South Africa, Korea & Mexico</p>

A. What is happening

On 29 March 2017 the UK officially notified the EU that it intends to withdraw from the EU. As of this date, the UK and the EU had two years to agree the 'Brexit' (unless postponed). On 14 November 2018, the EU and UK agreed a Draft Withdrawal Agreement (establishing the terms of the UK's withdrawal from the EU). However, this draft deal was voted down by the UK Parliament on 15 January 2019, less than 10 weeks before the Brexit deadline.


As indicated by many EU leaders, the risk of a no deal is increasing by each day closer to the deadline.

As such, chances that a third country ("WTO") scenario - commonly referred to as a 'hard' Brexit - will apply as of 29 March 2019 are increased significantly. This means that the UK has no longer preferred access to the EU single market and the EU Customs Union and vice versa.


Third Country (WTO)

<ul style="list-style-type: none"> Additional customs duties Additional customs formalities Import VAT, VAT formalities and VAT cash flow
<p>Example: Russia, USA, Japan, China</p>

B. What is the impact

 Means: **Additional formalities**

▶ Every transfer of goods between the EU and the UK will become subject to import and export formalities. Therefore, EU import and export declarations will have to be filed with local Customs Authorities. Customs formalities can create delays in the shipment of goods and may lead to additional costs within the supply chain.

 Means: **Additional custom duties**

▶ Custom duties are non-refundable and therefore create a cost for businesses. The changes may result in an average of 3% import duties, but some products may be subject to customs duties as high as 48%.

C. Factory/distribution center in the UK

If your business has a factory or distribution center in the UK from which the EU market is served, the impact of 'hard' Brexit will be significant: both in terms of administrative costs and customs duties.

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1 Current state / pre-Brexit



2 Future state / post-Brexit



	Pre-Brexit	Post-Brexit
Third country -> UK		
Formalities	Yes	Yes
Customs duties	Yes	Yes
UK -> EU		
Formalities	No	Yes
Customs duties	No	Yes

Impact

After a hard Brexit, the Customs Union with the EU will cease to exist for the UK. Therefore, customs duties and formalities will become applicable on any transfer of goods from EU to your factory/distribution center in the UK.

Possible mitigation measures

- ▶ **UK Distribution center**
Amend the supply chain for goods destined for the EU market by importing and storing them in an EU member state rather than in the UK. Formalities and duties will then not apply twice (both in the UK and in the EU).
- ▶ **UK Factory**
Customs exemptions/simplifications and authorizations (e.g. inward processing) may improve the position from a customs duty perspective. At the same time, changes might also have transfer pricing and corporate income tax consequences.

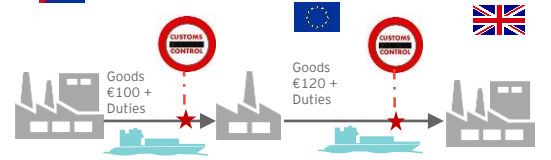
D. Factory / distribution center in the EU

If your business has a factory or distribution center in the EU from which the UK market is served, the impact of a 'hard' Brexit may have a significant impact from both an administrative costs and UK import duty perspective.

1 Current state / pre-Brexit



2 Future state / post-Brexit



	Pre-Brexit	Post-Brexit
Third country -> EU		
Formalities	Yes	Yes
Customs duties	Yes	Yes
EU -> UK		
Formalities	No	Yes
Customs duties	No	Yes

Impact

- ▶ The flow of goods from the EU to the UK will be impacted, as the EU Customs Union will no longer exist after a 'hard' Brexit (flow from third country to EU remains unchanged). Therefore, formalities and customs duties will apply on the flow of goods from the EU and the UK.

Possible mitigation measures

- ▶ Rather than transporting goods via an EU warehouse, goods could be transported from the third country directly to an UK warehouse. Import formalities and customs duties would then only apply at the UK border as the goods would not be transported via the EU.

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E. VAT

Import VAT

After Brexit, the movement of goods from UK to EU will be subject to import VAT (generally >20%), which must be financed. Depending on the country, it may take up to five years before import VAT is repaid. However, some countries apply an import VAT deferment scheme. Under this scheme, the import VAT is not payable immediately upon importation. Instead, payment is deferred to the periodical VAT return, where it can be deducted in the same VAT return, resulting in no actual import VAT payment and zero cash flow disadvantage. To apply this scheme, non-EU businesses may have to appoint a fiscal representative and set a bank guarantee in the EU.

EU VAT refunds

It can become more difficult for UK registered entities to reclaim EU VAT, since normal EU refund procedures no longer apply (and v.v.). EU countries can invoke reciprocity and put additional requirements on VAT refunds.

Import VAT refund	Import VAT deferment relief (cash neutral)	Regular non-EU refund procedure
Netherlands	Yes	Yes
Germany	No	Requires reciprocity
France	Yes, under certain strict conditions/requirements	Yes
Spain	Yes, under certain conditions/requirements	Requires reciprocity
Denmark	Yes, under certain conditions/requirements	Yes
Belgium	Yes, under certain conditions/requirements	Yes

E-commerce and distance sales

UK registered entities using the simplifications for e-commerce and distance sales in the UK need to reassess their VAT position as the simplifications no longer apply.

Legal certainty

EU law and jurisprudence may no longer be binding to the UK. This may result in uncertainty and potential deviations of VAT rates and treatment of transactions and industries. Further, there may be no protection against double taxation (VAT). Lastly, issues could arise in relation to where to keep the VAT records (EU vs. UK).

F. Other tax considerations

Post-Brexit operating model

Brexit brings various challenges and uncertainty, but also opportunities for multinational companies (MNCs) to rethink and make their existing operating models more efficient and sustainable. It is likely that some will need to make important structural changes to continue operating in the UK and across the EU in an efficient manner. Below a few examples are provided of operating model changes that Brexit may trigger:

- ✓ Supply chain reorganization resulting in transactional flows changes due to the new customs border between the UK and the EU;
- ✓ Undertaking more activity through presence established in the EU due to for instance specific sector regulations or the necessity to retain market access. This may be achieved via legal reorganizations and/ or organizational and business process changes (e.g. roles and responsibilities, decision-making, reporting lines, etc.);
- ✓ Rethinking intercompany financing model in order to, for instance, meet working capital needs.

These changes will drive various Direct Tax and Transfer Pricing (DTTP) implications such as changes in the existing TP model and support, taxable footprint and potential exit taxation.

EU Directives

The European Parent-Subsidiary Directive (“PSD”) and the Interest and Royalties Directive (“IRD”) provide for 0% withholding tax on dividends, interest and royalties paid between entities resident in EU Member States. Following the Brexit, these Directives no longer apply to the UK. The UK will need to rely on bilateral tax treaty rates, which often provide for a higher rate and stricter rules.

Below, we have included an overview of withholding tax treaty rates on dividends, interest and royalties of the EU Member States with the UK who would no longer allow a 0% withholding tax rate under the EU PSD and IRD. The rates below are based on the scenario where a UK holding company has a 100% interest in the EU Member State subsidiary.

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Pre-Brexit	Dividend	Interest	Royalty
Intra EU	0%	0%	0%

Post Brexit (DTT rates)	Dividend	Interest*	Royalty*
Austria	5%	0%	10%
Belgium	0%	0%/5%	0%
Bulgaria	0%	0%/5%	5%
Croatia	5%	0%/5%	0%/5%
Cyprus	0%	10%	0%/5%
Czech Republic	5%	0%	0%/10%
Denmark	0%	0%	0%
Estonia	5%	0%/10%	0%/5%/10%
Finland	0%	0%	0%
France	0%	0%	0%
Germany	5%	0%	0%
Greece	10%	0%	0%
Hungary	0%	0%	0%
Ireland	5%	0%	0%

Post Brexit (DTT rates)	Dividend	Interest*	Royalty*
Italy	5%	0%/10%	8%
Latvia	5%	0%/10%	0%/5%/10%
Lithuania	5%	0%/10%	0%/5%/10%
Luxembourg	5%	0%	5%
Malta	0%	10%	10%
The Netherlands	0%	0%	0%
Poland	0%	5%	5%
Portugal	10%	10%	5%
Romania	10%	10%	10%/15%
Slovak Republic	5%	0%	0%
Slovenia	0%	0%/5%	5%
Spain	0%	0%	0%
Sweden	0%	0%	0%

* The lower rate is subject to conditions.

As a mitigation measure MNCs may consider the following:

- ✓ Adjust holding company structures;
- ✓ Rethink intercompany financing and licensing structures;
- ✓ Request updated tax rulings, treaty exemption approvals, residence certificates, etc.;
- ✓ Obtain fair market value (FMV) step up for any transfer of business goodwill.

G. People

Brexit will directly impact companies and their international mobile employees including EU nationals staying and working in the UK or UK nationals staying and working in the EU. Impact will be both for expatriate assignments and short term business travelers alike.

Immigration

Within the EU the free movement of employees makes it easier for EU national employees to work in another EU country. As of the moment the UK is no longer part of the EU, this will no longer apply to UK nationals working in the EU or EU nationals working in the UK.

Even though both the UK and some EU countries are preparing for Brexit by introducing local legislation based on which individuals who are legally staying in the country before 29 March 2019 can continue to stay and work in the country with easier processes to obtain residence and work permits, companies should assess their workforce planning to guarantee they can have the right people working at the place they are needed. Not only now, but also after Brexit.

Social security

The EU regulation on social security will no longer be applicable to individuals coming from the UK or working in the UK. This may impact the social security position of the employees and self employed individuals. Either national laws or bilateral totalization agreements may help these individuals to continue their home country social security contributions in case of cross border activities. Whether or not the home country social security coverage can be continued will have a direct impact to the employer and employee on the country in which social security premiums have to be paid, current social security position for e.g. sickness and health insurance coverage and right to future benefits. A review of the impact and clear communication with the employee will help to avoid uncertainty for the employee concerned.



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Tax

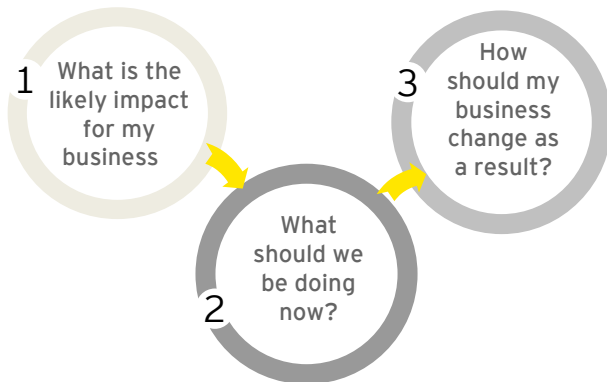
The allocation of the right to taxation for international working employees is based on bilateral agreements between countries and will therefore not be impacted by Brexit. National country specific tax rules and regulations may, however, only be available to EU nationals in order to avoid discriminatory situations and may therefore no longer be available to UK nationals after Brexit. An assessment of the impact and clear communication will help to avoid uncertainty with the employee concerned.

Transition rules

On 4 February 2019 the Dutch State Secretary of Finance published a letter in which he proposes transitional rules to be applicable in case of a no deal Brexit. The proposed transitional rules would result in the Netherlands considering the UK to be part of the EU for their national tax rules and regulations to avoid any big impacts during tax year 2019.

H. Legal

Legal considerations



Legal areas of impact

Contracts

Brexit can negatively impact and even break existing contracts. At best this negatively affects the economic value of the contract, at worst it means business disruption (lost revenue and litigation). Brexit may affect any contract whose term extends beyond 29 March 2019 (the formal Brexit date) and that relates to business or trade in or into the UK.

Provisions that should be reviewed, and taken into account when drafting new contracts which relate to business or trade in or into the UK, include: dispute resolution, governing law, territorial definitions that refer to the EU or Member States, material adverse changes, references to EU law (Treaties, Regulations, Directives), UK law based on EU law, government or other authority issued licenses, permits or authorizations, INCO terms, insurance terms and allocation of tax / customs costs. Based on the outcome of such review, it could be decided to either renegotiate and amend (the relevant provision of) the contract or, if there is ground to do so, terminate the contract in its entirety.

Due to the high chances of a hard Brexit and the limited time left until 29 March 2019, the urgency is to assess the likelihood that you will default under any of your contracts as a result of a hard Brexit, for instance due to delays by your suppliers or delays of your deliveries into the UK.

Corporate structures

In the field of Dutch corporate law, Brexit can have a number of consequences including:

Cross-border restructurings

Cross-border restructurings - such as cross-border mergers and cross-border conversions - may become impossible. Cross-border mergers and cross-border conversions are based on the 10th EU Directive (Directive 2005/56/EC) respectively ECJ case law. Following Brexit, the EU Directives and ECJ case law shall no longer apply to UK companies. Dutch corporate law does not provide for the framework to legally merge with or convert from or into a non-EU legal entity. As such, after 29 March 2019, it is likely no longer possible to implement a cross-border legal merger or conversion between the Netherlands and the UK.

EU corporate entities

European corporate entities such as the European company (SE) or the European Cooperative Society (SCE) with a seat in the UK are likely affected by Brexit. They may lose their legal basis in the UK and may have to move their seat or effect a change in legal form. On the other hand, UK legal entities may no longer be able to convert into a European corporate entity.

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EU Insolvency Regulation (EIR)

The EIR set out provisions for cross-border restructurings. Under the EIR, insolvency proceedings are automatically recognized across the EU if they are listed in Annex A to the EIR and are commenced in an EU Member State. If the UK leaves the EU without a deal, the EIR will no longer apply. UK insolvency proceedings will no longer be recognized by EU Members States. The consequences for cross-border restructurings will depend on what will be done to maintain the current arrangements with the EU.

I. How can EY help?

EY has a dedicated team of specialists to assist you through these turbulent times. We can do this in your preferred time zone and in your preferred language. We will help you analyze potential issues and will provide "best practice" solutions.

We are tracking the developments very closely, as we speak to the authorities on a very frequent basis. This allows us to keep you up to date of any new developments, opportunities or tax risks. Through our interdisciplinary approach and our strong world-wide network, we will be able to provide you an integrated approach of the Brexit challenges. This covers tax (Customs, VAT, transfer pricing and CIT), legal and people issues. In many cases we work with other external advisors (management, IT, HR, technical) and your internal business leaders to form a joint task force in order to prepare for a truly integrated supply chain transformation.

Brexit. Prepare for the worst, hope for the best!

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For more information on the above, please contact your EY advisor or any of the EY NL contacts below:

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