SLAUGHTER AND MAY/

TAX NEWS

PODCAST

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Zoe Andrews	Welcome to the July 2025 edition of Slaughter and May's "Tax News" podcast. I am Zoe Andrews, Head of Tax Knowledge. This podcast is later than usual because, in late June, there was a special episode on the One Big Beautiful Bill with Arvind Ravichandran, partner at Cravath, Swaine & Moore LLP. But we'll get back to that when we speak about Pillar Two. Tanja, over to you.
Tanja Velling	I am Tanja Velling, Tax Knowledge Counsel. Lots of important decisions have been handed down. In this podcast, Zoe and I will discuss the Supreme Court's decision in *Dolphin Drilling*, the Court of Appeal's decisions in *Haworth* and *Marlborough DP*, the Upper Tribunal's decision in *Osmond* and the First-tier Tribunal's decision in *Eastern Power Networks* (although not in that order). We'll also cover IP onshoring and cost contribution agreements, the government's new tax policy making principles, VAT news in relation to occupational pension schemes and what's next for Pillar Two. One important development that we aren't going to cover in detail is L-day. On the 21st of July, draft legislation for the next Finance Bill was published, including, as previously announced, to bring carried interest within the income tax regime, to charge inheritance tax on pension pots and to reduce inheritance tax reliefs on agricultural and business property (including AIM shares). There are also further changes to the multinational and domestic top-up tax legislation and a regulation-making power to introduce a standing reporting obligation for interest and credit card sales data. If we spot any points we want to highlight, we'll get back to you in the next episode! This podcast was recorded on the 29th of July 2025 and reflects the law and guidance on that date.
Zoe Andrews	Let's start off with a POEM. Unfortunately, not my favourite W.H. Auden poem, "Foxtrot from a play" or as I tend to remember it "You're my cup of tea", but the *Haworth* case on the interpretation and application of the place of effective management test, or POEM, in the context of the residence tie-breaker provision in the UK/Mauritius tax treaty. Although on the facts of this case, POEM was considered for the purpose of determining the residence of a trust, much of the reasoning of the Court of Appeal could apply equally to the determination of the treaty residence of a company. In order for a capital gains tax avoidance "round the world" scheme to work, the taxpayers in *Haworth* needed the POEM of the trustees of the family trusts to be in Mauritius at the time the

	trust disposed of certain shares. The POEM, argued the taxpayers, flipped from the UK to Mauritius and back to the UK during the course of the scheme. But the Court of Appeal disagreed. All three of the First-tier Tribunal, Upper Tribunal and Court of Appeal followed the approach in *Smallwood* and found in favour of HMRC that the scheme failed to achieve its objective and CGT is payable: the FTT was correct in its approach to determining the POEM of the trust to be in the UK throughout. Although trustees were appointed in Mauritius with the intention of making the trusts resident there, the trustees' role was to make the disposal as part of the scheme which was devised and run from the UK by the settlors and their UK advisers which meant that the POEM of the trust throughout the scheme was the UK.
Tanja Velling	How is the POEM test different to the CMC – central management and control - test which is applied under UK domestic law to determine whether a company is resident in the UK or not?
Zoe Andrews	The CMC test as articulated in *Wood v Holden*, looks to the place in which binding decisions are made by the authorised decision-making body, unless that function has been usurped. It is a purely factual question and is usually where the board of directors make key decisions. There can be more than one place of CMC (as a company may, I quote, "keep house and do business" in more than one place) but there can only be one POEM, as it is the purpose of the treaty tie-breaker to determine one place of residence. The POEM test looks at "realistic, positive management" or "real top-level management" which allows matters to be looked at more broadly than for CMC. Where there is a scheme such as in *Haworth*, POEM is to be determined by looking at the circumstances in which the scheme was devised and implemented. In *Haworth*, this included considering the reason for the Mauritis trustees being appointed and the fact their role was pre-determined to further an "overall single plan". The Court of Appeal concluded: "The Mauritius Trustees were (without impropriety) playing their parts in a script which had been written by others". The POEM test does not take a snapshot approach looking only at the moment of disposal but looks at whether there is a scheme of management going above and beyond the day-to-day management of the decision-makers for the time being.
Tanja Velling	Is POEM still relevant post-BEPS considering the UK has in many treaties embraced a move away from the POEM tie-breaker towards the Competent Authorities mutually agreeing the place of treaty residence?
Zoe Andrews	Yes. Even for treaties where the tie-breaker has been changed, POEM should continue to be relevant as one of the factors likely to be taken into account by the Competent Authorities (and it appears in HMRC's list in the International Manual of factors the UK Competent Authority would take into account when deciding their view on residence).
Tanja Velling	Given the similarities with the *Smallwood* round the world scheme, *Haworth* looks like a strong contender for the follower notice regime doesn't it, but I recall the Supreme Court already put a stop to that?

Zoe Andrews	Well remembered! HMRC had attempted to speed up the process of recovering the tax with a follower notice and accelerated payment notice in 2016, but the notices were quashed in a judicial review claim in which the Supreme Court in 2021 described the follower notice regime as "draconian". One of the conditions HMRC had to satisfy was to show that *Smallwood* is a "relevant ruling" for the purpose of Mr Haworth's arrangements. HMRC had to show that they had formed the opinion that the principles laid down, or the reasoning given, in the *Smallwood* decision would, if applied to the arrangements of Mr Haworth, deny all or part of the tax advantage he asserted. The question for the Supreme Court was what degree of certainty was required to satisfy this condition. The Supreme Court said that you had to interpret the word "would" restrictively (to produce minimum interference with the taxpayer's right to justice). This interpretation meant requiring HMRC to form the opinion that there is no scope for a reasonable person to disagree that the earlier ruling denies the taxpayer the advantage. HMRC accepted that they had only formed the opinion that it is "likely" that the application of *Smallwood* would deny the tax advantage to the taxpayer. This did not meet the strict requirements for a follower notice to be issued.
Tanja Velling	That gives some reassurance to taxpayers on the scope of the follower notice regime. But can we have a quick chat about the Supreme Court's decision in *Dolphin Drilling*? I remember you getting excited when we spoke about the Court of Appeal's decision that the case could have wider implications beyond the narrow meaning of "incidental" for the purposes of the hire cap under the oil contractor regime. In particular, we wondered whether the discussion of the meaning of "incidental" would be picked up in other tax contexts, such as in the application of the purpose test in a double tax treaty, or whether a purpose is a "main purpose" under the unallowable purpose test in the loan relationship rules (in section 441 of the Corporation Tax Act 2009).
Zoe Andrews	The taxpayer thought it had wider implications too; indeed, in order to get permission to appeal to the Supreme Court, the taxpayer argued that the case raised a point of law of general public importance because of the frequency of the use of the words "incidental to" in other taxing statutes. The Supreme Court, however, emphasised that the decision is based on the facts of this case and the specific statutory context, so it has turned out not as interesting to us as I had previously thought! Although the general point about giving the words "incidental to another use" their ordinary meaning may be helpful in other contexts.
Tanja Velling	Let's move on to *Osmond* where the Upper Tribunal agreed with the taxpayers that the transactions in securities (or TIS) rules had not been triggered. In particular, the Upper Tribunal decided that the taxpayer did not have a main purpose of obtaining an income tax advantage. The case was about preserving Enterprise Investment Scheme (EIS) disposal relief. The taxpayers had made successive EIS investments over a 30-year period and were concerned that a change of government might result in the relief from capital gains tax no longer being available and so they decided to trigger a disposal. As there was no third-party buyer, share buybacks totalling £20 million were used to effect the disposal. The FTT found as a fact that the taxpayers' main purpose of being party to the share buybacks was to crystallise EIS relief. The FTT then decided this finding automatically "as a matter of

	remorseless statutory logic" meant the taxpayers had a (deemed) main purpose of generating an income tax advantage. The FTT essentially accepted HMRC's argument that, if your purpose is to get a CGT relief, your purpose must include bringing the transaction within the CGT regime (and keeping it outside of the income tax regime), so you necessarily have a purpose of getting an income tax advantage (by being within scope of CGT (subject to any reliefs) rather than income tax).
Zoe Andrews	It seems quite a leap to say you have a purpose of obtaining a CGT relief and so you must also have a purpose of not paying income tax, doesn't it?
Tanja Velling	Yes. The Upper Tribunal agreed with you. They applied *BlackRock* to find that the FTT had erred in law in concluding that the purpose of obtaining a CGT relief necessarily constituted a main purpose of obtaining an income tax advantage. The income tax advantage was an effect or consequence but not a main purpose.
Zoe Andrews	As with every main purpose test, the facts are key, and it is interesting here that the UT hints that perhaps the FTT's findings of subjective intention were "generous to the taxpayers". The FTT had found that extraction of value from the company was not a purpose of the share buyback, the sole purpose was to crystallise the CGT relief. Let's now turn to a case on disguised remuneration, *Marlborough DP*, where the Court of Appeal upheld the Upper Tribunal's decision in favour of HMRC. What was the factual background again?
Tanja Velling	Dr Thomas ran a dental practice through a limited company, Marlborough DP. He entered into a tax avoidance scheme and, under that scheme, Marlborough DP paid an amount equal to its profits to a trust and the trust made loans to Dr Thomas. The idea here was that Marlborough DP would get a corporation tax deduction for the payments to the trust – so reducing its taxable profits to nil – and the loans to Dr Thomas would not be subject to either income tax or national insurance contributions. I suppose it is unsurprising that HMRC challenged this, and the Court of Appeal has now upheld the Upper Tribunal's conclusion that the loans were taxable for Dr Thomas under the loan charge in Part 7A of the Income Tax (Earnings and Pensions) Act 2003 and that Marlborough DP cannot get any corporation tax deductions. Whether or not the loans were subject to tax under Part 7A essentially turned on the meaning of "in connection with" – were they a means to provide rewards in connection with Dr Thomas' employment? Similarly to the Supreme Court in *Dolphin Drilling* in relation to the word "incidental", the Court of Appeal considered that "in connection with" is a versatile phrase that takes its meaning from the statutory context. This necessarily means that the way judges described (or paraphrased) the degree of connection required where that phrase is used in other statutory contexts is of limited use. In Part 7A, "in connection with" denotes a link that falls short of the causality required by phrases such as "by reason of" as used in ITEPA in the benefits code.
Zoe Andrews	On corporation tax deductions, the central question was whether the payments were "wholly and exclusively" for the purposes of Marlborough DP's trade. Two interesting points here. The first is that the Court of Appeal noted a tension between two of its earlier decisions: *Vodafone Cellular* which treated this as a question of fact and *Investec Asset Finance* which referred to it being a

	question of law. That categorisation is generally important given that appeals from the First-tier Tribunal are limited to questions of law; findings of fact can only be appealed on *Edwards v Bairstow* grounds, that no reasonable Tribunal could have made that finding on the evidence. Here, the categorisation didn't matter in the end because – rather unusually – the Court of Appeal considered that an *Edwards v Bairstow* challenge had been made out. Unfortunately, this also means that the potential tension between the *Vodafone* and *Investec* Court of Appeal decisions was not resolved.
Tanja Velling	How was the *Edwards v Bairstow* test met here?
Zoe Andrews	Quite unusually, at the FTT, the judge and Tribunal member had disagreed on "wholly and exclusively". The Tribunal member thought the test had been failed on the facts. In contrast, the judge considered it had been met – but the reasoning here was basically that, if the amounts are taxable under Part 7A, it logically followed that the payments were for Marlborough DP's trade because they were a reward for Dr Thomas' work. That's all quite unusual. So, the Court of Appeal's decision should by no means be taken to imply that *Edwards v Bairstow* challenges may be more readily accepted by the courts; they are very hard to make out – which is why it is key to put your best factual foot forward (so to speak) before the FTT.
Tanja Velling	It was also interesting that the Upper Tribunal didn't actually refer to *Edwards v Bairstow*; it was the Court of Appeal that interpreted the Upper Tribunal's decision as meaning that the Upper Tribunal had thought such a challenge had been made out. Anyway, shall we move on to the First-tier Tribunal's decision in *Eastern Power Networks*?
Zoe Andrews	This is a consortium relief case and a cautionary tale; had there been no structuring, the joint venture could have used one of the partner's losses against 40% of its profits. Instead, the FTT concluded that an anti-avoidance provision applied to cut that in half. But first things first – where does that 40% number come from? Well, the proportion of profits against which losses can be used is determined as the lowest of a JV partner's share in the economics, ordinary share capital and voting rights. Here, the commercial deal was that the relevant JV partner was entitled to 40% of the economics but held close to 100% of the ordinary shares and just shy of 75% of the voting rights. The argument advanced on behalf of the taxpayers was that the lowest proportion here was the voting rights.
Tanja Velling	How did that argument work when you've just said that they were entitled to 40% of the economics?
Zoe Andrews	Well, the interest in the JV group was held through a stack of three link companies each of which held an interest in the JV. Very broadly, the taxpayers argued that, on the wording of the legislation, this essentially required the economic entitlement to be counted several times so that you'd get to over 100%, and that would make the just under 75% of voting rights the lowest proportion. The FTT disagreed; the "statutory purpose is to arrive at a genuine, "real world" proportion" [of the economics] which was 40%.

Tanja Velling	And how do you then get to half of that?
Zoe Andrews	That's the effect of applying the anti-avoidance rule in section 146B of the Corporation Tax Act 2010. Following an earlier Court of Appeal decision, it was common ground that there were arrangements to prevent the link companies from controlling the JV. These arrangements took the form of a provision in the JV's articles requiring a 75% majority on any resolution of the JV. The remaining question before the FTT was then whether these arrangements formed part of a scheme with a main tax avoidance purpose. The FTT concluded that that was the case; an interesting point here is that the FTT found the "scheme" to be the corporate structure of the JV.
Tanja Velling	So, it seems that, when you're thinking about a scheme, that isn't necessarily always a transaction or series of transactions, but it could also be something that could be better described as a state of affairs. That's quite interesting. We should also note that the Supreme Court granted permission to appeal in two cases we previously discussed: in *ScottishPower* on the deductibility of payments in lieu of penalties and in *Gunfleet Sands* concerning capital allowances on preparatory costs of infrastructure projects. The taxpayer in *Beard* also applied for permission to appeal to the Supreme Court; given that he lost before the First-tier and Upper Tribunals and the Court of Appeal (with each agreeing that the relevant distributions were dividends of an income nature based on the earlier case of *First Nationwide*), it seems questionable whether PTA will be granted.
Zoe Andrews	That's quite enough on cases now so let's look at some other developments, starting with HMRC's guidance on the new clearance system for cost contribution arrangements (CCAs). CCAs are contractual arrangements for MNEs to share the costs and risks of developing assets such as intellectual property. HMRC has taken a different view from other tax authorities as to when a CCA can be an acceptable pricing mechanism under the OECD's Transfer Pricing Guidelines. HMRC's view has been that for a CCA relating to IP to be an acceptable pricing mechanism, the UK entity must also employ the functions which control risks associated with that IP. This has resulted in significant enquiry activity and in recognition of the problem this is causing for business, the corporate tax roadmap promised that the government would review the treatment of CCAs and explore a solution.
Tanja Velling	The solution is that clearance will be offered on the treatment of CCAs through unilateral Advance Pricing Agreements (APAs) using existing legislation. HMRC has published guidance at INTM422160 explaining the new APA programme and setting out the conditions to be satisfied for the clearance to be granted. A sample CCA APA is published at INTM422170. The guidance sets out (in paragraph 16) four things that an expression of interest in a CCA APA would need to cover. As expected, these include a narrative explanation of why the business considers the CCA to be commercially viable over the proposed term of the APA at the point of applying for the APA.

Zoe Andrews	Now for some more good news – in Revenue & Customs Brief 4 (2025), HMRC announced a new policy on the VAT deductibility of investment costs and administration costs linked to occupational pension funds. This was a bit of a surprise wasn't it?
Tanja Velling	Yes, it was. According to the Brief (which was certainly very brief), subject to the normal deduction rules, employers can claim back all the VAT on investment costs linked to occupational pension funds (as well as all administration costs) and no longer need to split the costs with pension trustees. Trustees that are VAT registered providing pension fund management services and charging the employer can also claim the input tax on their costs, subject to the usual VAT rules.
Zoe Andrews	This is certainly a lot simpler, and more generous than the previous policy that in some circumstances viewed investment costs as being subject to dual use by an employer and the trustees and required complex apportionment of such costs between the employer and trustee. From when does it apply?
Tanja Velling	It has applied since the 18th of June 2025, and it is subject to the normal four-year cap for claims for additional input tax. HMRC will publish guidance explaining the policy change by Autumn 2025. Speaking of tax policy – what are the new "Tax Policy Making Principles"?
Zoe Andrews	The government reiterated its commitment to having only one major fiscal event each year, but it is going to take a more flexible approach to consultations on policy and draft legislation. We would expect that, in practice, this may mean more of a drip-feed of consultation documents than having a large number published on the same day (which may well make responding more manageable). Whilst L-day will be maintained (as we have seen), draft legislation may also be published at other points in the year. The principles also indicate that different forms and durations of consultation may be used for different policy proposals; we would expect that this is largely an acknowledgement of the ongoing informal consultations that take place between the government, tax advisers and business through various channels.
Tanja Velling	No podcast is complete without a look at what's next for Pillar Two (the global minimum tax rules). When we recorded the podcast with Arvind Ravichandran on the One Big Beautiful Bill, we were still concerned about U.S. retaliation for UTPR implementation in the form of a new section 899, but Arvind told us that it would be unlikely in practice for the UTPR to trigger retaliatory measures under that section. And how right he was – shortly after the podcast was published, the G7 published an understanding on effectively a carve-out of U.S. groups from Pillar Two and section 899 was dropped from the One Big Beautiful Bill.
Zoe Andrews	"Effectively a carve-out" isn't quite the language used by the G7, though, is it?
Tanja Velling	No, the statement speaks of a two-system approach where the U.S. minimum tax rules (GILTI – now officially renamed "net CFC tested income" but I expect people will still call it GILTI) operate

	alongside the Pillar Two rules (taking U.S. parents and their domestic and foreign subsidiaries out of the IIR and UTPR rules). So, U.S.-parented groups are to be taken outside Pillar Two but it appears that the U.S. operations of non-U.S. parented groups would remain within the scope of Pillar Two (whether as a result of the IIR or the UTPR). QDMTTs should be unaffected. Another interesting point is the reference to a "greater alignment" between the treatment of substance-based non-refundable tax credits and refundable tax credits. This seems to hint at a potential improvement of the Pillar Two treatment of certain US tax credits, but we'll have to wait and see. What are some of the concerns about how this two-system approach will work?
Zoe Andrews	Although the section 899 U.S. withholding tax risk has gone away for now, a permanent solution needs the agreement of the OECD Inclusive Framework (which has 140+ members) and there are a number of concerns. If the OECD cannot reach agreement to implement this two-system approach, the U.S. has made it clear there would be some kind of U.S. retaliation. But the main concern is that the two-system approach could give U.S.-parented groups a competitive advantage as the GILTI rules are not fully aligned with the Pillar Two rules and are arguably more lenient; some companies would undoubtedly be better off under the U.S. system. There is a need to address substantial risks with respect to having a level playing field and BEPS. There are also concerns about how the two-system approach could be given effect in the EU and whether the EU Directive would have to be amended. Some countries have voiced the opinion that they want to abandon Pillar Two if it does not apply to the US. What is the latest from the OECD on the implementation of Pillar Two? Are we expecting any more Administrative Guidance?
Tanja Velling	Administrative Guidance takes a long time to agree and progress on Administrative Guidance has paused (some Administrative Guidance is time limited anyway, like the UTPR safe harbour guidance). There is now a move towards a committee of experts from implementing tax authorities (referred to as the "Amsterdam Dialogue", organised through the Forum on Tax Administration) to agree interpretative issues (where necessary, questions could also be referred to Working Party 11 of the Inclusive Framework). Where this expert group agrees on an approach, this would not have the same status as Administrative Guidance (because it would not have been agreed by all Inclusive Framework members) and it is unlikely to be published, for example, by the OECD, but we would expect it to feed into HMRC guidance.
Zoe Andrews	It's also worth mentioning that there is going to be a permanent safe harbour – a simplified Effective Tax Rate safe harbour – to reduce the administrative burden of applying Pillar Two. This may look like the current temporary country-by-country reporting safe harbour without relying on CbCR data (which was, of course, never intended for this purpose). It may be supported by a de minimis test. We understand that the UK government is keen to get this safe harbour agreed. On the UK's implementation of Pillar Two (in addition to draft legislation published on L-day making further tweaks to the multinational and domestic top-up taxes), HMRC published a

	response to the consultation on the draft MTT and DTT guidance; HMRC expect to publish the guidance as a manual shortly although it will still be work in progress and will be amended from time to time. As we predicted in the May edition of this podcast, the regulations which set out certain lists of qualifying territories and taxes have already been updated.
Tanja Velling	Now, in terms of what there is to look forward to – well, all I really have to say is a summer break, although I suspect that, like us, you may be spending part of August digesting the draft legislation published on L-day. In any event, the podcast is taking a break until September, so we hope you have a lovely August and thank you for listening. If you have any questions, please contact Zoe or me, or your usual Slaughter and May contact. Further insights from the Slaughter and May Tax department can be found on the European Tax Blog – www.europeantax.blog

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