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Finance (No. 2) Act 2023 Notes: Sections 331 – 332: freeports and investment zones

Sections 331 and 332 of the Finance (No. 2) Act 2023 (FA (No.2) 2023) essentially extend the tax reliefs available in freeport sites to investment zones, and allow the timeframe within which these tax reliefs are available to be extended, by providing the power for the current deadline, or sunset date, to be amended by regulation.

Section 331: designation of sites

Section 331 of the FA (No.2) 2023 extends the provisions for the designation of areas within a freeport under s113 (1) of the Finance Act 2021 (FA 2021), where for the purposes of Part 2 of the Capital Allowances Act 2001 (CAA 2001) (plant and machinery allowances), Part 2A CAA 2001 (structures and buildings allowances), and where the area is in England, Part 4 of the Finance Act 2003 (FA 2003) (stamp duty land tax) special capital allowances and SDLT exemptions are available,¹ to include areas situated in investment zones, by amending s113(2)(a) and (b) of the FA 2021.² Consequently, areas so designated to receive these tax reliefs within either freeports or investment zones are to be referred to as “special tax sites”, and s331(3) FA (No.2) 2023 amends s113(3) FA 2021 accordingly. The identification of freeport sites by the Treasury under s113(5) FA 2021 is similarly extended, and so, by s331(4) FA (No.2) 2023, the Treasury will also identify, or consent to the identification of, investment zones.

Section 332: altering the sunset date

The sunset date by which the tax reliefs were available³ to designated areas solely within freeports, was on or before 30 September 2026.⁴ The sunset date for reliefs is extended to allow sufficient time for reliefs in investment zones to be claimed. Section 332(1) to (3) FA (No.2) 2023 therefore provides for the insertion of a new formulation “the applicable sunset date in relation to the special tax site concerned”⁵ applicable in respect of specific statutory provisions which had previously contained freeport specific references to tax reliefs. These provisions are: s61A FA 2003 (relief from stamp duty land tax in case of transactions relating to land in designated sites);⁶ s45O CAA 2001 (enhanced capital allowances in case of expenditure on plant or machinery for use in designated sites);⁷ and Chapter 2A of Part 2A CAA 2001 (enhanced structures and building allowances in case of buildings or structures in designated sites) in particular s270BNA on the meaning of freeport qualifying expenditure as well as s270BNB providing for the apportionment of the expenditure as relates to the freeport tax site. The applicable sunset date in relation to the now so called special tax sites with reference to these particular provisions is specified in s332 (4) FA (No.2) 2023 as being either 30 September 2026⁸ or such later date as may be specified in relation to the site by regulations made by the

¹ See Glen Loutzenhiser, “Finance Act 2021 Notes: Sections 113-115 and Schedules 22 and 23: freeports” [2021] B.T.R. 433.

² FA (No.2) 2023 s331(2).

³ By either incurring expenditure under CAA 2001 s45O, or a building or structure is brought into qualifying use and qualifying expenditure is incurred under CAA 2001 s270BNA and s270BNB, or the effective date of a land transaction under FA 2003 s61A.

⁴ Except in relation to the NIC Act 2022 on which see later paragraphs in this note regarding FA (No.2) Act 2023 Sch 23.

⁵ This formulation is repeated in FA (No. 2) 2023 s332 (1), (2) and (3).

⁶ FA (No.2) 2023 s332(1).

⁷ FA (No.2) 2023 s332(2).

⁸ FA (No.2) 2023 s332(4)(a).

Treasury.⁹ Such regulations may specify different dates for different descriptions of special tax sites¹⁰ and may amend the sunset provisions.¹¹

Schedule 23: other statutory amendments

Pursuant to s331(5) and s332(6) of the FA (No.2) 2023, Schedule 23 to the FA (No.2) 2023 makes consequential amendments to the FA 2003,¹² the CAA 2001,¹³ and the FA 2001,¹⁴ to reflect the fact that s331 and s332 of the FA (No.2) 2023 have made freeport tax reliefs available to investment zones by replacing freeport specific terminological references with more neutral and collective terminology, such as “special tax sites” or “qualifying land”, depending on the applicable tax relief.

Schedule 23 to the FA (No.2) 2023 also makes amendments to the National Insurance Contributions Act 2022 (NICA 2022),¹⁵ which provided for the possibility of zero-rate secondary Class 1 National Insurance contributions for employees at freeport tax sites under certain conditions. The changes again extend the reliefs available in freeport sites to designated geographical areas within investment zones, by deploying the neutral terminology of “special tax sites” or substituting “freeport conditions” with the more neutrally phrased “applicable conditions”. Whilst the reliefs available remain substantively unchanged, the window within which they are available is again amended to reflect the adjustment in the sunset date, which in the case of the NICA 2022 applied to new employment which did not begin later than 5 April 2026¹⁶. Paragraph 23 of Schedule 23 to the FA (No.2) 2023 inserts a new subsection 2A into the NICA 2022 to provide for a new sunset date in a similar formulation applicable to the reliefs on capital allowances and SDLT, namely “For the purposes of this section “the applicable sunset date”, in relation to a special tax site, means 5 April 2026, or such later date as may be specified under section 332(4)(b) of the Finance (No.2) Act 2023 as the applicable sunset date in relation to the site concerned for the purposes of the provisions mentioned in subsection (4) of that section”¹⁷. Schedule 23 to the FA (No.2) 2023 also omits s3(1) NICA 2022,¹⁸ which would otherwise have provided for a final sunset date within which earnings are to be paid, of 5 April 2031.

What could the implications be?

The idea of freeports is nothing new, neither are investment zones. They are essentially designated geographical areas within which specific tax reliefs are available. Previous incarnations of these ideas include Enterprise zones, first introduced in 1980 and then reintroduced in 2011. The specific provisions in the FA (No.2) 2023 on the designation of special tax sites, and the power to alter the sunset clauses, facilitate the adjustment to

⁹ FA (No.2) 2023 s332(4)(b).

¹⁰ FA (No.2) 2023 s332 (5)(a).

¹¹ FA (No.2) 2023 s332 (5)(b).

¹² FA (No.2) 2023 Sch.23, paras 1 to 8 make several amendments to FA 2003 Part 4 (stamp duty land tax) and Sch.6C (stamp duty land tax: relief for freeport tax sites).

¹³ FA (No.2) 2023 Sch.23, paras 9 to 16 amending CAA 2001 s3, Part 2, Part 2A, s573A, and Part 2 of Sch.1 by essentially exchanging specific references to freeports with new collective neutral terminology which could include either a freeport and / or an investment zone.

¹⁴ FA (No.2) 2023 Sch.23, paras 17 to 19 amending the relevant headings in FA 2001 Part 4 to either include reference to investment zones or substitute references to freeports with the neutral special tax sites phrasing.

¹⁵ FA (No.2) 2023 Sch.23, paras 20 to 27 amending the heading before s1, sections 1 to 3, s5, s12 and s13 NICA 2022.

¹⁶ NICA 2022 s2(1)(a)(ii).

¹⁷ FA (No.2) 2023 Sch.23, para.23 inserting s2A(a) and (b) into NICA 2022 Part 1.

¹⁸ FA (No.2) 2023 Sch.23, para.24.

Government policy seen in the 2023 Spring Budget as part of its levelling up agenda, to encourage regional investment through the addition of investment zones to the already established policy of freeports. The effective replication of the tax reliefs for investment zones which are available within freeport sites, rather than the creation of a new scheme of benefits for the former, is to prevent competition for investment within the UK as between freeports and investment zones. This does not however rule out the possibility of competition between other regions in the UK and newly designated special tax sites, nor does it rule out the possibility of displacement.

These developments in Government policy are said to have been enabled by Brexit,¹⁹ as the UK moves away from EU state aid law obligations.²⁰ However, the reasons why this is exaggerated are twofold: first, EU state aid law does not prevent the existence of designated geographical areas where tax reliefs are available;²¹ and second, in accordance with its obligations under the EU-UK Trade and Cooperation Agreement (TCA),²² the UK has established its own domestic subsidy regime in the form of the Subsidy Control Act 2022 (SCA).²³ Unsurprisingly, a significant proportion of the SCA regime reflects the TCA provisions which are themselves reflective of EU state aid law.

There are also implications for these developments in Government policy under the domestic SCA regime.²⁴ Two of the most pertinent to the FA (No.2) Act 2023 provisions discussed in this note include the prohibition contained in s18 SCA on the relocation of activities, and the subsidy control Principles contained in Schedule 1 to the SCA, specifically Principle F, which is a domestic addition to the Principles contained in the TCA²⁵ and which aims to minimise any negative effects on competition and investment *within* the UK.²⁶

¹⁹ Philip Baker and Dilpreet Dhanoa, “Brexit and the UK Direct Tax System - 18 Months On” [2022] B.T.R. 264, 274.

²⁰ See Glen Loutzenhiser, “Tax and the UK Post-Brexit: Introduction to the Brexit articles” [2022] B.T.R. 253; Philip Baker and Dilpreet Dhanoa, “Brexit and the UK Direct Tax System - 18 Months On” [2022] B.T.R. 264; Philip Baker, “Fiscal subsidy control in the post-Brexit era” [2021] B.T.R. 14; Philip Baker, “Fiscal subsidy control in the post-Brexit era (part 2)” [2021] B.T.R. 361; and Andrea Biondi and Maria Kendrick, ‘How to spend (our) money wisely: The Subsidy Control Act and control of public spending in a post Brexit United Kingdom’, in Katarzyna Gromek-Broc (ed), *Public Law in a Troubled Era: A Tribute to Professor Patrick Birkinshaw*, (Kluwer Law International 2023).

²¹ The usual processes in accordance with Arts 107 and 108 Treaty on the Functioning of the European Union need to be complied with, such as notification to the European Commission. However, this does not prevent the existence, for example, of freeports or free zones https://taxation-customs.ec.europa.eu/free-zones_en [Accessed 26 July 2023].

²² Art.366 Trade and Cooperation Agreement between the European Union and the European Atomic Energy Community, of the one part, and the United Kingdom of Great Britain and Northern Ireland, of the other part [2020] OJ L149/10 (30 April 2021) (TCA) https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv%3AOJ.L_.2021.149.01.0010.01.ENG&toc=OJ%3AL%3A2021%3A149%3ATO%3AC [Accessed 26 July 2023].

²³ Freeports and / or investment zones would arguably fall under the definition of subsidy contained in SCA s2, including “the foregoing of revenue” under SCA s2(2)(c). The inclusion of these provisions in an Act of Parliament may not necessarily provide protection in accordance with SCA s1(7) and in relation to recovery under TCA art.373.

²⁴ As the SCA came into force on 4 January 2023, and the commencement of s331-332 of and Sch.23 to the FA (No.2) Act 2023 was on the day the FA (No.2) Act 2023 received royal assent, being 11 July 2023, the special tax site designations and the alterations to the sunset clauses pursuant to the FA (No.2) 2023 will both occur under the UK domestic subsidy control regime in the SCA.

²⁵ TCA art.366.

²⁶ On which see Andrea Biondi and Maria Kendrick, ‘How to spend (our) money wisely: The Subsidy Control Act and control of public spending in a post Brexit United Kingdom’, in Katarzyna Gromek-Broc (ed), *Public Law in a Troubled Era: A Tribute to Professor Patrick Birkinshaw*, (Kluwer Law International 2023).

The aim of the newly formulated “special tax sites” is to encourage regional investment in specific designated areas. Under s18(1) SCA a subsidy is prohibited if “it is given to an enterprise subject to a condition that the enterprise relocates all or part of its existing economic activities, and the relocation of those activities would not occur but for the giving of the subsidy”.²⁷ Relocation is defined as occurring if an enterprise is carrying on activities in an area in the UK before the subsidy is given and it ceases to carry on those activities in that area after the subsidy is given and carries them on in another area in the UK instead.²⁸ However, under s18(4) SCA the prohibition under s18(1) does not apply if: the effect of the subsidy is to reduce social or economic disadvantages in the area;²⁹ the giving of the subsidy results in an overall reduction in the social or economic disadvantages within the UK generally;³⁰ the subsidy is designed to bring about a change in the size, scope or nature of the existing economic activities of the enterprise.³¹ If the terms of the prohibition in s18(1) SCA are deemed to have been met, there is a potential issue here if the social and economic advantages of levelling up do not materialise sufficiently to invoke the disapplication of the prohibition.³²

There are also the implications of the UK specific additional Principle in Schedule 1 to the SCA.³³ Principle F provides that whilst subsidies should be designed to achieve their policy objective, at the same time they should also minimise any negative effects on competition or investment within the UK.³⁴ The extension of tax reliefs from freeports to investment zones through s331 and s332 FA (No.2) 2023, thereby providing for a replication rather than an alternative selection of tax reliefs, may serve to reduce competition for investment as between freeport and investment zone sites. However, this may not be sufficient to minimise negative effects on competition or investment within the UK as a whole as between areas designated as special tax sites on the one hand and non-designated areas on the other hand. At the time of the passage of the Finance (No.2) 2023 Bill, the Office of Budget Responsibility was quoted in Parliament as having insufficient information to assess the impact of investment zones, including the potential negative impact on other areas in the UK outside of the designated sites.³⁵ Ironically, it is the additional Principle on competition and investment within the UK which may become an issue, and this is not required by the TCA, but is rather a domestic addition.

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²⁷ SCA s18(1)(a) and (b).

²⁸ SCA s18(2)(a) and (b).

²⁹ SCA s18(5).

³⁰ SCA s18(6).

³¹ SCA s18(7).

³² It is not clear but a reasonable reading of s18(4) SCA 2022 is that the conditions in subsections (5) to (7) are cumulative, not either or, but at the time of writing this has yet to be pronounced upon by a court.

³³ SCA Sch.1, Principle F.

³⁴ SCA Sch.1, Principle F.

³⁵ HL Deb 4 July 2023, vol 831, cols 1191-1192.