

Explanatory Memorandum to The Welsh Tax Acts (Miscellaneous Amendments) (EU Exit) Regulations 2019

This Explanatory Memorandum has been prepared by Office of the First Minister and Cabinet Office of the Welsh Government and is laid before the National Assembly for Wales in conjunction with the above subordinate legislation and in accordance with Standing Order 27.1

Minister's Declaration

In my view, this Explanatory Memorandum gives a fair and reasonable view of the expected impact of The Welsh Tax Acts (Miscellaneous Amendments) (EU Exit) Regulations 2019.

I have made the statements required by the European Union (Withdrawal) Act 2018. These statements can be found in Part 2 of the Annex to this memorandum.

I am satisfied that the benefits justify the likely costs.

Rebecca Evans
Minister for Finance and Trefnydd
5 March 2019

PART 1

1. Description

- 1.1. The Regulations make a number of changes to the Welsh Tax Acts arising from the UK's departure from the European Union.
- 1.2. Part 2 of these Regulations will come into force on the day after the Regulations are made. The remaining parts of these Regulations will come into force on "exit day", which section 20(1) of the European Union (Withdrawal) Act 2018 ("the Withdrawal Act") defines as 29 March 2019 at 11.00pm.

2. Matters of special interest to the Constitutional and Legislative Affairs Committee

- 2.1. This instrument is being made using the powers conferred by paragraph 1(1) of Schedule 2 to the Withdrawal Act and a selection of powers conferred by the Land Transaction Tax and Anti-avoidance of Devolved Taxes (Wales) Act 2017 ("the LTT Act").
- 2.2. The provisions contained in Parts 3, 4 and 6 are necessary to ensure the respective provisions in the LTT Act are compatible with the UK's international obligations following the UK's exit from the EU. Due to the restriction on the use of the Withdrawal Act powers (found in section 8(7)(a) of that Act), it is necessary to make these provisions using the powers conferred by the LTT Act because they may have the effect of imposing or increasing a tax liability.
- 2.3. Accordingly, this instrument is being laid in draft for approval by a resolution of the Assembly.

3. Legislative background

- 3.1. This instrument relates to the withdrawal of the United Kingdom from the European Union and is being made under paragraph 1 of Schedule 2 to the Withdrawal Act. The Minister has made any relevant statements in Part 2 of the Annex to this Explanatory Memorandum.
- 3.2. Alongside the Withdrawal Act powers the instrument is also being made under sections 18(2), 30(6), 36(8) and 78(1) of the LTT Act.
- 3.3. In accordance with section 79(2) of the LTT Act, an instrument containing regulations made under sections 18(2), 30(6) and 36(8) is subject to the affirmative procedure.

4. Purpose and intended effect of the legislation

- 4.1. **Regulation 2** – this regulation is made using the power in section 18(2) of the LTT Act. The purpose of this regulation is to update a reference in the LTT Act in relation to what is to be considered to be consideration given for a land transaction.
- 4.2. The change will ensure that the legislation is clear as to its intention not to include any obligation to transfer payment entitlements under the basic payment scheme as chargeable consideration for the grant of a lease.
- 4.3. **Regulation 3** – this regulation is made using the power in section 30(6) of the LTT Act. The purpose of this regulation is to ensure that, following the UK's exit from the European Union, all charities registered outside the United Kingdom are treated in the same manner in relation to relief from LTT under Schedule 18 to the LTT Act.
- 4.4. The effect of the amendment will mean that EU and EEA registered charities will no longer be able to claim relief from land transaction tax under Schedule 18 to the LTT Act. This will bring the treatment of EU and EEA charities in line with charities registered in other countries, therefore ensuring these provisions are compatible with the UK's international obligations, as required by section 116A(3) of the Government of Wales Act 2006.
- 4.5. It is considered that the regulation of the charities permitted to claim relief from LTT should be of a standard similar to that in the UK. Had the rules been extended to all charities wherever located in the world there would be a risk that charities established in less regulated countries and territories would be used to exploit the relief available. The relief provided to charities will therefore continue only to be available to UK-registered charities.
- 4.6. **Regulation 4** – this regulation is made using the power in section 36(8) of the LTT Act. The purpose of this regulation is to ensure that, following the UK's exit from the European Union, the LTT Act is applied in the same manner to all collective investment schemes constituted, managed and authorised outside the United Kingdom.
- 4.7. The effect of the regulation will mean that EU or EEA co-ownership authorised contractual schemes ("CoACS") which are constituted, authorised and managed under the law of an EU or EEA State will no longer receive the same treatment as a UK-based CoACS. Following the UK's exit from the European Union, only a co-ownership scheme authorised by the Financial Conduct Authority under section 261D of the Financial Services and Markets Act 2000 will receive the treatment set out in section 36 of the LTT Act.

4.8. **Regulation 5** – this regulation is made using powers in the Withdrawal Act.

Regulation 5(2)

What did any relevant EU Law do before Exit Day?

4.9. Section 4 Tax Collection and Management (Wales) Act 2016 ('TCMA') prohibits a Member of the European Parliament ('MEP') from becoming a non-executive director of the Welsh Revenue Authority ('WRA').

Why is it being changed?

4.10. As the United Kingdom will no longer be a member of the European Union on exit day, the United Kingdom will have no MEPs. It is considered highly unlikely that MEPs of other member states will apply to be members of the WRA, and as such provision is no longer required. No provision is made in relation to members of legislatures of other states.

What will it do now?

4.11. Members of the European Parliament may be appointed as non-executive members of the WRA.

Regulation 5(3)

What did any relevant EU Law do before Exit Day?

4.12. Section 65 TCMA contains a reference to EU legislation which is taken into consideration when determining the application of the unjustified enrichment rules.

Why is it being changed?

4.13. The amendment made by regulation 5(3) ensures the unjustified enrichment rules operate, in relation to EU legislation, only to the extent that the EU legislation is retained direct EU legislation (as defined by section 20 of the Withdrawal Act).

What will it do now?

4.14. The amendment ensures the unjustified enrichment rules refer to the correct body of law that will exist and have effect in the United Kingdom after exit day.

Regulation 5(4)

What did any relevant EU Law do before Exit Day?

4.15. Section 67 TCMA contains rules that permit WRA to not make a repayment of tax to a taxpayer in 8 specified situations. Case 7 is where the tax was calculated using practice generally prevailing at the time the assessment of liability was made. However, the 'practice generally prevailing' rule does not apply in cases where the tax was charged contrary to EU law, (specifically where the charge is contrary to the provisions in the Treaty on the Functioning of the European Union

which give effect to fundamental freedoms of free movement of goods, services, people and capital).

Why is it being changed?

- 4.16. Whilst the UK remains a member of the EU the Case 7 exclusion must be retained to be compatible with EU law. However, following exit day it will no longer be appropriate to provide an exclusion from the rules that permit the WRA to not make a repayment that is based in EU law.

What will it do now?

- 4.17. The amendment to the rules will ensure that the application of the Case 7 exclusion will only apply to tax charged after exit day in respect of those rights which are recognised and available in domestic law under the European Union (Withdrawal) Act 2018 and any regulations made under that Act.

- 4.18. **Regulation 6** – this regulation is made using the power in section 78(1) of the LTT Act and makes consequential amendments as a result of regulations 3 and 4.

5. Consultation

5.1. A short period of informal consultation was held with a limited number of tax experts in the charity and land transaction taxes sectors with whom a draft of the relevant regulations was shared. This informal consultation was to explore whether the changes proposed through these regulations would meet the policy intentions set out in Section 4 above (purpose and intended effect of the legislation), and to familiarise them with the intended legislation ahead of laying. As the changes are minor and technical and will impact few, if any, individuals, charities or corporate entities a wider public consultation was not considered necessary.

5.2. A minor change was considered necessary to regulation 3 as a result of the informal consultation.

PART 2 – REGULATORY IMPACT ASSESSMENT

This Regulatory Impact Assessment will address only Regulations 3 (meaning of charity), and 4 (description of a co-ownership authorised contractual scheme). The other regulations are minor or technical amendments (regulations 2 and 5), or are consequential to regulations 3 and 4 (regulation 6).

The impact of the changes effected by regulations 3 and 4 are limited. This regulatory impact assessment is therefore provided in an abridged form.

Options

The LTT Act contains rules that provide specific treatment in relation to UK charities and co-ownership authorised contractual schemes (“CoACS”). In relation to charities entering into land transactions UK, EU and EEA charities can, subject to conditions, claim relief from land transaction tax. In relation to CoACS, section 36(6) of the LTT Act affords the same treatment to EU and EEA CoACS as the provision does to UK CoACS. However, once the UK leaves the EU, it will be necessary to ensure that more favourable tax treatment is not given to entities in certain countries and not to others.

Therefore, not making regulations 3 and 4 (and therefore continuing to offer preferential treatment to EU and EEA entities) was not a realistic option as the devolved tax system must operate in a way which is compatible with the UK’s international obligations. However, two options were possible; the first to limit the treatment to UK entities alone, or the alternative to extend the treatment to entities wherever located in the world.

The first option is preferred because of the importance of regulation of the entities being given the favourable tax treatment. Had the alternative option been pursued then, by extending the rules to all such entities wherever located in the world, there would be a risk to land transaction tax revenues. That risk would come from entities established in less regulated countries and territories seeking to exploit the tax treatment when that treatment should only be available only to those regulated to the standard required in the UK.

Impact of the preferred option

The effect of these regulations will mean EU and EEA charities and CoACS will be treated in the same manner as charities and CoACS established and registered elsewhere (those established and registered in the UK will continue to benefit from the favourable tax treatment).

As a result, the regulations may have the effect of increasing or imposing tax where it previously was not imposed.

Following the UK leaving the EU, EU and EEA registered charities will no longer be able to claim relief from land transaction tax when they buy property in Wales for charitable purposes. The number of land transactions entered into by

charities from outside the UK will be very small, with potentially no such land transactions in Wales. Therefore, the consequences of this amendment are unlikely to impact on EU and EEA charities. The amendments in these regulations will have no impact on a UK charity being able to claim relief from land transaction tax where that UK charity meets the relevant conditions.

In relation to EU and EEA CoACS the position is similar to that for EU and EEA charities. Under section 36 of the LTT Act, a CoACS is treated (for LTT purposes) as though it is a company, and the rights of the participants in the CoACS as though they were shares in that company. Absent this rule the obligation to make the land transaction return and pay the tax will fall on the individual participants in the scheme. Although the effect of this regulation will not result in any additional tax being payable on the transaction, liability to pay the tax and submit the return will shift from the operator of the scheme to the individual participants. This may result in increased costs for the scheme as making land transaction tax returns may become more complex and, potentially, more expensive.

Following the UK leaving the EU those non-UK entities will no longer benefit from the treatment accorded to similar UK entities. As the EU and EEA CoACS will no longer be treated as though they are a company (and the interests of the participants treated as though they were shares in that company) this may lead to liability to land transaction tax being incurred when an interest in land owned by the participants is sold. As a result of the changes made the participants in the CoACS will be treated as holding undivided shares in the properties that are part of the scheme. Therefore, when a participant sells an interest in the scheme they will be selling the interest they own in each and every property owned within the scheme and each such land transaction will, subject to notification rules, need to be notified to the Welsh Revenue Authority.

An example is helpful to illustrate this change of treatment. An EU CoACS with 100 participants owns 10 non-residential properties (4 within Wales) worth £50 million (and each individual property is worth £5 million). One of the participants with an interest of 1% in the scheme sells their interest to another person (be they already a participant in the scheme or not). For land transaction tax purposes, the former participant is treated as selling their interest in each of the separate Welsh properties. That is, that they have entered into a land transaction to sell the 4 separate interests in the Welsh property to the new participant. The new participant will need to make a land transaction return showing the details of the 4 properties and the consideration given for the land transaction $((4 \times £5 \text{million}) \times 1\% = £200,000)$, as the sale of the interests in the individual properties form a linked transaction.

If the CoACS was a UK scheme then the continued deemed treatment of the scheme as a company, and the interests of the participants as shares, there would be no land transaction to report to the Welsh Revenue Authority.

As noted in the Explanatory Memorandum the actual effect of these changes will be small or non-existent given that there will be few if any charities registered outside the UK acquiring land and buildings in Wales. UK, EU and EEA CoACS

were only given the deemed company tax treatment under stamp duty land tax when the Finance Act 2016 came into force on 15 September 2016. This change in the rules was also associated with the introduction at the same time with a 'seeding relief' that has not been introduced in Wales in land transaction tax. It is, again, considered unlikely that there have been, or will be in the near future, many, or any, CoACS, or their participants that will be affected by these changes.

The informal consultation held with a limited number of tax experts in the charity and land transaction taxes sectors explored whether the changes proposed through these regulations would meet the policy intentions set out in Section 4 above (purpose and intended effect of the legislation). As the changes are minor and technical and will impact few, if any, individuals, charities or corporate entities a wider public consultation was not considered necessary.

Specific Impact Assessments

Equality Impact Assessment: The regulations are considered to comply with the requirements of the Equality Act 2010.

Protected Groups: The regulations are considered not to have a differential impact in relation to any of the protected groups (age, disability, gender, transgender, marriage and civil partnership, pregnancy and maternity, race, religion and belief or non-belief, sexual orientation).

Human Rights: The regulations are considered to be compatible with the Human Rights Act 1998.

United Nations Conventions on the Rights of the Child: The regulations are not considered to directly impact on children.

Impact on the Welsh Language: The regulations are considered to comply with the Welsh Language Standards.

Sustainable Development: The regulations are considered not to have a detrimental impact on sustainable development objectives.

Health and Wellbeing: The regulations are considered not to have a detrimental impact on health and wellbeing objectives.

Rural Proofing: The regulations are considered not to have a detrimental impact on rural communities.

Impact on Privacy: The regulations are considered protect individuals, companies and organisations rights

Impact on the Voluntary Sector: The UK voluntary sector will not be detrimentally impacted by these regulations. EU and EEA charities where they meet the necessary conditions, however, will no longer be in a position to claim relief from land transaction tax.

Impact on Small Business: The regulations are considered not to have a detrimental impact on small businesses.

Competition Assessment

The competition assessment does not consider the impact of these regulations on charities.

In relation to the changes made to limit tax favourable treatment to UK CoACS, competition issues will potentially arise where EU and EEA entities will no longer be afforded the same treatment as UK CoACS. The changes essentially place the EU and EEA entities in the same position as similar entities elsewhere in the world. Any competition issues that arise are therefore not between UK entities, but rather between the UK and the rest of the world, now to also include the EU and EEA as a result of the UK leaving the EU.

Post Implementation Review

The LTT Act places a statutory obligation on the Welsh Minsters to make arrangements that an independent review of LTT is conducted before the end of 6 years following the date on which the Act received Royal Assent. That review must therefore be completed by 25 May 2023.

However, no specific requirements are considered necessary to specifically conduct a post implementation review for the changes made through these regulations.

Annex A

Statements under the European Union (Withdrawal) Act 2018

Part 1

Table of Statements under the 2018 Act

This table sets out the statements that may be required of the Welsh Ministers under the 2018 Act. The table also sets out those statements that may be required of Ministers of the Crown under the 2018 Act, which the Welsh Ministers have committed to also provide when required. The required statements can be found in Part 2 of this annex.

Statement	Where the requirement sits	To whom it applies	What it requires
Sifting	Paragraphs 3(7) and 4(3), Schedule 7 <i>Paragraph 3(7) (anticipated to be a requirement on Welsh Ministers in Standing Orders)</i>	The Welsh Ministers exercising powers in Part 1 of Schedule 2 to make a Negative SI Paragraph 3(7) applies to Ministers of the Crown, but Welsh Ministers have committed to make the same statement	A statement to explain why the instrument should be subject to the negative procedure and, if applicable, why they disagree with the recommendation of the CLA Committee (as sifting committee)
Appropriateness	Sub-paragraph (2) of paragraph 28, Schedule 7	Applies to Ministers of the Crown exercising powers in sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2. Welsh Ministers have committed to make the same statement when exercising powers in Schedule 2	A statement that the SI does no more than is appropriate.
Good Reasons	Sub-paragraph (3) of paragraph 28, Schedule 7	Applies to Ministers of the Crown exercising powers in sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2. Welsh Ministers have	A statement to explain the good reasons for making the instrument and that what is being done is a reasonable course of action.

		committed to make the same statement when exercising powers in Schedule 2	
Equalities	Sub-paragraphs (4) and (5) of paragraph 28, Schedule 7	Applies to Ministers of the Crown exercising powers in sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2. Welsh Ministers have committed to make the same statement when exercising powers in Schedule 2	<p>A statement to explain what, if any, amendment, repeals or revocations are being made to the Equalities Acts 2006 and 2010 and legislation made under them.</p> <p>A statement that the Minister has had due regard to the need to eliminate discrimination and other conduct prohibited under the Equality Act 2010.</p>
Explanations	Sub-paragraph (6) of paragraph 28, Schedule 7	Applies to Ministers of the Crown exercising powers in sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2. Welsh Ministers have committed to make the same statement when exercising powers in Schedule 2	A statement to explain the instrument, identify the relevant law before exit day, explain the instrument's effect on retained EU law and give information about the purpose of the instrument, e.g. whether minor or technical changes only are intended to the EU retained law.
Criminal offences	Sub-paragraphs (3) and (7) of paragraph 28, Schedule 7	Applies to Ministers of the Crown exercising powers in sections 8(1), 9 and 23(1) or jointly exercising powers in Schedule 2. Welsh Ministers have committed to make the same statement when exercising powers in Schedule 2	A statement setting out the 'good reasons' for creating a criminal offence, and the penalty attached.
Sub-delegation	Paragraph 30, Schedule 7	Applies to Ministers of the Crown exercising powers in sections 8(1), 9 and paragraph 1 of Schedule 4 to create a legislative power exercisable not by a Minister of the Crown or a Devolved Authority.	A statement to explain why it is appropriate to create such a sub-delegated power.

		Welsh Ministers have committed to make the same statement when exercising powers in Schedule 2 or paragraph 1 of Schedule 4 to create a legislative power exercisable not by a Minister of the Crown or a Devolved Authority	
Urgency	Sub-paragraph (2) and (8) of paragraph 7, Schedule 7	Welsh Ministers exercising powers in Part 1 of Schedule 2 but using the urgent procedure in paragraph 7 of Schedule 7	A statement that the Welsh Ministers are of the opinion that it is necessary to make the SI using the urgent procedure and the reasons for that opinion.

Part 2

Statements required when using enabling powers under the European Union (Withdrawal) 2018 Act

The statements below apply to the changes made using the powers under the European Union (Withdrawal) Act 2018, namely Part 5 of the regulations. The other regulations are made using powers within the Welsh Tax Acts and such statements in relation to those regulations are not required.

1. Sifting statement(s)

Not applicable.

2. Appropriateness statement

The Minister for Finance and Trefnydd, Rebecca Evans has made the following statement regarding use of legislative powers in the European Union (Withdrawal) Act 2018:

“In my view The Welsh Tax Acts (Miscellaneous Amendments) (EU Exit) Regulations 2019 does no more than is appropriate.

This is the case because the regulations are technical in nature and designed to address failures of retained EU law to operate effectively after exit day.”

3. Good reasons

The Minister for Finance and Trefnydd, Rebecca Evans has made the following statement regarding use of legislative powers in the European Union (Withdrawal) 2018 Act:

“In my view there are good reasons for the provisions in this instrument, and I have concluded they are a reasonable course of action. This is because the instrument makes a number of minor technical changes to the Welsh Tax Acts to reflect the UK’s departure from the EU.”

4. Equalities

The Minister for Finance and Trefnydd, Rebecca Evans has made the following statement:

“The draft instrument does not amend, repeal or revoke a provision or provisions in the Equality Act 2006 or the Equality Act 2010 or subordinate legislation made under those Acts.”

The Minister for Finance and Trefnydd, Rebecca Evans, has made the following statement regarding use of legislative powers in the European Union (Withdrawal) Act 2018:

“In relation to the draft instrument, I, Rebecca Evans, have had due regard to the need to eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under the Equality Act 2010.”

5. Explanations

The explanations statement has been made in paragraph 4 (Purpose & intended effect of the legislation) of the main body of this explanatory memorandum.

6. Criminal offences

Not applicable.

7. Legislative sub-delegation

Not applicable.

8. Urgency

Not applicable.