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On the Post Brexit, do the new VAT rules violate the VAT principles and leads agents to perform VAT avoidance?

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## **Thanks**

The realization of this thesis was one of the biggest challenges I have faced in my life, giving the complexity of the theme, and considering that there is not much literature around it. Although I have faced times where I wanted to give up on this, especially on the last month of its realization, I kept continuing and I ended being proud of its result.

I would like to thank firstly my family for supporting me during my student journey, especially my parents who since the beginning of my student career have always believed in my capacities and let me choose my own pattern on the professional world.

Secondly, I want to thank my friends who not only support me and gave me the accurate advice on the hardest times, but also understood the times I had to give up on group dinners or parties in order to finalise my thesis.

Thirdly, I would like to thank the company which I work for, Ryan, where I am able to learn a lot from VAT everyday and who were very flexible on the days I had to leave work earlier to assist classes or work on my thesis. Additionally, I want to also thank my colleagues at Ryan who I work directly with who were so understandable and who help me finding issues they have faced with Brexit since January 2021.

Lastly, I want to thank my mentor Tomás Cantista Tavares, for him availability to do meetings whenever I needed, to help me guiding through my investigation and realisation of the thesis, and to always make me believe this thesis was possible to be done giving all the challenges I have facing on the process. Additionally, I would like also to thank professor Miguel Correia who was able to give me additional bibliography and shared him knowledge with me on this topic, which was crucial to end with this good result.

## Resumo

Esta tese tem como foco estudar como o Brexit impactou a regularização da movimentação de bens entre a UE e o RU, depois de 1 de Janeiro de 2021. O principal objetivo é concluir quais são as novas regras do IVA aplicáveis às transações de bens entre a UE e o RU, como é que isso impacta o comportamento dos agentes da UE e do RU, se as novas leis criadas violam os princípios do IVA; e se existem formas de os agents, legalmente, praticarem evasão do IVA quando importam da UE/RU para o RU/UE. Em termos gerais, consegui concluir com esta tese que apenas um dos três objetivos do Brexit Trilemma foi atingido, no entanto tal aconteceu por violação do princípio da neutralidade do IVA. Adicionalmente, fui também capaz de concluir que o Protocolo criou uma forma de os bens passarem da UE para a GB pela IN sem pagar IVA em qualquer fase.

A literatura disponível sobre o assunto foi muito difícil de encontrar tendo em conta que, em primeiro lugar, considerando que este é um tópico muito recente, os agentes de IVA e os especialistas em IVA ainda têm bastantes dúvidas em perceber quais são as regras aplicáveis em cada caso (o que naturalmente, faz com que não escrevam ainda muito sobre isso) e, em segundo lugar, tal implica ler várias leis de forma a perceber como é que o IVA funciona em cada transação entre a UE, GB e IN. Tendo isto em conta, a minha tese foi feita principalmente lendo o que é referido no site do HMRC sobre o tópico, lendo o VATA 1994 nas secções relacionadas com o Brexit e lendo a Diretiva do IVA. Adicionalmente, encontrei também um livro bastante completo “The Law and Practice of the Ireland-Northern Ireland Protocol” e uma tese feita por um estudante Italiano neste assunto “A Tax Perspective on Brexit: which consequences on VAT and Customs Procedures?”, que me ajudaram a confirmar se o meu entendimento da lei estava correto.

A investigação terminou dia 16 de Fevereiro de 2023, o que significa que quaisquer leis criadas depois dessa data não foram consideradas nesta tese.

Palavras-chave: IVA; Brexit; Protocolo da Irlanda-Irlanda do Norte; princípio da neutralidade

## **Abstract**

This thesis focuses on study of how Brexit impacted the VAT regulation of the trade of goods between EU and UK, after 1<sup>st</sup> January 2021. The main objective is to conclude what are the new VAT rules applicable for the transaction of goods between EU and UK, how it impacts the consumption behaviour of EU and UK agents, if the new laws created violate the VAT principles and if there are ways where agents could, lawfully, perform VAT avoidance when importing from EU/ UK to UK/EU. In general terms, I was able to conclude with this thesis that only one of the three goals of the Brexit Trilemma was achieved, however it was done by violating the neutrality principle of VAT. Additionally, I was also able to conclude that the Protocol created a way of passing the goods from EU to GB through NI without paying VAT at any stage.

The available literature on the subject was very hard to find since firstly, considering that this is a very recent subject, the VAT agents and VAT specialist still have a lot of doubts on what the rules are applied in each case (which indeed, leads to them not to write a lot about it) and secondly, this implies reading many laws in order to understand how VAT works in each transaction between EU, GB and NI. In this regard, my thesis was done mostly by reading what is stated on HMRC website regarding this topic, by reading the VATA 1994 on the sections related with Brexit and by reading the VAT Directive. Additionally, I was also able to find a very complete book “The Law and Practice of the Ireland-Northern Ireland Protocol” and a thesis made on this topic by an Italian student “A Tax Perspective on Brexit: which consequences on VAT and Customs Procedures?”, which help me to confirm if my understanding of the law was correct.

The investigation ended on 16<sup>th</sup> February 2023, meaning that any laws created after that date were not considered on this thesis.

Keywords: VAT; Brexit; Protocol of Ireland-Northern Ireland; principle of neutrality

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## **Abbreviations and acronyms**

AT – Autoridade Tributária e Aduaneira

Client – a taxable person, a B2B business

CIVA – Portuguese VAT code

EEC – European Economic Community

EC – European Commission

EU – European Union

GB – England, Scotland and Wales

HMRC – His Majesty's Revenue and Customs (UK Tax Authorities)

IE – Ireland

NI – Northern Ireland

MS – European Union Member State

P3 – Third countries (all countries excluding MS and UK)

TA – Tax Authorities

TCA – Trade and Cooperation Agreement

TCTA 2018 – Taxation (Cross-border Trade) Act 2018

TDA - Transitional Delegated Act of the Union Customs Code

TIA - Transitional Implementing Act of the Union Customs Code

TFEU – Treaty on the functioning of the European Union

The Protocol – Protocol of Ireland-Northern Ireland

UCC – Union Customs Code

UK – England, Scotland and Wales and Northern Ireland

VATA 1994 – UK VAT Code emend after Brexit

VAT Directive – EU VAT Directive 2006/112/EC

WA – Withdraw agreement between UK and EU

## 1. Introduction

VAT and Brexit is a contemporary subject where there is a lot of confusion, both from companies and VAT agents, on what are the VAT regulations applicable for transactions of goods and services between EU and UK. Having in consideration that the UK belonged to EU for 43 years<sup>1</sup>, it was obvious that the VAT rules applicable for EU-UK transactions, after Brexit, would not be the same common VAT rules applicable on transactions between EU and another third country.

With the Brexit, NI became one of the reasons why the UK took almost four years to officially leave the EU, since legally it would belong to a non-MS (UK) but would divide a territory with a MS (IE). The biggest concern with this division was that this was likely to violate the Agreement of 1998, a peace agreement made between IE and UK which required almost a free circulation between IE and NI. However, from the EU perspective, if the Brexit regulations would comply with the Agreement of 1998, NI would be a region where goods could easily pass through to EU without complying with its sanitary rules. However, in order to comply with the EU customs rules and for the controls to not be done on the NI-IE border, which would violate the free circulation principle in the island of Ireland, this would imply to set NI different from GB, where UK would not be working as a Union.

To solve the so-called Brexit Trilemma described above, the solution was that the customs border would be located not in the NI-IE border but instead on the Irish Sea, which divides NI and GB. In order to regulate the Irish sea border, it was created the Protocol of Ireland-Northern Ireland which defines that, in relation to VAT, any transaction of goods (and only goods) between EU and NI would be regulated under the EU rules, however, it was establish in UK customs and VAT codes that any transaction of goods between NI and GB would be regulated under the UK rules.

Since this solution seemed to me that a good passing through NI after Brexit could benefit from the EU and UK laws, the goal of thesis is to conclude: firstly, if the Brexit Trilemma was achieve and if not, what are the consequences of that; secondly, if the solution of the customs controls being done on the Irish sea creates any violation on the

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<sup>1</sup> 1973 - 2016

VAT role and its principles; and thirty, if the Protocol is written in a way that I understand the agents could, lawfully, pay less or no VAT at all on the transaction of goods between EU and GB. For this purpose, the thesis is divided in three parts: on the first one, I will explain very briefly why the Brexit happened, what is the Agreement of 1998 and why the Irish sea boarder was the best solution for EU and UK; in a second part, I will analyse which VAT rules applied in transactions between EU, NI and UK; and lastly, in the third part, I will analyse the VAT rules explained in a critically way to answer the above questions and to be able to achieve my conclusions.

## **2. The causes of Brexit**

Although the UK had joined the EEC in 1973, being one of the countries joining the union at an early stage of its existence<sup>2</sup>, two years later, in 1975, the British government of the Prime Minister Harold Wilson held a referendum, on where was questioned to the British nation, for the first time in UK's political history, if UK should remain part of the EEC. At that time, the British nation had a clear preference in staying a member of the EEC, with 67% of votes. However, in 2016, this time at the British government of Prime Minister David Cameron<sup>3</sup>, when that same question was asked, the British nation had swift its preference by voting to leave the EU, with 52% of votes<sup>4</sup>.

The causes for the British nation this time voted to leave the EU are focus on three main aspects: immigration, national autonomy, and contributions to the EU budget<sup>5</sup>.

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<sup>2</sup> The EEC was created in 1957, where France, Italy, Germany, Belgium, the Netherlands, and Luxemburg were the funder countries. Only in 1973 the EEC has grown to eight members, with the entrance of UK and Denmark. (Economia Portuguesa e Europeia, Faculdade de Economia e Gestão da Universidade Católica Portuguesa)

<sup>3</sup> David Cameron was not a support of Brexit however he promised in elections in 2015 that if its conservative party wins, he would hold the referendum, since the population, including some members of the conservative party, was starting to consider Brexit very seriously. In this sense, since its party won the election and the referendum was hold, giving the results of it, with the Brexit option being the one chose among the population, he resigned as Prime Minister, giving way to Prime Minister Theresa May, which was the first Prime Minister starting the Brexit negotiations with the EU. (HM Revenue & Customs. Past Prime Ministers.)

<sup>4</sup> Most people in England and Wales chose to leave and the majority of NI and Scotland voted remain.

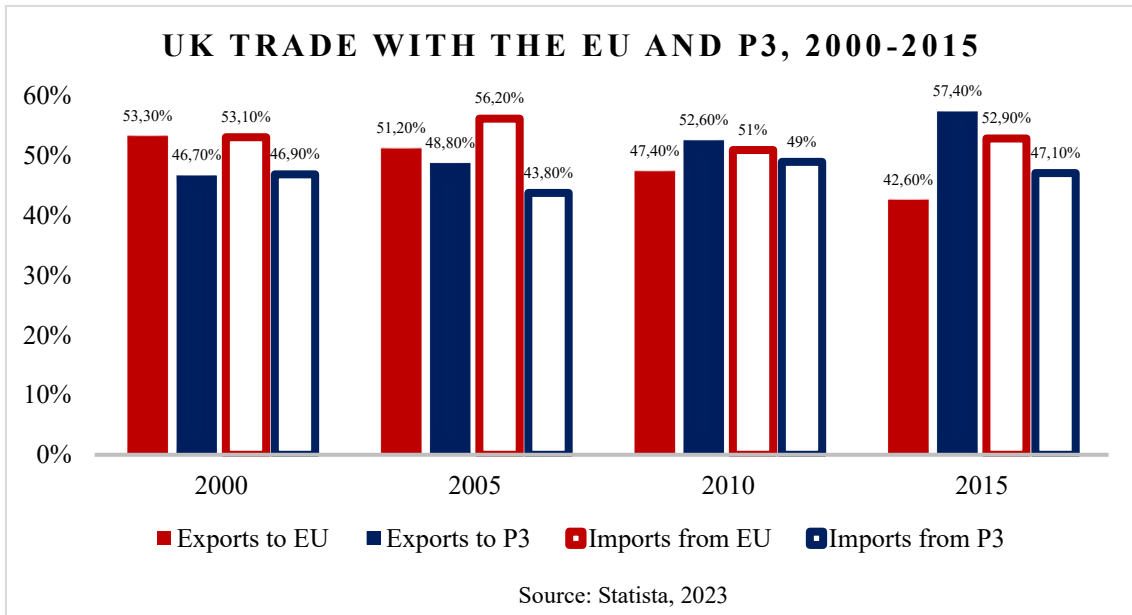
<sup>5</sup> EU budget. (n.d.). European Commission.

Regarding immigration, the British people considerer the UK was receiving too many people from other MS, which was threatening the job and educational opportunities for the British originally born in UK. In relation to national autonomy, it was considered unacceptable for most of the British people that the European Laws most of the time prevailed over the British Laws, especially in trials which would involve the European Court of Justice. Lastly, the UK was constantly one of the MS which would most contribute to the EU budged, being in the top three of the most contributors in 2015, with £8.8 billion, which was consider by British nation such a huge amount that the British government could spend instead to improve the public health services.

For those reasons and many others not so spoken in the media, together with the strong campaign maid by the parties who were in favour of Brexit, the UK would be starting to leave the EU on 23<sup>rd</sup> June 2016.

### **3. The reasons behind the creation of the Protocol of Ireland-Northern Ireland**

The UK leaving the EU would change the VAT regulations that used to be follow for transactions of goods and services between UK and EU. The UK would start to be treated in the VAT Directive as a third country, and EU treated in the VATA 1994 as a third country, meaning that most of the benefits of free trade stablished in the VAT Directive and TFEU, which will be analysed in section 5.1.1., would not apply anymore for transactions of goods and services between EU and UK. However, giving the fact that UK was a MS for 43 years, it was necessary to stablish special agreements for the UK-EU trade in the Brexit negotiations, especially for Brexit to impact the less companies which were so dependent on each other market – according to data retrieved from Statista, from 2000 to 2015, the EU has been one of the main partners for trade with the UK, representing almost always more than half of UK's exports and always more than half of UK's imports.



Graph 1 - UK trade with EU and P3, 2000-2015

However, one of the reasons for the UK on 23<sup>rd</sup> June 2016 have the confirmation that its nation wanted to leave the EU, but the exit was officially performed only on 31<sup>st</sup> January 2020, was the discussions between EU and UK on how VAT would be regularized NI, since with Brexit, the NI would become a region which legally would belong to a non-MS (UK) but would divide a territory with a MS (Ireland). NI was seen from EU as a threat to the security controls made for goods entering EU, since the union has come over the years with very restrict sanitary rules which goods must comply in order to enter the EU, for the purpose to preserve as possible the health and security of its citizens. With the UK leaving EU territory, having NI as a region which connected a MS to a non-MS, it was very important for EU to establish strict rules to be followed by the goods that would pass through NI. However, from the UK side, there was a very important agreement made with Ireland, which was mandatory for UK government to preserve on the Brexit negotiations – the Agreement of 1998.

### 3.1. The Agreement of 1998

The Republic of Ireland was a colonize region by the UK since the 13<sup>th</sup> century. Most of the Irish citizens did not agree with the British domination, however, most of the citizens of NI believed that it was more beneficial for the Republic of Ireland to remain part of UK. In 1920, Ireland was able to gain the independency from UK, however NI

decided to remain part of UK. This political separation, which from the first time divided the island of Ireland into two different regions, Ireland and NI, led to a big war in the island, between nationalists, which believed that the NI would always benefit from being part of UK, and the unionists, which believed the island of Ireland should be unified and the same rules should be applied in all island. To end this civil war, it was establishing between Ireland and UK, in 1998, a peace agreement, the so-call Good Friday Agreement or the Belfast Agreement.

The most relevant principle established in this Agreement of 1998 was that, since the sign of that agreement, any new laws that the UK could create in any subject could never ruin the Irish north-south cooperation. In relation to VAT and customs rules, it was established, in accordance with this main principle, that any good would be freely transact between Ireland and NI, meaning that no VAT or additional customs duties would be charged when a good would be transact between NI and IE. Since in 1998 both IE and UK were MS of the EU, this free circulation deal was easy to comply with since within EU, as will be described in section 5.1.1., the goods are trade fully exempt of VAT. However, as referred in section 3, with the UK leaving the EU, this free circulation requirement establish in Agreement of 1998 was not so easy to comply with.

### **3.2. The Irish Sea border solution**

With Brexit, by the first time in the island of Ireland, there would be a territorial division between a MS (IE) and a non-MS (UK). Moreover, as referred in section 3.1., the EU wanted to stablish strict customs rules in order to control as much as possible the goods that would enter EU from UK, in order to make sure that any good that would enter the EU would comply with the EU sanitary rules (something that, since the UK would leave the EU, any good transact within UK would no more have to comply with). However, the creation of strict customs regulations on the NI-IE border would go against the Agreement of 1998 since the free trade would not be applicable for goods enter in IE from NI. Since the EU was not able to give up on the customs controls of goods entering the EU from UK and the UK was also not able to disregard the Agreement of 1998, specially having in consideration that it was an Agreement that stablish the peace between

unionists and nationalists and the disrespect of such agreement could lead to a new war in the island of Ireland, the EU and UK had the so-called Brexit Trilemma to be solved: how could the UK leave the EU, (i) and UK keeping work as an union where would be avoid checks and controls on goods moving between GB and NI (ii) respecting the EU customs control requirements for goods entering EU from UK and (iii) respecting the Agreement on 1998 by avoiding checks and controls on goods moving between IE and NI? The solution was that the customs border would be located not in the NI-IE border but instead on the Irish Sea, which divides NI and GB.

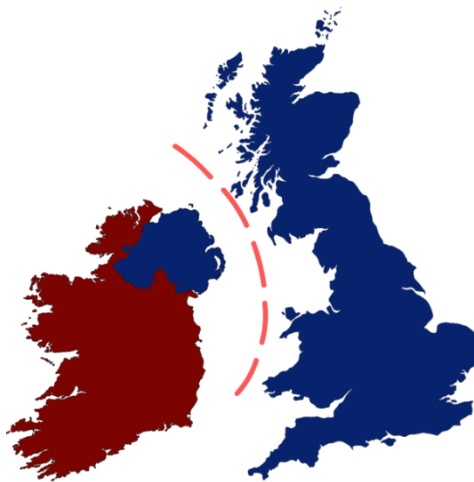


Figure 1 - The Irish Sea border solution

In order to regulate the Irish Sea border, it was created the Protocol of Ireland-Northern Ireland, which belongs to the WA, one of the special agreements made between EU and UK in consequence of Brexit. The Protocol defines that, in relation to VAT, any transaction of goods (and only goods) between EU and NI would be regulated under the VAT Directive and TFEU however, it was establish on the Brexit negotiations with EU that any transaction of goods between NI and GB would be regulated under the VATA 1994 and the TCTA 2018. In this sense, there were establish a lot of new special VAT rules for the transaction of goods between EU and GB, especially when such transaction involved NI. Those new VAT regulations will be analysed in detail in section 5.

## 4. The scope of the thesis

Since it is defined in the Protocol that the EU VAT rules are applicable in NI only in relation to transactions of goods between NI and EU (and not services<sup>6</sup>), all the analysis is done for the VAT rules applicable on NI-EU-UK transactions only in relation to goods. Additionally, for simplicity purposes, I will also assume that the movement of a good never includes the transportation, since it would add complexity to the analysis, that was not my intention. In relation to the goods transact, I decided not to define a specific one to keep the analysis simple and more general as possible, however, having in consideration that special rules were created in related to specific goods<sup>7</sup>, those are out of scope of this thesis, meaning that when I refer a “good”, I am not referring to none of those special ones.

In terms of law, I will only analyse the new VAT rules established in the Protocol, in the EU and in the UK VAT regulations, meaning that none of the new rules defined for other customs duties regulation will be analyse (i.e., excise duties). Moreover, in relation to the customs formalities, they will be mentioned in few times, however in a very superficial way, since the focus of this thesis is to discuss only the issues related to VAT. Additionally, having in consideration that on the first year that UK has officially left the EU, meaning between 30 January 2020 and 31 December 2020, the Brexit VAT regulations adopted were different than the ones applied after that, the so-called “transaction period”<sup>8</sup>, I will only analyse the laws applicable for goods that would be exported from one of the regions (EU, GB or NI) to another after the transaction period – the VAT rules applicable since 1<sup>st</sup> January 2021.

Lastly, since I understand that VAT avoidance is more likely to be done by taxable persons, I decided to do the VAT rules analysis only in relation to B2B transactions of

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<sup>6</sup> In relation to services, it is established in VATA 1994 that NI follow the VAT rules applicable in UK.

<sup>7</sup> These goods include the movement of medicines, guide dogs and other certain animals like sheets and goats. (EU-UK relations: solutions found to help implementation of the Protocol on Ireland and Northern Ireland. (2021, June 30). European Commission)

<sup>8</sup> Between 31 January 2020 and 31 December 2020, special rules were defined in the WA for goods that would leave one of the reasons before 31 January 2020 but would arrive the country of importation after that date. I wanted my thesis to just analyse a situation where today a good from EU or UK would be exported to UK or EU where the new rules defined under the Protocol and under the EU and UK VAT codes would apply.

goods between EU and UK (meaning that VAT rules for distance sales will not be analysed), where I assume that the client is VAT register in the country of importation and the supplier is VAT register in the country of exportation.

## **5. VAT Laws applicable on B2B transactions of goods between NI, EU and GB**

### **5.1. Movement of goods between EU and NI**

The Protocol established in article 5, number 3, 4 and 5 that, even after the transaction period, the VAT Directive and the TFUE will continually to be applicable on the transaction of goods between EU and NI<sup>9</sup>. Giving the fact that NI is still part of UK, where, as referred in article 7 number 1 of the Protocol, the VAT regulations in NI are regulated under the UK VAT rules, it was necessary to create a new section on VATA 1994 which would transpose the VAT Directive law in the UK VAT law<sup>10</sup>, but just in relation to NI. This new section is entitled as “schedule 9ZA” in VATA 1994, which regulates the transaction between NI and EU according to the VAT Directive harmonized rules<sup>11</sup>, where, according to article 8 of the Protocol, is the HMRC who is responsible to regulate the application of these EU rules transposed into VATA 1994<sup>12</sup>.

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<sup>9</sup> Both supplier and client VAT register in UK would have to add the prefix “XI” to the UK VAT number on all documentation related with the movement of goods, for customs to proceed with customs controls according to EU VAT and Customs rules.

<sup>10</sup> This procedure adopted by HMRC is similar to the procedure adopted in any another country who becomes a MS. For example, in relation to Portugal, the VAT Directive laws are also verified in CIVA. In this way it allows for the VAT codes of any MS to not be oppositional to what is establish in the VAT Directive.

<sup>11</sup> The harmonized rules are in respective of, for example, how to declare it on the VAT returns (as input or/and output tax) and the dispatches and arrivals being exempt of VAT. In relation to, for example, the rates applicable when not exempt or how taxpayers can recover the VAT is specific of each MS.

<sup>12</sup> This is also verified for others MS. For example, in Portugal, it is also the AT who verifies if the VAT Directive law transposed into Portugal is being correctly applicable. The special thing here is that a third country is verifying if EU rules are being correctly applicable. This might not be a big issue because UK was for 43 years a MS, so HMRC is used to regulate such rules, which did not change much since Brexit happened.

### 5.1.1. Intracommunity transactions of goods

According to article 20 of the VAT Directive, a transaction of goods between two MS is entitled as an intracommunity transaction. According to article 40, the main principle of taxation applicable to these transactions is the destination principle, where, according to article 138, there is an exemption of VAT in the country where the good is dispatched, and, according to article 2 number 1 b), a taxation in the country where good arrives, applicable according to the VAT rules of the MS acquiring the goods<sup>13</sup>. However, it is defined in article 30 of TFUE<sup>14</sup> that it is forbidding to charge VAT on the transactions of a Union good, when moved from a MS to another MS, including NI. A good can be consider a Union good under article 153 of UCC, if the good has Union origin<sup>15</sup> and was not been removed from EU (unless if it was done under the customs special procedures)<sup>16</sup> or if it is a good imported from a third country into a MS in which the importer has put the good in free circulation, by complying with customs procedures and paid all customs duties liable, including VAT, in the moment of entrance of the good in EU.

Exemplifying, if a certain good is imported to IE, a MS, from Switzerland, a non-MS, not under any customs special procedure, as soon as the good enters IE, the importer will have to pay all customs duties, including VAT, for the good to be consider then a Union good and being able to be freely transact within IE and within the EU, meaning that, when that good is then dispatch to NI, a MS in relation to transaction of goods with one of the 27 MS, the NI importer is not liable to pay VAT in order to acquire the good bough to the Irish exporter. The same happens when the good is imported to NI from Switzerland and is then dispatch to IE.

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<sup>13</sup> Although there is harmonization of the VAT rules within the EU, the VAT rules applicable in each MS differs in some aspects. One of the non-harmonized rules between the 27 MS is the VAT rate applicable for the same goods transact within the EU.

<sup>14</sup> The Protocol clarified in article 5 number 3 and number 5 that TFUE still applies on transactions of goods between EU and NI.

<sup>15</sup> A good can be consider as having Union origin if it is entirely obtained in UE, which, according to article 31 TDA, means all the components and the manufacturing process were done there. If some components are from a third country or the manufacturing process was not all done in UE, the products will need to comply with the origin rules described in UCC, TDA and TIA. The rules to acquire Union origin are quite complex and are out of scope of the thesis.

<sup>16</sup> Article 153 number 3 of UCC

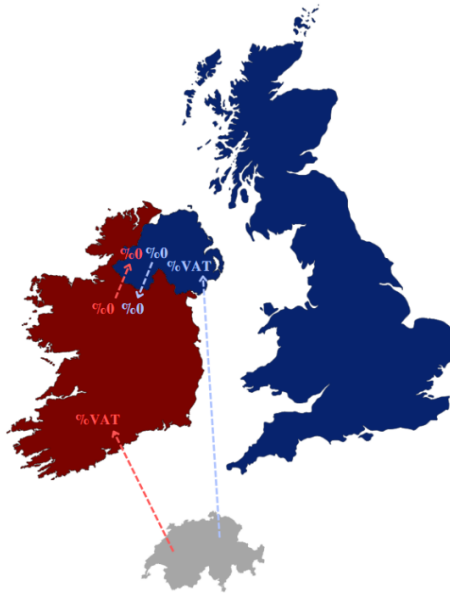


Figure 2 - VAT procedure on movement of goods between EU and NI

In conclusion, there is no VAT in transactions between one of the 27 MS and NI if all articles described above are verified.

## 5.2. Movement of goods between GB and NI

Considering article 4 of the Protocol, NI remains part of UK's customs territory, where is applicable the UK's VAT rules on transaction of goods between GB and NI, according to section 40A, schedule 9ZA of VATA 1994, with the supervision of the HMRC. However, the transaction of goods between GB and NI could not be regulated under the local transactions VAT rules applied within GB (England, Scotland and Wales), giving the NI specificities mentioned in section 3. In this sense, it was created a new section in VATA 1994, entitled as "schedule 9ZB", to regulate transactions of goods between NI and GB.

Under this section, in relation to VAT, the usual VAT rules to follow in transaction of goods between NI and GB are the usual VAT rules we commonly known for transactions with third countries. According to schedule 9ZB section 3 number 1, the supplier dispatches the good exempt of VAT and, according to section 3 numbers 2 and

4 and section 4 number 2, it is charged the UK VAT<sup>17</sup> that would be charge in an UK importation from a third country, where, according to section 4 number 3, it is the client<sup>18</sup> the one liable to pay the VAT to HMRC. However, the technical VAT rules to follow on the transaction of goods between NI and GB are not the same when the goods are moved from NI to GB or on the opposite direction, since a movement from GB to NI can mean an indirect movement between GB and a MS, and a movement from NI to GB would be a local transaction of goods in UK.

### **5.2.1. Movement of goods from GB to NI**

Giving the EU requirement of existing customs controls when goods would enter the EU from UK, including NI, it was established a rule in article 5 of the Protocol, which would prevent goods entering EU from NI without complying with EU rules, but at the same time, traders who import goods from GB to NI to remain in NI would not be affected by additional costs regarding VAT.

According to article 5 number 2 of the Protocol, the main rule is that goods are classified as goods “at risk of moving to EU”. In those cases, according to schedule 9ZB, paragraph 4, number 2 and 3, it will be applied the UK VAT rules for the importation of goods, meaning that the client will be liable to pay the UK VAT to HMRC, on the moment of importation<sup>19</sup>. Article 5 number 2 of the Protocol also clarifies that goods moving from GB to NI are not consider being “at risk of moving to EU” if, according to paragraph a) they are not subject to further commercial processing in NI<sup>20</sup>, or if, according to paragraph b), they fulfil the criteria established by the Joint Committee in article 3 of the Decision no

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<sup>17</sup> Movements between NI and GB are fully regulated under the UK VAT rules, which implies that any VAT charged on the transaction is always the UK VAT

<sup>18</sup> Except in certain supplies referred in section 6, number 3A of VATA 1994, where in this case it is the supplier the party liable to pay the UK VAT to HMRC. Since this time, it is an “internal movement” (where NI belongs to UK) and considering the assumption that the exporter is are always VAT register in the country of exportation, even in the case the supplier is exporting goods from NI, there is no need to a new VAT registration from the supplier to charge and pay the UK VAT to HMRC, unless if he was only VAT register in NI after the Brexit.

<sup>19</sup> In relation to the tax rate, it will be applicable the UK tax rates for importation.

<sup>20</sup> Defined under the Article 2 of the Decision No 4/2020

4/2020. The below table summarises when goods being moved from GB to NI are considered as being “at risk” or “not at risk” of moving to EU.

<b>Goods moving from GB to NI</b>	
<b>Main rule: goods “at risk”</b>	<b>Exceptions: goods “not at risk”</b>
Goods are going to be moved to EU	<p>Goods are not going to be moved to EU if:</p> <ul style="list-style-type: none"> <li>• they are not subject to further commercial processing in NI, defined in Article 2 of Decision 4/2020; or</li> <li>• <sup>21</sup>the customs duties applied under the UCC for that good would be zero<sup>22</sup>; or</li> <li>• <sup>23</sup>the client is authorized by the UK government to bring goods into NI for sale to or final use by end-consumers in NI.</li> </ul>

Table 1 - Requirements to classify the goods as "at risk" or "not at risk" of moving to EU

If goods are classified from HMRC as “not at risk of moving to EU”, according to article 5 number 1 of the Protocol, the EU VAT rules for importation of goods will no longer apply, where there is then a full exemption in the movement of good from GB to NI. However, even in case the good is classified as “at risk of moving to EU”, where EU VAT must be paid on the importation, the importer can demonstrate and prove that the good has entered NI and did not move to EU<sup>24</sup>. If such proof is accepted from the HMRC,

<sup>21</sup> Article 1 a) i) of article 3 of the Decision no 4/2020

<sup>22</sup> This can be verified if the goods moved from GB to NI have UK origin under the TCA, since transactions of goods with EU or UK origin are VAT and duty exempt. (HM Revenue & Customs. (2020i, December 14). Check if you can bring your goods into Northern Ireland from Great Britain without paying duty).

<sup>23</sup> Article 1 a) ii) of article 3 of the Decision no 4/2020

<sup>24</sup> This is verified, for example, in case goods were imported for the sale to final consumers in NI or for business use in NI.

under article 5 number 6 of the Protocol, the HMRC may reimburse or waive the duties<sup>25</sup>, or “compensate undertakings to offset the impact”, where such compensations must be in accordance with the EU’s state aid rules.



Figure 3 - VAT procedure on movement of goods from GB to NI

### 5.2.2. Movement of goods from NI to GB

For goods moved from NI to GB, in most of cases, there is not applied VAT or other special control procedures, since there is almost a prohibition on imposing barriers on the entry of such goods in GB. Indeed, as mentioned in article 4 of the Protocol, goods are being trade under the same customs territory and so, as mentioned in article 6 number 1 of the Protocol, nothing should affect the free access of goods from the GB market when acquired to NI market. However, the inexistence of such controls is not applied to all goods moving from NI to GB.

According to paragraph 6, number 1 of schedule 9ZB, if the good exported from NI to GB is qualified as an NI good, both the importation and the exportation can be subject to an exemption, where neither the supplier nor the client have to pay UK VAT at point of export or at the point of import. However, under the definition described on paragraph 3 of The Definition of Qualifying Northern Ireland Goods (EU Exit)

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<sup>25</sup> HMRC may claim reimbursements or waiver of duties up to a maximum of €200,000 of aid over three tax years.

Regulations 2020, for a good to be classify as so, the good must have been processed in NI<sup>26</sup> or have acquired in NI the free circulation status<sup>2728</sup>. In the case the good is not processed in NI and then have to firstly acquire the free circulation status, where UK VAT must be paid by the NI supplier in order for the good to be consider in free circulation in UK, there is not verified the a fully exemption of VAT described in paragraph 6, number 1 of schedule 9ZB, but a taxation in exportation and an exemption on importation.

If the good is qualified as not an NI good, according to schedule 9ZB, paragraph 3, number 1 there is an exemption on the dispatch of goods from NI and, according to number 2 and 4, a charged of UK VAT on the importation of the goods to GB, being the GB importer liable to pay the UK VAT to HMRC.

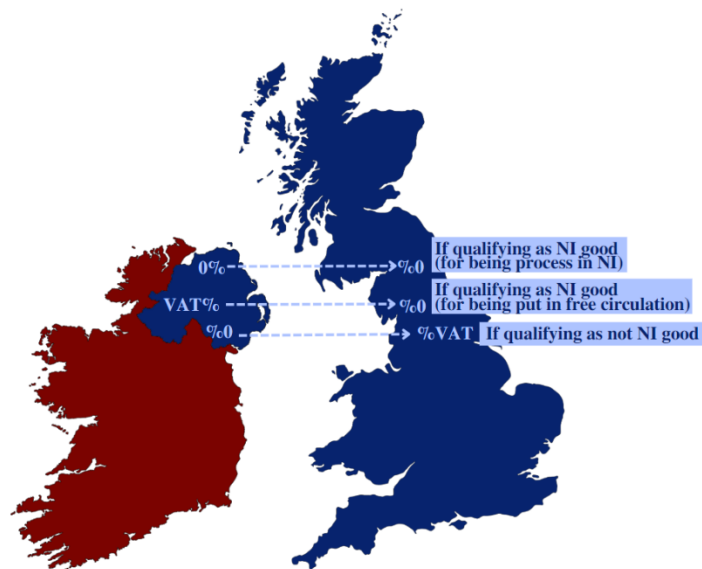


Figure 4 - VAT procedure on movement of goods from NI to GB

<sup>26</sup> Defined in paragraph 3, number 3 of The Definition of Qualifying Northern Ireland Goods (EU Exit) Regulations 2020

<sup>27</sup> Acquiring the free circulation status does not mean that the good has UK origin.

<sup>28</sup> Defined in paragraph 3, number 2 of The Definition of Qualifying Northern Ireland Goods (EU Exit) Regulations 2020

### **5.3. Movement of goods between GB and EU**

From the moment the UK left the EU, for goods which were exported after the transaction period<sup>29</sup>, the transaction of goods between the two regions is now treated as a transaction between two third countries, regulated by both UK and EU VAT rules. However, giving the fact that there is a special region between EU and UK, the trade is not so easy to be understand and to even be regulated.

We can conclude after analysing sections 5.1. and 5.2. that NI has a special treatment between the two regions, because a transaction of goods between EU and NI, is regulated under the EU VAT rules and a transaction between GB and NI, is regulated under the UK VAT rules. Taking this in consideration, on this section I will only analyse the applicable rules when the goods trade between GB and EU do not cross NI, and then on section 6, I will analyse the applicable rules when the good trade between EU and GB cross NI.

#### **5.3.1. Movement of goods between GB and EU not through NI**

Considering that Brexit never wanted to damage the companies dependent on EU and UK market, it was establish in article 21 of TCA a special treatment where it is described that a good moved between EU and GB could benefit from a fully exemption of VAT if agents can prove that the good meets the origin rules from annex 3 of the Protocol for it to be consider as having an EU or UK origin.

In cases where no full exemption is applied since non-Union goods or non-UK goods are being transact between GB and EU, the VAT rules to adopt are the ones commonly known for the transaction of goods between two third country. In relation to exportations from GB to EU, the non-Union or non-UK good become subject to the export UK VAT regime, meaning that there is an exemption on GB, defined under the section 30, number 6, of VATA 1994<sup>30</sup>, in which there is a taxation of the MS VAT on the MS,

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<sup>29</sup> The EU VAT rules are still applicable until five years after the transition period on trade between UK and EU only if the good was exported from one of the regions before the transition period and arrived after the transition period on one of the regions.

<sup>30</sup> The VAT exemption applies only if the good is exported within a maximum time limit of three months from the moment the dispatch is declared and if the supplier provides on the UK customs evidence that

where the party liable to comply with both VAT and customs procedures depends on the Incoterms clause agreed between the parties<sup>31</sup>. In a similar way, in relation to exportations from EU to GB, there is an exemption on the MS from where the goods are exported, and a taxation in the country of importation, GB, where the party liable to pay the VAT to the TA follows the rules of the new UK import regime, which are not the same for every good imported in UK – the rules to apply depend if the value<sup>32</sup> of goods imported is below or above a threshold of £135.<sup>33</sup>

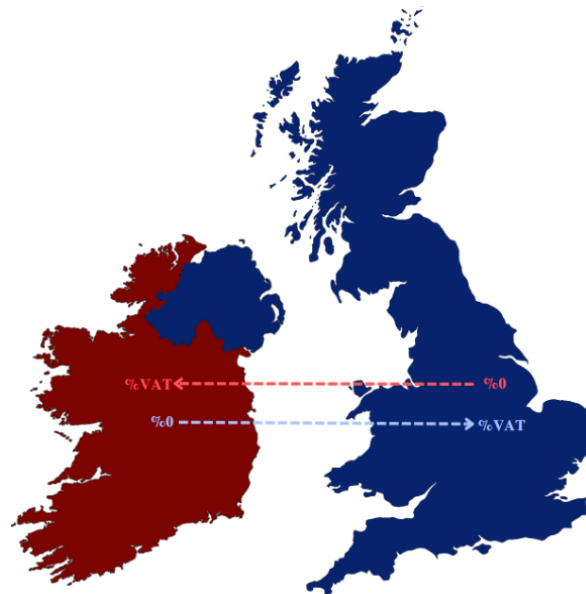


Figure 5 - VAT procedure on movement of goods between EU and GB not through NI

In conclusion, there is always VAT to be paid to the TA in direct transactions between EU and GB.

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proofs the transaction has taken place. If the supplier is not able to comply with one of the two conditions, he is required to account for output VAT on his UK VAT return in the period in which the appropriate time limit expires or he is not able to provide evidence, but the transaction remains exempt, mining that the client does not directly support such VAT (supporting it indirectly at the price).

<sup>31</sup> This will not be analysed since it is not relevant for the research question of this thesis.

<sup>32</sup> Value is defined in TCTA 2018, section 16 and in VATA 1994, section 19

<sup>33</sup> This will not be analysed since it is not relevant for the research question of this thesis.

## **6. Movement of goods between GB and EU through NI**

When the good is transact directly between GB and EU, as described in section 5.3.1, the only concern is to understand the specificities of the new rules to applied (mainly who is the party liable to pay the VAT at importation) because the transaction in a macro view is regulated by the commonly rules known for movement of goods between two third countries. However, for indirect movements of goods through NI is not that straight forward: now the good is being moved through a region on which is part of UK, following UK VAT rules, but which is also consider a MS for the transaction of goods with EU, following the intracommunity EU VAT rules.

In this sense, we could say that this transaction of goods might be attractive to agents since it seems that the movement of goods can comply with EU or UK rules, being able for them to follow the VAT rule which is more convenient. Therefore, in this section, I will analyse if this was something that the EC and HMRC have thought in their Brexit negotiations, mainly in the formulation of the Protocol, if there are any special rules to follow in case of this indirect transactions and if there are any loopholes in the law which urge from the Brexit in which allows agents to, lawfully, pay less VAT (or not pay any VAT at all) on the trade of goods between EU and GB. This analysis only concerns to movement of goods with no Union or UK origin, since as referred in section 5.3.1., the transaction of those goods between EU and UK is fully exempt, mining that passing through NI does not have any impact.

### **6.1. Movement of goods from GB to EU through NI**

In respect of this transaction, there are special VAT rules to follow, which differ from the rules defined in section 5.3. However, the VAT treatments to follow in this indirect transaction of goods are not always the same, since it depends on where the good is at the point of sale<sup>34</sup>, something previously agreed between supplier and client.

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<sup>34</sup> The point at which the transfer of rights to the goods takes place (HM Revenue & Customs. (2022, May 18). Accounting for VAT on goods moving between Great Britain and Northern Ireland from 1 January 2021.)

### **If goods are located in GB at the point of sale**

If the good is in GB at the point of sale<sup>35</sup>, the GB supplier will have to issue the invoice to the EU Client with UK VAT, in which the EU client will pay such UK VAT when the invoice is issued, together with the good's price<sup>36</sup>, being the GB supplier liable to pay such VAT to HMRC. Then, when the good arrives in EU in a second step, it is applied a zero EU VAT, so no MS VAT needs to be paid by the European client.



Figure 6 - VAT procedure on the movement of goods from GB to EU through NI when the good is in GB at the point of sale

### **If goods are located in NI at the point of sale**

If the good is in NI at the point of sale<sup>37</sup>, in relation to VAT, agents must consider two separately transactions of goods: the first concerns the movement of goods from GB

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<sup>35</sup> Here I am considering cases where goods are exported from GB to EU though NI but in any time the good remains in NI (NI is just a passing point). These transactions can typically happen when the good is imported by IE.

<sup>36</sup> When the supplier issues an invoice with VAT, the client would be liable to pay the so-called gross amounts, which includes the sum of good's price, also known as base amount, and the VAT applicable for that good.

<sup>37</sup> Here I am considering cases where goods are exported from GB to EU though NI but remain in NI for a specific time period. These transactions can occur when the supplier firstly moves the good to a warehouse belonging to subsidiary established in NI and then agrees with selling it to the EU client.

to NI and the second concerns the moment of goods from NI to EU. On the first one, the British supplier issues the invoice with UK VAT, in which such VAT will be paid by the EU client to GB supplier, together with the good's price, being the GB supplier liable to pay such VAT to HMRC. The second transaction will be treated as described in section 5.1.1. when a good from a third country first enters an EU MS, in which the British supplier exports the good from NI exempt of VAT and instead it is charged to the EU Client, on the importation, the MS VAT, where the client is liable to pay such VAT to MS TA, in order for the good to be consider in free circulation.

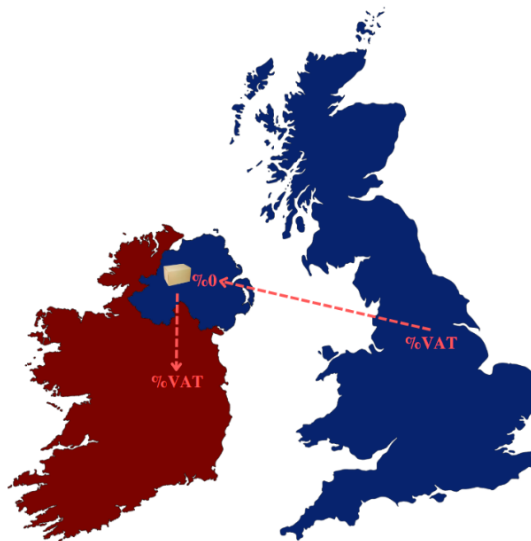


Figure 7 - VAT procedure on the movement of goods from GB to EU through NI when the good is in NI at the point of sale

### **6.1.1 Does agents save on VAT costs if opting for the indirect transaction of goods from GB to EU?**

From the EU importer, it is clear that, in relation to the second indirect transaction of goods from GB to EU described, in which the good is in NI on the point of sale, there is a double taxation for the EU client, since it pays UK VAT on the moment the sale invoice is issued by the GB supplier but the EU client also pays MS VAT at the moment of importation of the good to the MS. In this case, it does not compensate for the EU importer to perform an indirect transaction of goods through NI in order to acquire the good from GB, since in a direct transaction the EU importer would only have to pay MS VAT on the importation of the good to the MS.

However, in relation to the first indirect transaction of goods from GB to EU described in which the good is in GB on the point of sale, either the client opts for a direct or an indirect transaction, he will have to pay VAT only one time (meaning that there is no double taxation). What differs in this case the direct from the indirect transaction is that if the client opts for the direct transaction, the client will pay the MS VAT for importation of goods, and if the client opts for the indirect transaction, the client will pay the UK VAT for importation of goods. In this sense, I understand that the option the client would follow would depend on the VAT rules applicable for the same good in UK or EU and which VAT paid would be easier for the client to recover<sup>38</sup>.

From the GB supplier perspective, it is indifferent the transactions chose from the EU importer, since in both cases the GB exporter will not have to support VAT: if the EU importer opts for the direct transaction, there will be an exemption of VAT on the exportation of the good to EU; if the EU client opts for the indirect transaction, the GB exporter would charge the UK VAT on the invoice, being liable to pay such VAT to HMRC, but the VAT is paid by the EU client to GB exported, together with the good's price on the moment the invoice is issued (where, at the end, no VAT is supported by the GB supplier).

## **6.2. Movement of goods from EU to GB through NI**

We could say that EU and UK have thought about the possibility of agents to transact goods indirectly between EU and GB through NI since additional rules were created in order to regulate these transactions. In this sense, I understand that the legislator had in mind that the way the law was being created could be used, lawfully, by agents, in order to benefit from the best of both worlds giving the fact that NI benefits from the EU and UK VAT rules. However, the special rules were only created in regards of the

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<sup>38</sup> For example, if for that product, in UK the VAT rate applicable would be 5% but in the MS the VAT rate applicable would be 9%, the client could opt for the indirect transaction of goods. However, if EU client will have more difficulties in recover the 5% UK VAT paid in UK (for example, if the client is not VAT register in UK), the client could then opt to pay the 9% MS VAT, since it would be easier to recover. Having in consideration that new reimbursed methods to recover VAT incur on transactions between EU and GB are quite complex, which required a detailed analysis, I will not analysing through this thesis. However, the reimbursed methods on transactions between GB and Portugal are very well described on Ofício Circulado N.º: 15803 of the Autoridade Tributária e Aduaneira.

movement of goods from GB to EU through NI, meaning that there were not created any additional rules or restrictions on transaction of goods from EU to GB through NI, in order to respect with the Agreement of 1998 and try to keep UK working as a Union. That being said, the rules applicable in these transactions are the rules previously described on section 5.1. and 5.2.2.

By application of the rules described in section 5.1. for the first transaction (from EU to NI), exemplifying with the same example used, if the good is imported to IE, a MS, from Switzerland, a non-MS, not under any customs special procedure, as soon as the good enters IE, the importer will have to pay all the VAT and customs duties for the good to be consider then a Union good and being able to be freely transact within IE and within the EU. In this sense, giving the fact that, according to article 5, number 3, 4 and 5 of the Protocol, the VAT Directive and the TFUE will continually to be applicable on the transaction of goods between EU and NI, when that good is then dispatch to NI, the NI importer is not liable to pay VAT in order to acquire the good from the Irish exporter. In conclusion, there will be no VAT in the movement of goods from EU to NI if complying with all EU VAT rules mentioned.

By application of the goods described in section 5.2.2 for the second transaction (from NI to GB), keeping with the example, if same good previously imported from IE to NI is then exported from NI to GB, there are three options in terms of taxation: there could be applicable an exemption of VAT on importation and exportation, where neither the supplier nor the client have to pay VAT at point of export or at the point of import if the good is qualified as an NI good (where that classification became from the fact that the good had been processed in NI); a taxation on the exportation and an exemption on the importation, if the good has to firstly acquire the free circulation status to be classify as NI good for being able to be then freely export to GB; or a taxation on the importation and an exemption on the exportation, if the good did not acquired the qualification as an NI good.

By analysing the rules applicable in this indirect transaction, I can conclude that there is not a full exemption on VAT when the good is not process in NI because either the NI supplier would have to pay VAT in NI for the good acquire the free circulation status and being consider a qualifying NI product in order to be import free of VAT from

GB, or either the GB client would have to pay it on GB since the good did not acquired any time the status of qualifying NI product. I understand if either the VAT is paid in NI or in GB, the VAT amount would be the same, since the VAT applicable both in NI and GB would be the UK VAT, in which rules (in relation to taxes) are the same, defined under VATA 1994<sup>39</sup>, so this procedure would only require the parties to stablish who would be the entity liable to pay the VAT to HMRC, meaning that this is not when the agents could save on VAT costs on the total transaction. However, the situation where agents could lawfully do not pay VAT is when the good comes from Ireland free of taxes giving the free circulation status defined in the UCC, is then processed in NI, acquiring the qualification as NI good, and then can be exported to GB free of VAT.

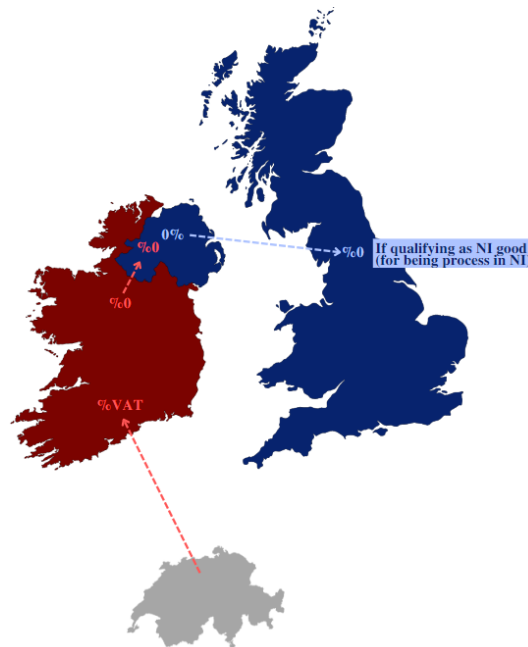


Figure 8 - VAT procedure on the movement of goods from EU to GB through NI when the good is process in NI

During my searching, I find no control mechanisms for goods which follows this way when they are being moved between EU and GB. Moreover, it is referred on HMRC website that any agent which might move his goods from EU to GB through NI for avoidance purposes may receive penalties<sup>40</sup>. However, how can the HMRC confirm that this transaction was made for avoidance purposes? Any company which is not capable of

<sup>39</sup> In terms of VAT return declarations, both transactions in NI or in GB are declared in the same VAT return declaration.

<sup>40</sup> HM Revenue & Customs. (2020h, December 11). Moving qualifying goods from Northern Ireland to the rest of the UK.

producing its goods, or it is just able to produce part of them, will be dependent on other companies, which can be established in the same country or not, in order to have access to those goods and being able to keep its business. However, the companies are free to choose its supplier among all the suppliers in the world, where that choice can depend on many factors. For example, some companies might prefer to have the best suppliers in their business industry, rather than save in supplier costs, in order to make sure they sell the best quality products, where other companies might prefer to work with suppliers which produce goods with lower quality, but they can save more on supplier costs. As referred, this choice is free and is a consequence of the globalization area we lived in – the economic agents will choose the option which fits its business the better. That being said, if a certain company chose to change its supplier to a NI supplier, after 1<sup>st</sup> January 2021, it might be done for the purposes of saving costs or for the purposes of having more quality products to sell to its customers and not being related to avoidance purposes. In conclusion, I understand it is very hard for HMRC, if they detect, for example, that an EU company, which used to have a Germany supplier, has switched to a NI supplier, to sell the final goods to GB, to prove that it was done for avoidance purposes.

## **7. Was the Brexit Trilemma solved?**

After describing the rules applied in every situation and after analysing every way of moving goods between EU and UK, in this section I will explain the loopholes I was able to identify when analysing the Protocol, the EU and UK VAT rules and analyse if the three goals of the Brexit Trilemma were achieved.

### **7.1. UK keeping work as an Union**

With the Irish border solution, the goal of the Brexit Trilemma which would be the hardest to achieve would be keeping UK working as a Union, since it was established that the customs controls would be performed within the UK (on the Irish sea), which would inevitably set NI as a different region from GB.

It was established in TCA 2018 that a good which would enter UK should be subject to pay VAT and all other customs obligations on the moment of importation, in

order for the good to be then trade freely of VAT within the UK<sup>41</sup>. Although the articles from TCTA 2018 which regulate how a good can acquire the free circulation status in UK refer that this rule applies also in regard to goods trade between GB and NI, that is not what happens in most of the cases. Article 4 of the Protocol refers that NI is part of the customs territory of UK, however, by the analysis of the rules presented on sections 5 and 6, we can conclude that, due to Brexit regulations, the VAT rules applied in transactions of goods between NI and GB are most of the time regulated as if NI is a third country in relation to GB. This different treatment on the transaction of goods between NI and GB leads to cause some sort of inequality competition within UK.

### **7.1.1. Decreased demand for NI from the GB market**

In relation to transaction of goods from GB to NI, as detailed in section 5.1., there are transactions of goods from GB to NI that follow the free circulation principle detailed in TCTA 2018, since no VAT is due on such movement of goods. However, this only happens when the good transact is classify as “not at risk of moving to EU”, which is very rare due to the several criteria that the good must comply with in order to not be consider “at risk of moving to EU”. In fact, the main rule to applied on transactions of goods from GB to NI, established in article 5 of the Protocol, is to consider the good “at risk of moving to EU”, which means that, in almost cases, the NI client supports VAT when buying a good from GB, which goes against the free circulation principle applicable in all UK according to TCTA 2018.

Although even this VAT can be reimbursed by proving that the good remained in NI, at the moment the goods arrive in NI, the client supports VAT in an initial state, which required the NI client to have some cash flow in order to pay this VAT in advance. In this sense, in order to avoid payment this payment on advance, NI agents might have preferred start working with EU suppliers rather than GB suppliers, since when a NI agent acquires a good from an EU supplier, the NI client is not liable to pay VAT on importation, oppositional to what happens when the NI client acquires the good from GB market. In

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<sup>41</sup> According to article 3 number 3 a) and article 4 number 1 a) of the TCTA 2018 free circulation rule is applicable within the transaction of goods between all the four regions of UK: England, Scotland, Wales and NI.

this sense, I understand the Brexit rules established in transactions from GB to NI lead to a decrease in NI demand from GB market and increase in NI demand from the EU market.

### **7.1.2. Increased demand for GB from the NI market**

In relation to transactions of goods from NI to GB, article 6 of the Protocol mentions that “nothing in the Protocol shall prevent the UK from ensuring unfettered market access for goods moving from NI to other parts of the UK’s internal market”, however, by analysing section 5.2.2, we can say that this article is not complied. As explained in that section, if a good enters NI from EU and is not there processed, there are two options the agents could follow: if they decide that the good should be freely acquire by the GB Client, the NI exporter has to pay VAT in NI for the good to acquire the free circulation status and be able to be freely trade within the UK; if they decide that the good should be freely export to GB, the NI supplier exports the good to GB free of VAT but then in GB the client has to pay VAT on the acquisition. In both options there is VAT to be paid by one of the parties, which means that in fact there is no “unfettered market access for goods moving from NI to other parts of the UK” when goods are moved from EU to GB through NI.

However, as detailed in section 6.2., the free circulation principle can be applied to transactions of goods from NI to GB when GB clients acquire unfinished goods from EU if the unfinished good is processed into the final good in NI. Although this method seems to comply with the free circulation principle, this is due to a special way of moving goods from EU to GB indirectly through NI, which not only can be used by agents for avoidance purposes, but also disrupts the competition between NI and GB market. For example, in case of movements of goods directly from EU to Wales, the importer who receives the unfinished good would have to pay UK VAT on the importation of the good, being liable to pay such VAT to HMRC. Then, after the good being processed in Wales, when the final good is sold on England, since the good is in free circulation in UK according to TCTA 2018 rules, the supplier would not be liable to charge VAT on the invoice. In this sense, although he might be able to recover the VAT supported on importation from EU by reimbursed processes, it immediately supports it when the transactions occur. If instead the importer receives the unfinished good imported from EU in NI, he would not be

liable to pay UK VAT on the importation of the good. Then, after the good being processed in NI, when the final good is sold to England, since the good is in free circulation in UK according to TCTA 2018 rules, the supplier would not be liable to charge VAT on the invoice. This time, the agent will not be liable to pay VAT in any stage.

In this regard, with Brexit rules, the GB agents dependent on EU companies in order to keep its business work, might have decided to start preferring to have their factories located in NI instead on one of the three other regions of GB, because in this way they can avoid supporting VAT on importation, oppositional to what happens when the NI client acquires the good from GB market. In this sense, I understand the Brexit rules established in transactions from NI to GB lead GB to increase its demand for the NI market and decrease its demand from the GB internal market.

## **7.2. Respect of EU customs control**

This was the goal of the Brexit Trilemma which was achieved in the Brexit negotiations with the Irish boarder solution. In terms of VAT, respecting the EU customs control would be easier than complying with the three other requirements of the Brexit Trilemma since in order to comply with it, EU and UK would have to define stricter rules only in relation to the movement of goods from GB to EU, since how the customs rules would be regulated on the transaction of goods from EU to GB would be mostly an UK's problem and something that was not a big issue for UK, since UK was part of EU for 43 years and indeed UK was not afraid of having goods entering UK complying with the EU security and sanitary rules. The challenge on the establishment of the stricter rules to regulate goods moved from UK to EU was not the direct transaction of goods from GB to EU, since the customs rules applicable would be similar to the ones applicable for goods entering EU from any other third country, but the indirect transaction of goods from GB to EU, which would cross NI.

By analysing the rules detailed in section 5 and 6, I could conclude that, although EU have signed the Protocol agreement and agreed that in NI would be applied the EU rules in relation of goods exchanged with EU, mostly to comply with the Agreement of

1998, the EU was afraid that NI would be a region of controls avoidance and a threat to the EU security that has been built for so many years. In this sense, it was necessary to create additional VAT rules to regulate the transaction of goods from GB to EU beyond the usual rules applicable for movements of goods from another third country to EU. However, these sticker rules applied in the movement of goods from GB to EU also lead to disrupting of the competition between EU and GB agents.

### **7.2.1. Decreased demand for EU from the UK market**

Although the Protocol establishes that in NI EU rules are applicable, in which include that any good transacted between EU and NI would be fully exempt of VAT, which might indicate that this way there was a probability that EU and UK could trade freely of VAT, in fact, this only applies when the good is exported from EU to NI, because on transactions from NI to EU, there is, most of the time, VAT to be paid. Firstly, as detailed in section 5.2.1., if the good is, in a first step, exported from GB to NI where neither the GB supplier nor the NI client had intentions of moving the good latter to EU, the NI client would be, with higher probability, liable to pay VAT to acquire the good to GB, which, although no VAT would be charge if the good would be then exported to EU, the NI client would indirectly charge the VAT paid initially to acquire the good from the GB supplier on the price. Secondly, as detailed in section 6.1., if the good is moved from GB to EU through NI and is in NI at the point of the sale, the EU client would support UK VAT and MS VAT to acquire the good. Lastly, if the good is moved from GB to EU through NI and is in GB at the point of the sale, the EU client would support UK VAT to acquire the good.

In relation to indirect movements of goods from GB to EU through NI when the good is in NI at the point of sale, VAT is a way of customs control, meaning that the EU requirement of having customs controls on the border was achieved, however, this is done at the cost of a double taxation from the EU client. I believe that this way of EU agents importing goods from GB never happens in practice since among all the rules created, this is the only situation where a double taxation is verified and, giving the free circulation rules, according to TCTA 2018, which applies to all UK, including NI, GB agents which goods where at first located at NI can firstly move those goods to GB, freely of VAT, and

then proceed with the exportation to EU, by application of the rules defined for indirect transactions from GB to EU through NI, when the good is in GB at the point of sale, or by direct transaction from GB to EU. I understand that this time this cannot be considered a VAT avoidance because a double taxation, according to the VAT rules detailed in section 8, is something out of scope of VAT since VAT taxes every stage just one time.

Although there are ways of avoiding the double taxation on the importation of goods to EU from GB, there is always VAT applied in such transactions. When UK was part of EU, the free circulation principle was applied in the trade of goods between the regions, meaning that no VAT would be applied in movements of goods from GB to EU. In this sense, although there are mechanisms of reimbursed the VAT support on importation of goods into EU, in comparison to the exchange of goods within EU, similar to what happens on the importation of goods from NI to GB described above, the EU agents would support VAT in an early stage (at importation), which implies EU business to have some cash flow in order to be able to pay this VAT in advance. In this regard, since the MS have other 26 MS to trade goods with, where no VAT would apply, the EU agents might decide to shift them UK suppliers by its EU suppliers, which lead to a decrease in the EU demand for the UK market.

### **7.2.2. No changes to the demand for UK from the EU market**

Although after Brexit new VAT regulations were established in UK and EU VAT codes, considering each other third countries, which lead almost every transaction of goods between UK and EU to be subject to VAT, whether on the pre Brexit not VAT would be supported by the GB clients, the GB clients can avoid the payment of VAT on the importation of a good from EU, if applied the method described in section 6.2. In this sense, if the UK agents are well informed about the possible ways of importing goods from EU, they might keep its the demand for EU products, since there is a way of avoiding payment VAT on the importation of those goods. Oppositional to what is referred in section 7.2.1. in relation of choosing other ways to export goods from GB to EU in order to avoid double taxation, I understand that in this case, following the trail described in section 6.2., the economic agents are avoidance VAT.

### **7.3. Respect of the Agreement of 1998**

This last goal of the Brexit Trilemma was the most relevant to be achieved from the Brexit negotiations. Whereas the first was a goal for the UK and the second one was a goal for EU, this third one a goal which EU and UK would both wanted to archive since the infringement of the Agreement of 1998 would could lead to a war between a MS, IE, and an UK region, NI (although that for the UK it was even more important, since if it did not comply with the agreement, it would be consider unlawful with the rules established between IE and UK). In this sense, the Protocol was created as a special code within in the WA, to regulate the EU-UK transactions in a way where the Agreement of 1998 was respected.

By analysing in detail how the Protocol is written, we notice that the Agreement of 1998 is referred many times (for example, in the introductory paragraphs and in the first article of the Protocol), however, in my point of view, it is mentioned several times to demonstrate and guarantee to the island of Ireland citizens that rules stablish in the Brexit negotiations fully respect the Agreement of 1998. Although according to the rules established in the Brexit negotiations, the Agreement of 1998 is fully complied, because the free circulation rule of the TFEU is perfectly applicable in all transactions of goods from EU to NI – even in indirect movements of goods from EU to GB through NI – if we analyse the rules stablished on the movements of goods from UK to EU, we can conclude that most of they go against the Agreement of 1998.

Firstly, if we analyse the article 5 of the Protocol, we can understand that, because an NI importer would have to pay VAT in order to acquire a good from GB, when the good is consider “at risk of moving to the EU”, here the part of the free circulation of goods between NI and IE that is referred in the Agreement on 1998 is not complied. A good being probably exported to IE (a MS) makes the NI exporter liable to pay VAT to HMRC in order to proceed with the exportation to the EU, which goes against the rules established in the Protocol that refers that free circulation movement of goods, defined under the TFEU, where no VAT is charged in any step of the transaction of a good within EU, is applicable in NI. Although this liability to pay VAT on the importation of a good to NI from GB seems to just be damaging the UK working as an Union, as criticize in section 7.1., it also damage the cooperation between NI and IE, because the fact that a

good is described as “at risk of moving or not to EU”, this description indirectly establishes a customs control on the NI-IE board. In this sense, although it was defined that the customs controls would be done on the Irish Sea boarder in order to comply with the Agreement of 1998, in fact, there are established indirect customs controls on the NI-IE boarder.

Secondly, there is also a clear violation of the Agreement of 1998 on the rules defined when a good is indirectly moved from GB to EU through NI and the good is in NI at the point of sale, because, as described in section 6.1, when the good is moved from NI to IE, the Irish importer must pay VAT on the moment of importation. As referred in section 7.2., although I understand that this movement of good does not happens in practice if the economic agents are well aware of the possibilities of exporting a good from GB to EU, and this seems to be just an anti-avoidance rule created to avoid economic agents to use NI as region to practice VAT avoidance in the movement of goods from GB to EU, the rule cannot be ignored because in the Agreement of 1998 is referred that “any rule that would be established in UK could not any time violate the norther and south of island of Ireland” and indeed this rule clearly violates that line. In conclusion, although it is mentioned in the Protocol in the twentieth introductory paragraph that there is a “firm commitment to no customs and regulatory checks or controls and related physical infrastructure at the border between IE and NI”, in fact the Protocol articles make clear that checks and controls are needed on the NI-IE boarder.

In conclusion, I understand that the Brexit rules are not written in a way of protecting the Agreement of 1998. Since this was something notice by the UK and IE when the rules started to be applicable on 1<sup>st</sup> January 2021, on 13<sup>th</sup> June 2022 it was introduced a bill by the UK Government which consists in a purpose of alteration of the Protocol, especially because of it does not comply with the Agreement of 1998. One of arguments for the purpose of the Bill is that it is consider the Protocol was firstly created to protect the Agreement of 1998, however, at the end, it preserves the protection of the EU Single Market more than the Agreement of 1998, which is easy to conclude by the interpreting article 5. However, if we think that Brexit negotiations wanted to forbidden checks and controls on goods moving between GB and NI, the implication is that some other action would be needed to protect the EU’s Single Market, which indeed could imply to not comply so well with the Agreement of 1998.

## 8. Violation of the principle of VAT neutrality

It is clear by analysing sections 7.1. and 7.2. how VAT nowadays can be a competitor factor on the EU-NI-GB transactions, influencing the behaviour of agents however, one of the main characteristics of VAT, which advises it as the ideal system of consumption taxation, is its neutrality.

According to the principle of VAT neutrality, economic operators who performs the same operations, meaning transact and sale the same type of goods, being indeed in competition with each other, must be treated in same terms in relation to VAT, which means that the principle of VAT neutrality must be taken into account when interpreting the exemption rules, in order to ensure that the exempt rules do not allow traders carrying out the same transactions to be treated differently in the VAT collection<sup>42</sup>. This main principle includes the principle of elimination of distortions of competition resulting from different treatment from the point of view of VAT, which is clearly a principle violated under the VAT rules applicable on the transaction of goods between EU and UK described above.

Of course, with the UK leaving the EU, the VAT treatment on the movement of goods between UK and EU would be different, because now the agents would have to support VAT in order to move goods between UK and EU, where on the pre Brexit, no VAT was support, giving that the free circulation principle under UCC applied also to UK. Indeed, although the VAT principle on destination defined under international rules, where a certain good is imported from the country, like Switzerland, free of VAT, and then when enters IE, the client would support the IE VAT, was a principle created in order to avoid VAT to influence the least the agents behaviour on the demand of goods from other countries outside its Union, in order to promote a global trade<sup>43</sup>, as refer in sections above, it is different to be liable to pay VAT at a first stage and then wait for it to be reimbursed, than to not be liable to pay VAT at any stage (because for the first one it requires companies to have some cash flow). In this sense, I understand that the principle of neutrality would not be violated under the normal VAT consequences of a MS leaving

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<sup>42</sup> CAAD, Processo n° 435/2017-T

<sup>43</sup> Oliveira, M. O. (2017). O Imposto Sobre o Valor Acrescentado.

the EU, since it is normal that such change would lead to lower the demand on each other market and indeed other ways would have to be defined beyond VAT to avoid such impact on the economic agents dependent on each other market.

The problem is that, with Brexit, the VAT rules lead to a creation of an inequality demand for each other market - in relation to movements of goods between EU and UK, there was a decreased in the demand for EU from the UK market but no changes to the demand for UK from the EU market; in relation to movements of goods within UK, there was an increase in the demand for GB from the NI market but with a decrease in the demand for NI from the GB market.

In relation to movement of goods between EU and UK, this inequality of taxation among agents of the different unions is a consequence of an existence of a way of GB clients to acquire goods from EU free of VAT by performing tax avoidance, detailed in section 6.2., but, on the opposite direction, there were created anti avoidance rules for an EU client to acquire goods from GB, detailed in section 6.1., where the application of those rules generate double taxation on the side of the EU importer. Although the double taxation is not considering a principle which can be violate or not<sup>44</sup>, oppositional to the principle of neutrality, VAT is a multi-phase indirect tax that affects the entire act of consumption, where the goal is only for the ending consumer to support VAT at the last stage of distribution, allowing the economic agents to deduct from the tax assessed the tax on its purchases. If double taxation happens, the economic agent supports VAT two times, in which, although there might be ways of recover it by reimbursement processes, it must have the double of cash flow a normal VAT agent, in the same conditions, subject to just one taxation needs to have. In this sense, in a same economic view, a VAT agent which does not support VAT in any stage, does not need to have that cash flow, being more able to invest its profit on the company's economic purposes. In this sense, we could conclude that VAT nowadays is used on the EU-UK transaction of goods regulations EU perspective as customs control tax, where the AT benefits from that tax profit, but on the UK side, VAT is used as a way of continuing to be economic competitive with the EU companies.

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<sup>44</sup> Provedoria de Justiça - Parecer n.º R-4479/06

In relation to movements of goods within UK, although it cannot be considered that there is a tax avoidance way of avoiding to pay VAT because, as described in section 5.3., this is done by simple application of the free circulation principle defined under TCTA 2018, we can conclude that it is more easy to acquire goods from EU to UK by importing them to NI instead of importing them to GB giving that in NI the free circulation principle defined under TFUE is applicable in EU, which consequently causes the GB importers to prefer using NI market as an intermediary region in order to import goods freely of VAT from EU instead of using the GB internal market (Wales, Scotland or England).

I understand that this consequence of VAT being a competitor factor between EU and UK was foreseen by the UK and EU on the Brexit regulations, having in consideration that there were created in the WA some rules to prevent Brexit to cause inequality competition among agents<sup>45</sup>. However, although those rules were created and might reduce the competition between both Unions, VAT could not in any time be a competition factor, because indeed it would violate its neutrality principle.

## **9. Solutions**

After analysing the rules applicable on the transaction of goods between EU and UK, if the Brexit Trilemma was achieved, and how the VAT principle of neutrality is violated, I was able to conclude that the main problem which urges to create inequality competition between EU and UK agents is that there are a lot more sticker rules on the movement of goods from UK to EU when comparing to the movement of goods from EU to UK, which was a natural consequence of the Brexit Trilemma and the exigencies of EU and UK: EU wanted sticker customs controls goods on the movement of goods between EU and NI and the UK wanted almost a free circulation on the movement of goods between NI and GB.

I consider that VAT rules applicable on the regulation of the movement of goods from GB to NI is the best deal the UK and the EU could have agreed to since the movement

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<sup>45</sup> The issues of State aid and VAT are linked to the concept of a level playing field. The fact that the Protocol gives exporters in NI a unique advantage in having unfettered access to both the UK and EU markets means that it is legitimate and necessary to ensure that that advantage is proportionate and not compounded by any other easements that could be unfair on competitors.

of goods from GB to NI could mean an indirect movement between GB and a MS. As mentioned in section 5.2.1., with the rules established in article 5 of the Protocol, it would be possible to comply with the EU requirement of proceeding with customs controls when a good would be moved from UK to EU, but at the same time, traders who would import goods from GB to NI to remain in NI would not be affected by additional costs regarding VAT. Giving that one of the main issues of the VAT regulations between EU and UK was how VAT was a competitor factor, I understand that one solution that could avoid VAT to have that role on the international trade, preventing NI being a region used by agents to perform VAT avoidance and also equalizing the degree of rigidity of the rules applicable on the movement of goods from UK to EU and on the movement of goods from EU to UK, would be to remain the rule described on article 5 of the Protocol for indirect movements of goods from GB to EU through NI and to create a similar one for indirect movements of goods from EU to GB through NI.

In relation to indirect movement of goods from GB to EU through NI, as detailed in section 5.2.1, the main rule would be to consider the good arrived in NI from GB is “at risk of moving to EU”, where the NI client would be liable to pay the UK VAT to HMRC, on the moment of acquisition of such good. Although there were created special rules for the indirect movement of goods from GB to EU through NI, depending on whether the good is located at the point of sale (detailed in section 6.1.), I understand that, in relation to VAT, those rules should not be applied in order to avoid creating double taxation rules and inequality payments of VAT. Indeed, although those rules were created to preventing NI being a region for VAT avoidance, the controls should be more related with the exigence of special customs documents. In relation to indirect movement of goods from EU to GB through NI, the main rule would be to consider the good arrived in NI from EU “at risk of moving to GB”, where the NI client would be also liable to pay the UK VAT to HMRC. On both cases, the VAT could be then reimbursed to the party who supported the VAT if the agent would be able prove that the goods were not moved from NI, in a similar way as described in article 5 number 6 of the Protocol.

By applying this rule, VAT would be treated as a prepayment made on the beginning of any transaction between EU and GB, working as simple customs control rather than a competitor factor which influences the trade behaviour of agents. In relation to the Brexit Trilemma, the second part “respecting the EU customs control requirements

for goods entering EU from UK” would be complied, however, the other two parts of the Brexit Trilemma could remain to be consider in cause. In relation to the first part, “keeping UK working as a Union”, on both direction of movement of goods, the NI Client would always have to pay VAT, either to acquire goods from GB or to deliver goods to GB, which would go a little against the free circulation principle defined under the TCTA 2018 for transactions of goods within UK. In relation to the third part “respecting the Agreement of 1998”, this would be considering also threat on the north south cooperation, as concluded in section 7.3., by the main principle of consider the good “at risk of moving to EU” or “at risk of moving to GB”, where the NI client would always have to pay VAT, either to acquire goods from EU or to deliver goods to EU.

In the case the UK and EU wanted to prevent VAT being a competitor factor and to violate the principle of neutrality, but at the same time does not want to violate UK’s VAT law and the Agreement of 1998, one solution in order to comply with the Brexit Trilemma by respecting the VAT principles (by application of the rules described in paragraph above) would be to reformulate the principle of free circulation defined under the TCTA 2018 and the Agreement of 1998. The more drastic solution to cover all the problems urge with Brexit, would be the UK to create another referendum, open to be answer by the British citizens, in order to understand if the citizens opinion on Brexit still remains the same and for UK to reconsider if it would benefit or not from re-enter the EU as a MS – something also never happened before in the EU history.

## **10. Conclusion**

What I conclude from this all analysis is that, firstly, the EU and UK could only achieve one of three goal of the Brexit Trilemma – with the new VAT rules created in consequence of Brexit, the customs control were established for goods entering EU from UK. From the beginning, the EU and UK could have concluded that it would be impossible to be verified all the three parts of the Brexit Trilemma, because, as mention on the introduction, complying with one of the parts would mean not to comply with another: in order to comply with the Agreement of 1998, where it imposes a free circulation of goods between NI and IE, this could cause goods to enter the EU without complying with its sanitary rules; in order for the goods to not enter the EU without

complying with its sanitary rules, but also comply with the Agreement of 1998, it was established that the customs controls would be done on the Irish sea instead of on the NI-IE border; however, with the customs controls being done on the Irish sea, the UK would no longer be working as an Union as it sets NI as a different region from GB. In this regard, it was barely impossible to achieve the three parts of the Brexit Trilemma. However, it is very questionable if the EU customs controls requirement was the most important part of the Brexit Trilemma to be achieved, specially having in consideration that the Agreement of 1998 is seen as a peace agreement which was the interest of both parties, UK and EU, to protecting it at all costs. Moreover, even for complying with this EU requirement, this was achieved by violating the VAT principles since VAT is not only being used as customs controls but instead a competitor factor among between EU and UK.

Secondly, in relation to the creation of the Protocol, although this was created in order for Brexit to respect the Agreement of 1998, by analysing carefully its articles, I could conclude that it has more a role of complying with the EU requirements rather than assuring the Agreement of 1998 is complied. Moreover, by following the Protocol with the VAT Directive and VATA 1994 rules for the movements of goods between EU, NI and EU, not only the neutrality VAT principle is violated most of the times by causing distortions of competition amount agents and creating a double taxation on the movement of goods from GB to EU through NI when the good is in NI at the point of sale, there is created, in the law, a way of agents, lawfully, import goods from EU to GB without the liability of paying VAT at any stage – the GB agents can firstly import an unfinished good from EU to NI to be there processed to be able to then move the finish good from NI to GB freely of VAT.

I conclude with my thesis that the Brexit laws should be reformulated in order to firstly, avoid the new Brexit laws to violate the VAT principles, by avoiding creating competition distortions amount agents and secondly, create laws in which agents could not perform tax avoidance in consequence of loopholes created on the law. In order for the TA to achieve these VAT goals (which should not be goals but unviolated principles), the prepayment solution described in section 8 could be an option, where the VAT is used as a customs control and not an additional cost support by agents trading between EU and UK. In relation to the Brexit Trilemma, as also concluded in section 8, I understand that

it is impossible for the three goals to be achieved, so the Agreement of 1998, the TCTA 2018, the VATA 1994 and the Protocol should be reformulated in order for the Brexit to not create new avoidance ways of not supporting VAT and for the Brexit to impact the least all agents and all deals made on the past when UK was part of the EU. In case all these goals cannot be complied, a last option for British nation would be to re-questioning its decision made in 2016, by creating a new referendum, where at this time the question would be “should UK join the EU again?”.

Lastly, I can also conclude from the Brexit analysis that the EU might take Brexit as a learning curve for the future. The fact that the EU has created article 50 on the TFEU, the EU was foreseeing to have to deal with a left of one of its MS on its years of existence. However, it is clear that the EU did not prepare itself, in relation to VAT, a harmonized law among MS, in case some MS puts in practice article 50. In this sense, Brexit can be considered an alert to EU to anticipate the challenges and creating rules on the VAT Directive and on the TFEU to be applicable in case another MS leaves the EU, especially because most of its MS divides physical territory (for example, Portugal and Spain), meaning that the problems the EU is facing with Brexit on trying to ensure that the goods which enter the EU comply with its sanitary rules, with higher probability, would be the similar problems it would face in case another MS decides to leave the Union.

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