UK Freeports – The Tax Angle

On Wednesday 7 October 2020, the UK government published the Response document to the Freeports Consultation that was originally launched in February 2020.

The creation of freeports is a flagship policy for the UK government. It touches on so many of the government's core aims and objectives. In microcosm, the freeports ideal provides a sketch of the UK's vision of its post-Brexit identity as a Global Britain, championing globalisation and free trade. At the same time, the freeports policy is inward looking. It seeks to help remodel the UK economy outside of the EU, to "level up" economic prosperity across the whole country, support the Northern Powerhouse and create centres that support and spur innovative new businesses. Freeports could also prove to be a measure of the UK's attempt to be free to provide generous, targeted, state aid outside of the constraints of the EU (and the willingness of the EU to respond, should it feel the need). In sum, freeports, strongly advocated by the Chancellor of the Exchequer, Rishi Sunak, lie at the heart of the government's plans to remake the UK economy at a time when it grapples with the triple economic threat resulting from the COVID-19 pandemic, Brexit disruption and climate change.

The ultimate success of freeports will depend on the effectiveness of a combination of multiple strands of both central government and devolved authority policy initiatives and industrial strategies. By necessity, freeports are local and specific in nature. The consultation covered diverse topics, including planning, regeneration, innovation and controlling illicit abuse. However, ultimately, at its core, a freeport is defined by its tax and customs offering.

Unfortunately, the Response document provides few specific details on exactly what that tax and customs offering will be. It does, however, outline what will (and, just as important, what will not) be available. In broad terms, UK freeports will benefit from a medley of "long-term" (undefined but, ultimately, time-limited) tax and customs incentives. In brief, these include:

- **Value Added Tax (VAT)** – Import VAT will be suspended. In combination with Postponed VAT Accounting (PVA), this should not only create cash flow advantages, but also reduce the administrative and compliance burden on freeport businesses.
- **Customs** – Freeport businesses bringing goods into a freeport customs site will be able to claim duty deferrals, duty exemptions and duty inversion. Customs procedures are expected to benefit from certain administrative simplification and facilitation but will need to comply with the UK's 2025 Border Strategy. Businesses should expect (and should be ready to adopt) some form of digital technological processes.
- **Business rates** – Businesses operating in a freeport will benefit from business rates relief on their premises.
- **Capital allowances** – A key object for freeports is to encourage capital expenditure. To encourage businesses to invest, the government will offer Enhanced Capital Allowances and an enhanced, freeports-specific, Structures and Buildings Allowance (SBA) for businesses in a freeport tax site.
- **Stamp Duty Land Tax (SDLT)** – Commercial (non-residential) land and property transactions within a freeport tax site will benefit from a relief from SDLT. It is unclear whether this will take the form of a reduced rate or an exemption.
- **Employer National Insurance Contributions (NIC)** – The government hopes that freeports will promote the creation of high-skilled jobs. To help businesses reduce the cost of employment, employing businesses located in a freeport tax site will be entitled to a relief from employer NIC in relation to eligible employees based in that site.
- **Administrative facilitation** – The government has promised to ensure tax incentives are readily available and can be claimed quickly and easily. Again, no details are currently available, but businesses should expect (and should be ready to adopt) some form of digital technological processes.

Almost inevitably, businesses should expect the incentives to be accompanied by robust anti-avoidance measures. The UK government is alive to the criticism that freeports can facilitate illicit activity, and will be keen to demonstrate that the reliefs they offer are targeted, effective and claimed legitimately. The danger, of course, is that ineffective anti-abuse provisions that restrict the scope of the incentives too much, or impose too many pre-conditions, could have an equally detrimental effect. The detail will need careful consideration.

Despite the emphasis on creating "dynamic environments, capitalising on new ideas and fostering the conditions that will attract new businesses, investors and innovations", the government has decided that it will not offer a specific research and development (R&D) tax incentive in freeports. This is possibly surprising, but might be explained by the publicised concern that the R&D credit regime has been the subject of widespread abuse. It will be interesting to see how, if at all, the government's thinking on how to use the tax system to enhance innovation and digital technologies evolves in the coming months in relation to freeports and more generally.

Finally, it is also worth noting that the UK's tax policies for freeports are limited to those businesses operating in the freeport. They do not, for example, make any provision for incentivised investment in the freeport businesses themselves. In the US, opportunity zones are similarly defined geographic places where certain tax-incentivised investments can be made. There is nothing, currently, to suggest the government has considered adopting something similar in the UK. Again, how the UK develops its investment incentive regimes in the short and medium term is likely to be something worth tracking.

Full details of the special freeports tax and customs rules will be included in the Bidding Prospectus, which is expected to be published in the coming weeks. The bidding process should then formally open before the end of 2020. The first freeport in England should be open for business by the end of 2021.

Will freeports allow the UK to "sail onto [its] next, great, prosperous destination"?

With the UK simultaneously negotiating multiple new free trade agreements, freeports could make a significant contribution to making the UK's post-Brexit economic and trade policy truly global. The government will look to use freeports to advertise the opportunities Brexit has provided. It will seek to ensure that the policy delivers on advantages previous studies have suggested it can bring, including, for example, the ability to catalyse regions, stimulate economic regeneration, boost multimodal connectivity and create highly skilled jobs in new sectors.

Many will welcome the government's confirmation that it will pursue its freeports policy. Some, however, may be slightly underwhelmed by the level of ambition and creativity it sets out. Ultimately, the success of the policy is likely to depend on how closely a freeport's incentives can be targeted at, and aligned with, local industrial strategies and needs.

Whether the UK's freeports will be as transformative as the government hopes, and do not simply dislocate existing activity attracted by the tax and regulatory incentives, will depend on the scope, flexibility and accessibility of the detailed package in the Bidding Prospectus.

We will, of course, share further details on the mechanics of freeports, tax incentives and state aid implications, as and when they become available.

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