Response to the consultation on 'International Tax Enforcement: disclosable arrangements'

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Mazars LLP is the UK firm of Mazars, an international advisory and accountancy group. Mazars LLP is registered by the Institute of Chartered Accountants in England and Wales to carry out company audit work.

1. Executive summary

We welcome HMRC's consultation in to the various elements of DAC 6 and in general find HMRC's views as expressed in the consultation helpful and practical. We do, however, still have concerns on the scope of the provisions and the potential for rather trivial and/or benign arrangements to be disclosable, along with arrangements which would already be disclosable to HMRC through existing information provision (necessitating a double disclosure).

With regard to the hallmarks, we have concerns around how disclosure will practically operate for Hallmark E. This Hallmark is not restricted by the main purpose test and so may capture a wide range of arrangements that are consistent with the OECD transfer pricing guidelines and therefore compliant with Part 4 TIOPA 2010. Further guidance from HMRC would therefore be welcome in these areas.

In respect of penalties, it is our view that it is disproportionate to apply the same daily penalty to non-disclosure for failure to disclose arrangements with a main purpose of tax avoidance, as to those arrangements that do not have such a main purpose. The fact that the penalty applies whether the behaviour was deliberate or not does not appear to give a Tribunal or an HMRC officer any discretion in determining the level of the penalty. This again appears disproportionate in the case of an arrangement with a hallmark that does not require obtaining a tax advantage to be a main purpose.

2. Our response to the consultation

2.1 Do you have any suggestions about how HMRC can provide more clarity about when an arrangement will concern multiple jurisdictions?

Paragraph 2.5 of the consultation document indicates that a permanent establishment entering into an arrangement in its own jurisdiction, which only concerns the permanent establishment (such that the jurisdiction where the company is tax resident will not be of material relevance) would not be a cross border arrangement. It would be helpful to have HMRC's view clarified concerning the common situation of the UK permanent establishment (PE) of a foreign enterprise receiving assistance from that foreign enterprise in the form of use of intangibles, marketing, financing or the provision of goods or other services. In this case there may be a direct link between the provision of those goods and services by the foreign enterprise and the arrangement in the jurisdiction of the permanent establishment. We would welcome HMRC's clarification on whether it would still not regard the wholly domestic arrangements as forming part of a cross border arrangement.

Considering permanent establishments further, we note that Article (3) para18(c) of the DAC, concerning the definition of 'cross border arrangements' appears to restrict that definition to circumstances where "the arrangement forms part of the whole business of that permanent establishment". We would welcome HMRC's further guidance on what it considers to be arrangements forming "part of the whole business of that permanent establishment" with reference in particular the provisions of goods and services, use of intangibles and financing.

It would be helpful to have HMRC's view on whether the relocation of a property investment company's tax residence from outside the UK to inside the UK in connection with the April 2020 introduction of UK corporation tax for non-UK companies investing in UK property, would be regarded as a cross border arrangement coming within hallmark E3. An alternative restructuring possibility might be to transfer the business to a newly incorporated UK subsidiary.

The UK property business would be subject to UK income tax prior to the April 2020 change, and corporation tax after that date. With respect to UK commercial property, all gains on that property would be subject to UK corporation tax from April 2019.

2.2 Are there any people who might be caught by this approach to defining 'intermediary', who you think should not be caught?

The definition of an intermediary includes someone who manages the implementation of a cross border arrangement. The consultation document distinguishes between different types of intermediary identifying 'promoter' and 'service provider'. Neither of these terms are identified in the draft regulations or the EU directive.

If a UK tax adviser provides tax compliance services to a newly incorporated company after having undertaken money laundering checks, but without knowledge of the background on whether the company was established in the UK as part of a reportable cross border arrangement – would that adviser be regarded as helping to implement the

arrangement (a ‘promoter’ in consultation terms) or not (and therefore only a ‘service provider’ in consultation terms)?

2.3 Does this definition of intermediary risk not catching certain types of intermediary who should be caught?

None that we can think of, subject to clarification of the point at question 2.

2.4 Do you identify any particular practical challenges with regard to HMRC’s approach to identifying intermediaries, and what information they have in their knowledge, possession or control?

Without clear operational rules distinguishing between HMRC’s definition of ‘promoter’ and ‘service provider’ it may in our view be easy for HMRC operational staff to mix the two categories.

2.5 Do you have any other comments about the definition of intermediary and who will be caught under the proposed rules?

If an intermediary considers themselves in the category of a ‘service provider’ who does not need to disclose, the taxpayer may need to report under the requirements. An intermediary in this position may have little evidence to demonstrate that he could not have known of a reportable arrangement – other than the fact that he does not have the information. Does HMRC expect intermediaries in this situation to make clear to each client whether it considers itself to be a ‘promoter’ or ‘service provider’ so that the client is clear on whether an intermediary is liable to disclose?

2.6 For the purposes of the ongoing requirement on relevant taxpayers, do you agree that a relevant taxpayer should be regarded as participating in the arrangement in any year where there is a tax effect or where it could reasonably be expected that there would be a tax effect in a subsequent year?

This requirement would create an on-going requirement to report for as long as an enterprise existed where the hallmark for disclosure was E3. This seems unduly onerous, particularly where the arrangement has no tax avoidance purpose in the first place.

2.7 Do you agree that the amount of evidence required for intermediaries and taxpayers to satisfy themselves and HMRC that all the necessary information has been reported is appropriate?

In our view the lack of an obligation for one disclosing intermediary to pass on the full information to another intermediary, will lead to multiple disclosures of the same arrangement, possibly all with slightly different disclosures. This would seem to create a lot of duplication.

The ability of intermediaries and taxpayers to satisfy themselves that all necessary information has been reported will depend on the availability of guidance on how to interpret the hallmarks (which can be very widely interpreted) and the consistency of each relevant jurisdiction’s guidelines. Our comments on other consultation questions may be relevant here (for example question 19).

2.8 Do you think that the approach to defining the main benefit test and tax advantage is proportionate?

It is our view that the UK implementing rules should apply EU DAC6 rules in line with EU Directives, so that the expansion to cover taxes of other jurisdictions is an unnecessarily onerous broadening of the scope of the definition of 'tax advantage' for the purpose of applying the hallmarks listed in EU DAC6.

It is not unusual for certain tax work to be charged for based on the tax savings achieved. Examples of this type of service in the UK could include for capital allowances and R&D tax relief. Ordinarily the achieving of such 'tax advantages' is entirely in line with the policies behind the provisions. There may be circumstances where R&D work between group companies with one being in the UK and another overseas, results in an ability to claim R&D tax relief in both jurisdictions for what effectively amounts to the same expenditure according to the tax rules of each jurisdiction, because neither jurisdiction has taken account of how their R&D tax relief rules interact with those of the other jurisdiction. Would such a cross border arrangement and the tax advantage arising be considered to be entirely within the policy objectives of those provisions for the purpose of the main benefit test?

If the group already has entities in the two relevant jurisdictions (where it was possible to claim R&D relief in both jurisdictions) and cross border R&D work is undertaken, would the fact that the entities and relevant staff are located in those jurisdictions mean the arrangement would fail the main benefit test? If that is the case, how would a group be treated for the purpose of the main benefit of obtaining a tax advantage test (if its competitor already established there was obtaining, or could obtain, favourable tax advantages) – if it located a new subsidiary in the relevant overseas jurisdiction for the purpose of undertaking the R&D work?

2.9 Do you have any comments on the approach set out for hallmarks under Category A?

The comment at paragraph 8.15 implies that an arrangement achieving a tax advantage not consistent with the underlying legislative intent could still be caught. However in a cross border arrangement the legislative intent of one jurisdiction can by definition only consider the rules as they apply to entities in that jurisdiction. How is one to apply the 'legislative intent' consideration where two (or more) different jurisdictions' legislative intent needs to be considered?

2.10 Do you have any comments on the approach set out for hallmarks under Category B?

No further comment at this stage.

2.11 Are there any points in the definition of associated enterprise which you think require clarification or explanation in guidance?

We agree the definition of 'associated enterprise' for the purpose of EU DAC6 is clear. However there are different definition of 'associated' enterprises in different parts of the UK tax legislation, so we would hope that clarification on the definition of 'associated for EU DAC6 purposes will be included in any guidance.

2.12 Do you think the above approach will prevent unnecessary reporting of benign activities, while avoiding loopholes that could enable intermediaries and/or relevant

taxpayers to avoid their reporting obligations? If you foresee problems with this approach, please provide details of possible solutions.

No further comment at this stage.

2.13 Do you think that this approach will also work for dealing with Collective Investment Schemes? Alternatively, what other approaches do you think would be better?

No further comment at this stage.

2.14 Do you think particular guidance is needed in respect of hallmark C(3)?

No further comment at this stage.

2.15 Do you agree that this hallmark should refer to the amount treated as payable for tax purposes? What do you think are the advantages and disadvantages of this approach, and of any other suggested approaches?

How would this hallmark apply to a reorganisation involving two other member states and the UK in a situation where TCGA 1992 s140A applies, so that for UK tax purposes the acquisition and disposal consideration was treated as made at nil gain/nil loss, but the arrangement resulted in a different taxable consideration in one of the other jurisdictions? Could such a transfer result in an overlap between hallmarks C4 and E3 so that both hallmarks would need to be disclosed?

2.16 Do you have any general comments about the approach to hallmarks under category C?

The comment in the consultation document at paragraph 10.15 for C(1)(d) with respect to preferential tax regimes may need further clarification. If the preferential regime (for example patent box, or special economic zones) is a measure entirely within the stated policy, how could it result in a disclosable arrangement under hallmark C1(d) as there would presumably be no main benefit?

It will be helpful to have further guidance on the interpretation of the 'main benefit' test with practical examples illustrating HMRC's view in 'grey areas' concerning the possible application of hallmarks C(1)(b)(i), C(1)(c) and C(1)(d).

2.17 Do you have any comments about the approach to hallmarks under Category D?

No comment at this stage.

2.18 Where an arrangement relates to companies which are resident for tax purposes in jurisdictions where corporate tax applies at the group level, should hallmark E(3) similarly apply at the level of the sub-group located in that jurisdiction or at the company level? What would be the particular advantages or disadvantages of applying the rules at the group level?

Our view is that the approach should be consistent across the EU.

2.19 Do you have any comments about the approach to hallmarks under Category E?

The comment at paragraph 12.1 that hallmark E seeks disclosure of arrangements that are contrary to the OECD's transfer pricing guidelines does not seem to take account of the fact that the hallmarks contain no such qualification (in other words the arrangements can

be wholly consistent with the OECD's transfer pricing guidelines and still require disclosure). A specific qualification in the UK regulations would therefore be welcome to this effect or otherwise a recognition from HMRC, for the avoidance of doubt, that the hallmarks under Category E are not so restrictive in their application. We would note in the latter case that this may result in a far more significant level of disclosures, noting that hallmark E is not restricted through meeting the "main benefit test" and that tax authorities should already have access to information on E2 and E3 hallmarks through financial statements or corporate income tax returns.

Hallmark E1 requires disclosure of the application of unilateral safe-harbour provisions. It would be very helpful to understand HMRC's approach to what is a 'unilateral safe-harbour' provision.

For example the latest OECD transfer pricing guidelines at chapter 4 section E2 para 4.102 comments *"…A safe harbour in a transfer pricing regime is a provision that applies to a defined category of taxpayers or transactions and that relieves eligible taxpayers from certain obligations otherwise imposed by a country's general transfer pricing rules. A safe harbour substitutes simpler obligations for those under the general transfer pricing regime…."* At section E1, the guidelines say: "*It should be recognised that a safe harbour provision does not bind or limit in any way any tax administration other than the tax administration that has expressly adopted the safe harbour."*

The UK legislation has adopted the latest OECD transfer pricing guidelines (TIOPA 2010 s164). The guidelines include the possibility, for example, of using a simplified basis for low value intragroup services (D2 of chapter VII of the 2017 OECD transfer pricing guidelines)." This is described in HMRC's manuals at INTM440071 and would therefore appear to be acceptable from a UK perspective.

Although other countries may in practice apply the OECD transfer pricing guidelines, we understand it is not in all cases clear that their legislation has adopted the OECD transfer pricing guidelines and they may not have anything explicit on safe-harbour provisions for low value intragroup services. For example, we understand this is the case with Germany.

If a cross border arrangement involves a UK and a German enterprise for example and the UK enterprise, as part of those arrangements, adopts the OECD approach to low value adding services, this could then be interpreted as an arrangement which involves the use of unilateral safe harbour rules. If this interpretation were correct the arrangement would be disclosable.

We can see a number of technical interpretations as to why any simplified approach approved in the OECD Guidelines should not be regarded as unilateral safe harbour (for example that the Guidelines are themselves the general transfer pricing rules in the UK). We would however welcome HMRC confirmation that following any simplified approach approved within the OECD Guidelines (and their approach to low value adding services in particular) would not fall within hallmark E1.

As noted at question 1, would the incorporation of a non-resident landlord UK property business in response to the introduction of UK corporation tax from April 2020 result in a required disclosure under hallmark E3?

We would also welcome confirmation of HMRC's view in the case of a business which disposes of assets or a part or all of its business to a third party with the intention of distributing the proceeds to its parent in another jurisdiction. This could be part of a wholly commercial decision to de-risk a business in the vendor jurisdiction (and reinvest in the parent jurisdiction in the longer term or otherwise be part of a partial exit. There would be the possibility of reinvesting in a similar or new business in the vendor jurisdiction instead of the parent jurisdiction.

In this situation, the asset sale to a third party would appear to be part of an arrangement involving a cross-border transfer of assets (the subsequent distribution) after which the EBIT of the transferor could be expected to be less than 50% over the three year reference period had the transfer not been made (for example if the proceeds had been reinvested in the business rather than distributed). Does HMRC consider such arrangements as meeting hallmark E3?

2.20 Do you have any suggestions for how the penalty regime could be improved?

As the hallmarks include arrangements that do not need to have the obtaining of a tax advantage as a main benefit, it seems disproportionate to apply the same daily penalty to non-disclosure for failure to disclose these arrangements as for those arrangements with a hallmark which does have tax avoidance as a main purpose. The fact that the penalty applies whether the behaviour was deliberate or not does not appear to give a Tribunal or an HMRC officer any discretion in determining the level of the penalty, which again appears disproportionate in the case of an arrangement with a hallmark that does not require obtaining a tax advantage to be a main purpose.

2.21 Do you have any particular comments about the commencement rules, and HMRC's approach to dealing with the backdated reporting requirements?

No further comments at this stage.

2.22 Are there any particular areas of DAC 6 that you would like HMRC to provide guidance on, which are not covered elsewhere in this consultation?

We have noted some areas in response to the above questions and may have further points which we wish further clarification on.

3. About Mazars LLP

Mazars LLP is an international, integrated and independent organisation, specialising in audit, accountancy, tax, legal and advisory services. Mazars LLP and its correspondents operate throughout 89 countries and territories. Mazars LLP is an integrated partnership drawing on the expertise of over 23,000 professionals to assist major international groups, SMEs, private investors and public bodies at every stage of their development.
Mazars LLP has a large client base with clients of all sizes, from SMEs to mid-caps and global players, as well as start-ups and public organisations at every stage of their development. Mazars is ranked the 8th largest UK partnership by audit fee income and we are also one of Europe's largest accounting firms with a huge global presence. Mazars in the UK has over 1,700 employees and around 140 partners.
Mazars is a member of Praxity AISBL, the world's largest Alliance of independent and unaffiliated audit and consultancy companies. Recognising the support arising from globalization we are able to recommend renowned companies in significant countries. Our contacts to these Praxity participating firms enable our clients a professional support in their transnational activities from a single source.

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