The City of London Law Society

4 College Hill
London EC4R 2RB
Tel +44 (0)20 7329 2173
Fax +44 (0)20 7329 2190
DX 98936 – Cheapside 2
mail@citysolicitors.org.uk
www.citysolicitors.org.uk

Adrian Morton
HM Revenue & Customs
Level 5
1 Ruskin Square
Croydon
CR0 2LX
uncertaintaxtreatmentconsultation@hmrc.gov.uk

27 August 2020

Dear Mr Morton,

RE: CITY OF LONDON LAW SOCIETY'S RESPONSE TO NOTIFICATION OF UNCERTAIN TAX TREATMENT BY LARGE BUSINESSES

Please find below The City of London Law Society's ("**CLLS**") response to the HM Revenue & Customs ("**HMRC**") consultation document entitled "Notification of uncertain tax treatment by large businesses" (the "**Consultation**").

INTRODUCTION

The CLLS represents approximately 17,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi jurisdictional legal issues.

The CLLS responds to a variety of consultations on issues of importance to its members through its 17 specialist committees. This response to the Consultation has been prepared by the CLLS Revenue Law Committee. The current members of the committee are herewith:-

http://www.citysolicitors.org.uk/clls/committees/revenue-law/revenue-law-committee-members/

We would like to preface our response by questioning whether an additional compliance and reporting burden on large business to address the legal interpretation tax gap is appropriate or necessary. The 'legal interpretation' part of the 'tax gap' necessarily involves situations where the taxpayer reports on a basis that is too favourable as a matter of law, but it is not clear that a reporting obligation of this kind would be necessary or proportionate to deal with this issue:

a) If the taxpayer has filed on a basis that is legally correct, then there is in no sense a 'gap' here, even if HMRC might disagree with the taxpayer's view.

b) There would be a legitimate concern for circumstances where the taxpayer is not right, but where the point does not surface in a way that enables HMRC to test and prove its view. However, in our view the existing legal framework of tax compliance already adequately incentivises taxpayers not to take overly aggressive positions in their returns. The existing framework provides for extended time periods, and penalties, if you are careless (or worse) in your reporting. In our experience taxpayers in the large business community (at which this measure is aimed) generally respond very well to those incentives. That is particularly so, given that we can see HMRC using those levers more now than they have in the past.

Overall, we consider that HMRC's existing policies and powers to investigate large business taxpayers, combined with the cooperative relationships that many large businesses have with HMRC, ought to be sufficient to ensure that any such 'legal interpretation' gap is minimal. Our responses to the questions below should therefore be read in this light.

1. Do you think the suggested threshold criteria are suitable for the requirement to notify?

Clear definition needed on when uncertainty exists. If, contrary to our recommended position, additional reporting obligations are to be legislated then specific reporting triggers (reflecting the situations when HMRC is likely to disagree with a treatment) should be legislated (see question 9 below for suggestions on how this could be drafted):

(a) The judgement of whether HMRC might disagree with the treatment will often be a difficult one, as taxpayers are not in a position to know what HMRC would think of any given transaction or treatment. HMRC's published guidance can provide an indication of HMRC's view, but where clear guidance is available our experience is that large business taxpayers will seldom take a contrary position. In the absence of clearly applicable guidance, guessing HMRC's preferred view on any given technical issue is not as simple as selecting the interpretation that produces the most tax, as any particular interpretation can produce more or less tax for different taxpayers or in different circumstances. The question whether this a position HMRC is likely to disagree with or challenge naturally raises the question who do we mean by HMRC, given it is not a single person but a multitude of individuals with a wide range of views, and what do we mean by challenge? Is a notice of enquiry a challenge? If so, that's calling for a subjective judgment on the relevant CCM/HMRC personnel and what they are likely to do. Is it asking the taxpayer to predict whether if there is an enquiry, but the relevant facts come out and the right HMRC specialists are engaged, the enquiry will be closed with no adjustment? Or that it thinks the case team would likely propose an adjustment but that would/would not be endorsed by TDRB, or the DPT board, or transfer pricing board, and would/would not be something HMRC would be prepared to litigate? And if that's the test, do we assume HMRC will have taken appropriate advice from Counsel etc. when we are hypothetically applying the Litigation and Settlement Strategy (referred to in para 2.4 of the Consultation). We feel it is important to emphasise how difficult we expect this to be in practice.

(b) A definition of when uncertainty exists should be as clear and easy to apply as possible. Minimising the compliance burden ought to be a key consideration, as taxpayers and advisers are already struggling to meet burdensome DAC 6 compliance obligations covering similar ground.

(c) The consultation document contains different formulations which would in practice impose quite different thresholds. In particular, "HMRC may not agree" (para 2.6) is not the same as "HMRC is likely to challenge" (para 3.7). There will be far more situations where a corporate would expect challenge and testing as part of HMRC's corporation tax compliance approach, and far fewer where even after full debate and involvement of specialist teams HMRC would not agree. This in particular should be clarified.

2. Do you think there are any other areas that should be excluded from the notification regime?

Exclusions to prevent overlap with all mandatory and optional disclosure regimes. The proposal to have exclusions from the notification requirement where there would be overlap with existing disclosure regimes is welcomed. To minimise compliance burden, this should be extended to all other instances where a transaction or treatment may be disclosed to HMRC, including where a transaction is disclosed under DAC 6 or DOTAS, or is described to HMRC as part of the transparent relationship required by the Banking Code of Conduct. Additional exceptions should be available where the treatment is covered by a formal clearance including an APA.

The proposed exception where CCMs have been given information is welcome to deal with less formal disclosures by large business taxpayers as part of their general relationship with HMRC. However, the requirement for a CCM to confirm in writing that sufficient information has been provided appears unduly cumbersome and we would recommend that an exception be made where taxpayers can reasonably conclude that sufficient information has been provided. The approach could, perhaps, be modelled on section 92(7)(c) Finance Act 2015 (which provides a similar exception from the obligation to notify of potential liability to diverted profits tax).

Transfer pricing uncertainties should be excluded or carry a reduced disclosure obligation as to quantification. International businesses would be subject to a large additional compliance burden if it was necessary to disclose transfer pricing uncertainties. In the field of transfer pricing it is also particularly difficult to disclose a number quantifying the tax at stake, given there will generally be a range of possible outcomes in the arm's length range. As such, either reporting without a quantification element, or including flexible alternatives for quantification would be appropriate – for instance, options to disclose either the size of the provision in the accounts, or some other metric that could give an indication of the importance of the issue.

Exception for disclosures that would disclose legally privileged information. Taxpayers should not be required to disclose any details that would betray legally privileged information. For instance, if a taxpayer has received legal advice on the arm's length range of pricing for a transaction, the disclosure requirement should not involve the taxpayer effectively reporting the range of prices described in the advice. Similarly, the description of the uncertainty must not require the taxpayer to describe alternative interpretations of the law on which the taxpayer has received privileged advice. This illustrates the need for the disclosure to be flexible.

Taxes other than corporation tax. HMRC should consider carefully which taxes other than corporation tax are material to the legal interpretation gap and not expand the scope of this regime wider than is necessary to capture material areas of concern.

3. Do you think the definition and principles in IFRIC23 are appropriate to be used for the requirement to notify?

The concepts used in IFRIC23 as regards:

- whether an entity considers uncertain tax treatments separately;

- the assumptions an entity makes about the examination of tax treatments by HMRC; and
- how an entity considers changes in facts and circumstances, and perhaps even subsequent case law,

could be appropriate as a basis for the proposed rules. However, a clearer legislative definition of when uncertainty exists would be appropriate (as noted above; see also question 9).

4. Do you think there would be any problems with the person considering whether notification is required, being different to the SAO?

No comment

5. Do you think the proposed de minimis threshold of £1m is reasonable for the notification of uncertain tax treatment?

We support the inclusion of a de minimis threshold but have no strong views on how precisely that threshold should be set.

6. Do you believe there are strong arguments for a materiality threshold?

No comment

7. Do you envisage problems determining the £1m threshold for indirect taxes, particularly VAT?

No comment

8. If so, can you suggest how these problems could be mitigated?

No comment

9. Do you consider that it would be beneficial to supplement the main requirement with a specific list of indicators of uncertainty?

In paragraph 3.21 of the Consultation Document, HMRC describe specific examples where they consider there is an uncertainty. Specific reporting triggers reflecting the situations where HMRC is likely to disagree with a treatment should be legislated, and this should be a standard which can be applied by taxpayers by reference to HMRC's publicly stated views. These reporting triggers could include, as noted in the Consultation Document:

- Adoption of a tax treatment which is under dispute in the courts,
- Adoption of a treatment which is contrary to HMRC's stated view in a VAT Brief or Statement of Practice.
- Adoption of a treatment where HMRC clearance was requested and was not given,

but in each case we feel strongly that the triggers **must be in the public domain**. A dispute in the courts at first instance will not be generally known, for example.

10. Do you agree with the proposed examples, and do you have any others which you consider would be helpful?

No comment

11. Do you think the SAO certification process is appropriate for the notification requirement?

To minimise compliance burden, the timing of the notification requirements should be aligned with the filing of the relevant tax return. The SAO certification process is likely to be too soon after the end of an accounting period for the required information to be prepared.

12. Would reporting VAT and PAYE issues occurring in the tax year, rather than in the accounting period for the company, cause any significant difficulties?

No comment

13. What alternative person could be responsible to make the notification for large partnerships?

No comment

14. Alternatively, what process (other than the SAO) could be used for a single, annual notification?

No comment

15. For each relevant tax, what information do you think could be reasonably provided as part of the notification requirement, in addition to a concise description and indication of amount?

No further information should be required. As noted above, the level and form of disclosure should be flexible to protect legal privilege and to recognise that quantification can be highly challenging (e.g. for transfer pricing issues).

16. Do you think there are any common disputes, that due to the complex nature of such disputes, where specific documents or information should be provided alongside the notification?

No comment

17. Do you think the principle and quantum of the existing SAO penalty regime is sufficient for the integrity of the notification requirement?

HMRC should specify clearly in guidance that, at the very least in the first years to which this legislation applies, they would not intend to impose penalties in respect of failure to notify a treatment where a reasonable and good faith attempt has been made to determine whether that treatment falls within the regime. This is particularly the case as the regime will apply to (amongst other things) corporation tax returns for accounting periods ending on or after 30 April 2020 (see paragraph 1.4), which will include transactions carried out before the legislative detail is published and in some cases before the consultation document was published.

18. Regarding the penalty in 6.3.2, who do you think should be liable to a penalty, the person liable to notify or the entity, and, if more than one (legal) person, in what circumstances, and to what quantum, would these persons be culpable/liable?

No comment

19. Do you have any comments on the assessment of equality, and other impacts?

No comment

POINTS OF CONTACT

Should you have any queries or require any clarifications in respect of our response or any aspect of this letter, please feel free to contact me by telephone on 020 7296 5783 or by email at Philip.harle@hoganlovells.com.

Yours faithfully

Philip Harle

Chair City of London Law Society Revenue Law Committee