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What is the current thinking with respect to U.K. laws, regulations or other pronouncements that have been issued [or proposed] with respect to the relevant BEPS Actions (8–10, 13)?

The U.K. has laid claim to being a leader in the development of the BEPS Action Plan and in implementation of the anti-avoidance measures arising from the project. Tax avoidance and aggressive tax planning by large multinational groups have attracted enormous media attention in the U.K. since the financial crisis of 2008 and it has been publicly expedient for the U.K. government to be seen to be leading the charge to tackle such action, while simultaneously courting international business through setting out plans to cut the corporation tax rate to 17% by 2020.

HM Treasury states in its "Business tax road map" that:

> The government successfully helped initiate the G20-OECD BEPS project, and worked with G20 and OECD partners to bring this to a successful conclusion in October 2015. The BEPS project represents a major effort to reform the international tax system.[1]

A. Diverted Profits Tax

The British government has raced to place the U.K. at the forefront of nations adopting the BEPS recommendations, even going so far as to jump the gun in advance of the U.K. general election of 2015 through the Chancellor of the Exchequer's announcement on December 3, 2014 of the intention to introduce the Diverted Profits Tax (DPT) before the BEPS reports had been finalised, causing some alarm, both among the business community and within the OECD.

The DPT (known colloquially as the "Google Tax") was introduced by the Conservative-led Coalition government in the pre-election Finance Bill in 2015 to *"target the contrived arrangements used by multinationals to artificially shift profits to low or no-tax locations where there is little or no economic activity."*[2] The tax came into effect from April 1, 2015 and HM Treasury claims that evidence is already emerging of large businesses changing their behavior as a result and paying tax more in line with their economic activities in the U.K..

Asked about the OECD's reaction to the U.K.'s introduction of the DPT, Pascal Saint-Amans, Director of the OECD's Centre for Tax Policy and Administration, stated:

> It is an embarrassed view, I must say. We have sympathy for the need to move and there is an electoral context . . . where the government, which has been very instrumental in supporting BEPS in raising the profile of this project, wanted to show that it was acting very, very quickly – even before the time line of the BEPS project, which is after a very important electoral date in the UK.
>
> On the other hand, unilateral actions are not exactly in the sense of what we are trying to develop, which is, 'Let's wait for a comprehensive package and then countries will decide'. You are sovereign; you will decide what to do. But you will be better informed with better instruments and with a lesser risk of having disruptive actions, which might push other countries . . . to take unilateral measures, which are not that great when you are negotiating a multilateral package.[3]

The British government was also widely criticised by the business community. John Cridland, Director General of the Confederation of British Industry, was quoted at the time of introduction as saying:

> "It is unfortunate that the UK has decided to go it alone with a diverted profits tax, outside this process, which will be a real concern for global businesses. The legislation will be complex to apply, and if other countries follow suit businesses will have a patchwork of uncoordinated unilateral rules to navigate, which risks undermining the whole OECD approach."[4]

Although HM Revenue & Customs (HMRC) claims that the impact of DPT is limited to those large business and multinational enterprises that are using contrived arrangements to divert profits, with the names of such companies as Google, Amazon and Starbucks being referred to in this context in the press, in reality the tax has caused considerable consternation among

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much smaller taxpayers, concerned that they may inadvertently be caught by the tax, resulting in a widespread increased compliance burden as numerous groups conduct reviews to assess their exposure.

B. Actions 8–10

Following the publication and approval of the BEPS reports, the subsequent Conservative government has swiftly legislated in respect of the outcomes of both Actions 8–10 and Action 13.

With respect to Actions 8–10 the government legislated, in the current Finance Bill, to update the existing links in the U.K.'s transfer pricing rules, in section 164(4) Taxation (International and Other Provisions) Act 2010 and section 357GE(1) Corporation Tax Act 2010, to the OECD Transfer Pricing Guidelines, to incorporate the revisions to the Guidelines agreed in the final Actions 8–10 Report ("as revised by the report, Aligning Transfer Pricing Outcomes with Value Creation, Actions 8–10 – 2015 Final Reports, published by the OECD on October 5, 2015").[5] This maintains the links between the U.K. rules and the OECD Transfer Pricing Guidelines, ensuring consensus on the practical application of transfer pricing principles.

The measure has effect for accounting periods beginning on or after April 1, 2016. Nonetheless, even in advance of the incorporation of the revisions to the Guidelines into British law, HMRC's advice to practitioners was to apply the new OECD guidance to transfer pricing matters. Maura Parsons, Deputy Director and Head of Transfer Pricing at HMRC, stated on February 9, 2016 that the advice being giving by HMRC to taxpayers was to look at clarifications on transfer pricing as set out by the OECD's report of October 5, 2015.[6]

Given the explicit connection between the interpretation of British legislation and the Guidelines, in the U.K. conflict is generally avoided between domestic legislation and the contents of the Guidelines. The changes to the Guidelines arising from the final BEPS report are considered on the whole to provide greater clarification, rather than a changed interpretation, of the U.K.'s transfer pricing rules, although there are certain aspects of Actions 8–10 which perhaps go beyond the arm's length principle, for example parts of the guidance on hard-to-value intangibles, and which therefore probably cannot be incorporated into U.K. law simply through the statute's being "read" in a certain manner.

C. Action 13

One possible area of conflict remains in respect of the new Chapter V of the Guidelines, on documentation, and whether it is in fact recognized in British law. Chapter V appears to have been excluded, presumably by design rather than by oversight, from the updates to the chapters of the Guidelines that the U.K. legislation recognizes. As we have seen, in the current Finance Bill, the U.K. updates its definition of the OECD Transfer Pricing Guidelines to incorporate the revisions arising from BEPS Actions 8–10. However, no reference is made to BEPS Action 13, in which Chapter V of the Guidelines has been fully revised.

Whereas the U.K. has taken steps to adopt country-by-country (CbC) reporting in The Taxes (Base Erosion and Profit Shifting) (Country-by-Country Reporting) Regulations 2016, these do not give effect to the incorporation of the whole of the revised Chapter V in interpreting U.K. law. It would appear to mean that the U.K. now recognizes in its domestic legislation an idiosyncratic version of the OECD Guidelines that accepts in large part the most recent 2015 revisions, but rejects the latest Chapter V, for which the 2010 chapter will still apply.

1. Country-by-Country Reporting

The Taxes (Base Erosion and Profit Shifting) (Country-by-Country Reporting) Regulations 2016 give effect in the U.K. to the OECD CbC reporting guidance set out in "Transfer Pricing Documentation and Country-by-Country Reporting, Action 13: 2015 Final Report" published on October 5, 2015. The U.K. was the first country formally to commit to implementing the CbC reporting template when it was published by the OECD in September 2014. Once again the government has swiftly legislated, and requires U.K. multinationals to file the template with HMRC for 2016 accounting periods onwards, in its desire to be seen as leading the field in combatting avoidance.

The legislation came into effect on February 26, 2016 and requires parent entities of multinational enterprises with consolidated group revenue of €750million or more to complete the CbC reporting template, with the stated purpose of improving transparency between business and tax authorities and providing useful information that allows for an effective assessment of risks to tax systems arising from aggressive tax planning.[7] Submission of the first reports is due by the end of 2017. CbC reporting is seen by business as the most immediately impactful of the measures arising from BEPS and this has many groups preparing draft CbC reports in advance of filing next year.

The British government has made it known that it is a supporter of the European Commission's (EC) proposal for public country-by-country reporting. HM Treasury states in its "Business tax road map" that:

> "The government believes there is an opportunity to go beyond the outcomes of the BEPS project and enhance transparency over multinationals' tax affairs by requiring them to make the details of tax paid publicly available on a country-by-country basis. The UK will therefore press the case for public country-by-country reporting on a multilateral basis."[8]

Whether that commitment survives the U.K.'s historic vote on June 23, 2016 to leave the European Union (EU) remains to be seen. Even if the EC's proposal for public country-by-country reporting goes on to be approved by the EU (Germany is known to oppose the measure), the U.K. may no longer fall within the purview of the proposed Directive. As an advocate of public country-by-country reporting hitherto, it will be interesting to see whether the British government introduces it unilaterally under new leadership. During debate on the current Finance Bill on June 28, 2016, such a proposal by a group of politicians was defeated on the back of fears that it would disadvantage U.K. business at a time of increased uncertainty. Finance Secretary David Gauke stated that the U.K. is committed to improving the transparency of multinational tax affairs but supports *"an effective multilateral approach."* [9]

The new U.K. CbC reporting legislation deviates significantly from the template of the OECD model legislation and has introduced a pragmatic, though not entirely unique, interpretation of secondary reporting, through the creation of measures that require submission of a restricted "U.K. country-by-country report" (UK CbC Report) by a U.K.-resident group entity in situations where a full CbC report is not received in respect of non-U.K. headed multinational groups.[10] The UK CbC Report contains details only of U.K. entities in a multinational group and their subsidiaries and excludes all other group entities.[11]

Subsequent to the U.K.'s introduction of its CbC reporting regulations, the Council of the EU approved amendments to Directive 2011/16/EU, introducing a specific requirement for CbC reporting for accounting periods commencing on or after January 1, 2016. The Directive mandates the introduction of secondary reporting for accounting periods commencing on or after January 1, 2017 but leaves it to the discretion of the Member State whether secondary reporting is required for prior accounting periods. The U.K.'s acceptance of a UK CbC Report under secondary reporting circumstances would appear to be overruled by the EU Directive from 2017, as the latter specifies submission of a full CbC Report under secondary measures. The Directive requires that *"A Constituent Entity resident in a Member State as defined in the first paragraph of this point shall request its Ultimate Parent Entity to provide it with all information required to enable it to meet its obligations to file a country-by-country report, in accordance with Article 8aa(3)."*[12] Only time will tell whether the U.K. considers it necessary to change its newly created law to comply with the EU Directive, an uncertainty exacerbated by the outcome of the U.K.'s referendum to leave the European Union. On August 2, 2016, HMRC clarified that the U.K. will amend its CbC reporting rules to bring partnerships into scope as reporting entities, in line with the new OECD guidance published on June 29, 2016, whereas it has remained silent on the question of secondary reporting, hinting that it considers no changes necessary in that area.[13]

The UK's CbC reporting regulations allow for the possibility of surrogate filing by a U.K. subsidiary entity of a foreign parent. Given the U.K.'s extensive network of double tax agreements, this facility had created interest in the tax community, specifically with reference to U.S. multinational enterprises (MNEs) seeking a surrogate filing entity as a result of the deferred U.S. adoption of CbC reporting (for periods commencing on or after July 1, 2016). The U.S. was understood still to be debating whether it would accept voluntary filing of CbC Reports for years commencing January 1, 2016, but in the absence of this concession, the U.K., with its common language, was likely to be a favoured surrogate jurisdiction for CbC filing.

However, the OECD's publication on June 29, 2016 of *Guidance on the Implementation of Country-by-Country (CbC) Reporting* has unveiled the possibility of "parent surrogate filing," whereby jurisdictions not immediately implementing CbC reporting for fiscal periods from January 1, 2016 may be able to accommodate voluntary filing from ultimate parent entities resident in their jurisdiction. Japan, Switzerland and the United States have confirmed that they will offer the opportunity for such parent surrogate filing for periods commencing from January 1, 2016, which will no doubt reduce significantly the number of MNEs seeking to employ a surrogate filing entity in the U.K.. HMRC had previously estimated that 100 U.K. constituent entities of non-U.K. headed MNEs would be required to complete a template for a short period, expected to be a year, until the heads of those MNEs started to report their results in their country of residence.[14]

The Regulations state that the CbC Report will be in a form yet to be determined, although it is inconceivable that it will differ in any material way from the OECD template. HMRC indicated in the explanatory memorandum to the draft regulations in October 2015 that electronic filing of the CbC Report would be introduced, and that the form and content of the report will follow the template developed by the OECD, with the result that advisory firms and software providers are already jostling for space to supply that reporting niche.[15]

2. Master File and Local File

The new U.K. legislation makes no reference to master file or local file, but the same explanatory memorandum to the draft regulations last October made clear that HMRC believe they have the power already to demand the provision of such files if required.[16] It is understood from HMRC that they are still debating as to what should be the contents of the master file and local file. Presumably we shall hear about this in the future with a view to the formal introduction of transfer pricing documentation along the lines of the OECD's three-tiered hierarchy.

3. Value Chain Analysis

One subject arising from BEPS Action 13 that has animated the U.K. tax community is the opportunity presented for applying the concept of "value chain analysis" in support of the transfer pricing analysis, a consequence of the group-wide disclosure of business activities in the CbC Report and the specification for a general description of the "important drivers of business profit" in the OECD master file.[17] In fact, as already discussed, the U.K. does not appear to recognise the elements of the new Chapter V relating to master file in its legislation, but elsewhere we do find HMRC showing an interest in value chain analysis, as in HMRC's DPT guidance on the documentation to be submitted with a notification to HMRC that a company is potentially within the scope of DPT, which includes *"a value chain analysis of the complete activity undertaken by the group."*[18]

Multinational enterprises are being urged by practitioners to undertake a thorough value chain analysis of their group. One of the Big Four accounting firms even went so far as to claim on its website that *"VCA is no longer just best practice, but required practice."* What a value chain analysis actually consists of, however, the level of authority that it conveys and how it is to be presented are questions that are open to endless interpretation, in the absence of any official guidance.[19] The debate on the substance and merits of value chain analysis is likely to continue, while practitioners and businesses consider how and in what situations it is to be applied.

D. Future Developments

Looking to the future, the U.K. continues to participate in the ongoing work at the OECD subsequent to the BEPS Project to develop further the OECD Transfer Pricing Guidelines and in its own words it *"continues to call for targeted measures to be introduced to protect them from abuse."*[20]

Notwithstanding this previously stated position, the full tax implications of the British vote to leave the EU and the effect that this will have on the U.K.'s response to BEPS will not be known for some time. Tensions have already emerged as new policy is shaped by conflicting impulses. In the immediate aftermath of the referendum, the (then) Chancellor of the Exchequer informed the Financial Times that he wanted to set the lowest corporation tax rate of any major economy, announcing a target of less than 15%, to prove to investors that the country is still *"open for business."* [21] This is likely to cause nervousness in some quarters. Pascal Saint-Amans is quoted by Reuters, in an internal OECD memo, as saying that the consequences of Britain's departure from the EU *"may push the UK to be even more aggressive in its tax offer"* but that further steps in that direction *"would really turn the UK into a tax haven type of economy."*[22] Since being appointed to the role of Chancellor, Philip Hammond has announced plans for a "fiscal reset," although no specific policy details are anticipated until the Autumn Statement.[23] Any such fiscal reset that involves the cutting of corporate taxes can be expected to have a significant influence upon the forthcoming Brexit negotiations, and this prospect has prompted the Swedish Prime Minister to comment to Bloomberg that potential UK plans to lower corporate taxes considerably will "of course make discussions more difficult."[24]

Chas Roy-Chowdhury, Head of Taxation at ACCA, is cited as commenting that *"Any tax policy will be closely aligned with what the EU does because that will create much greater certainty for businesses. So while the Brexiteers may be talking about all this autonomy, I think the reality is there will be very close alignment with the EU."* [25]

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NOTES

1 Business tax road map, HM Treasury (March 2016), 1.15.

2 *Ibid.* 1.17.

3 Pascal Saint-Amans, OECD, statement to the Australian Parliament's Economics References Committee, April 2015.

4 John Cridland, CBI (December 10, 2014).

5 Clause 71(1)(a) of the current Finance Bill.

6 *"U.K. Firms, Follow OECD's Advice on Transfer Pricing,"* Bloomberg BNA 24 Transfer Pricing Report 1263 (February 2016).

7 *Business tax road map*, HM Treasury (March 2016), 2.29.

8 *Ibid.* 2.29.

9 *"U.K. Backs Away From EU Plans for Country-Specific Reporting,"* Bloomberg BNA Transfer Pricing Report (June 28, 2016).

10 The Republic of Ireland has adopted a very similar approach, through the introduction of an "Equivalent CbC Report" for secondary reporting purposes, in its Country-by-Country Regulations.

11 Regulation 5 of The Taxes *(Base Erosion and Profit Shifting) (Country-by-Country Reporting) Regulations 2016*.

12 Directive 2011/16/EU, Section II.1 of Annex III, *Filing rules for Groups of multinational enterprises*.

13 HMRC's update can be found at https://www.gov.uk/government/news/update-on-country-by-country-regulations; For the OECD guidance, see Guidance on the Implementation of Country-by-Country Reporting: BEPS Action 13, OECD (June 29, 2016)

14 Policy paper *Country by Country reporting – updated*, HMRC (February 26, 2016).

15 *Explanatory Memorandum to the Taxes (Base Erosion and Profit Shifting)(Country-by-Country Reporting) Regulations 2015*, HMRC (2015), paragraph 4.4.

16 *Explanatory Memorandum to the Taxes (Base Erosion and Profit Shifting)(Country-by-Country Reporting) Regulations 2015*, HMRC (2015), paragraph 7.5.

17 *OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations* (2016), Annex I to Chapter V.

18 *Diverted Profits Tax:* Guidance, HMRC (November 30, 2015), DPT2050.

19 For proposed guidance on the application of value chain analyses in the context of profit splits, see the *Discussion Draft on the Revised Guidance on Profit Splits*, OECD (July 4, 2016), paragraphs 24 to 27.

20 *Business tax road map*, HM Treasury (March 2016), 2.29.

21 *"George Osborne puts corporation tax cut at heart of Brexit recovery plan,"* Financial Times (July 3, 2016)

22 *"Tax haven route won't work for post-Brexit UK, OECD says,"* Reuters (July 3, 2016)

23 "U.K. Chancellor Ready to 'Reset' Fiscal Policy on Brexit," Bloomberg (July 22, 2016)

24 "Sweden Warns Against Aggressive Tax Cuts Amid Brexit Talks," Bloomberg (August 21, 2016)

25 *Ibid.*