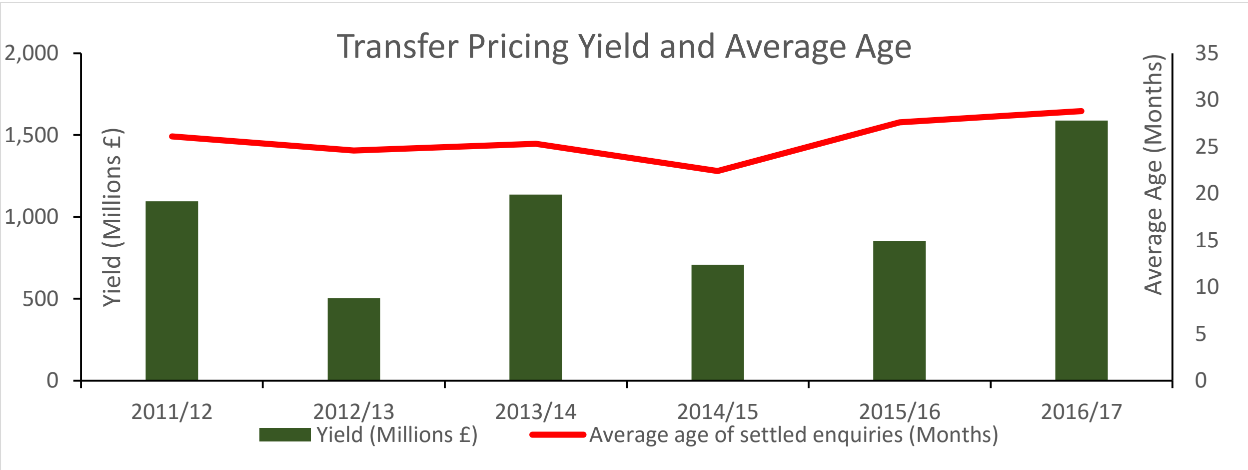
Transfer Pricing and Diverted Profits Tax statistics, to 2016/17

The Transfer Pricing rules and the Diverted Profits Tax are important elements in a range of measures to make sure multinationals pay the right amount of tax on the share of their profits that belong to the UK.

Transfer Pricing

The UK's Transfer Pricing rules set out how transactions between connected parties are priced for tax purposes. This includes transactions between companies in the same group. The rules ensure that the UK can tax its share of profits in accordance with the internationally recognised transfer pricing principle (known as the arm's length principle).

HM Revenue and Customs (HMRC) challenges arrangements that do not allocate the right amount of profits (the arm's length amount) to the UK. In the years from 2011/12 to 2016/17, HMRC secured **£5.914 billion of additional tax**[1] by challenging the transfer pricing arrangements of multinationals.



Year	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
Total Amount	£1,095m	£504m	£1,137m	£707m	£853m	£1,618m

[1] Some of this additional tax was secured as a result of HMRC's investigations into arrangements within the scope of the Diverted Profits Tax legislation, where businesses have adjusted the transfer pricing on those arrangements during the investigation.

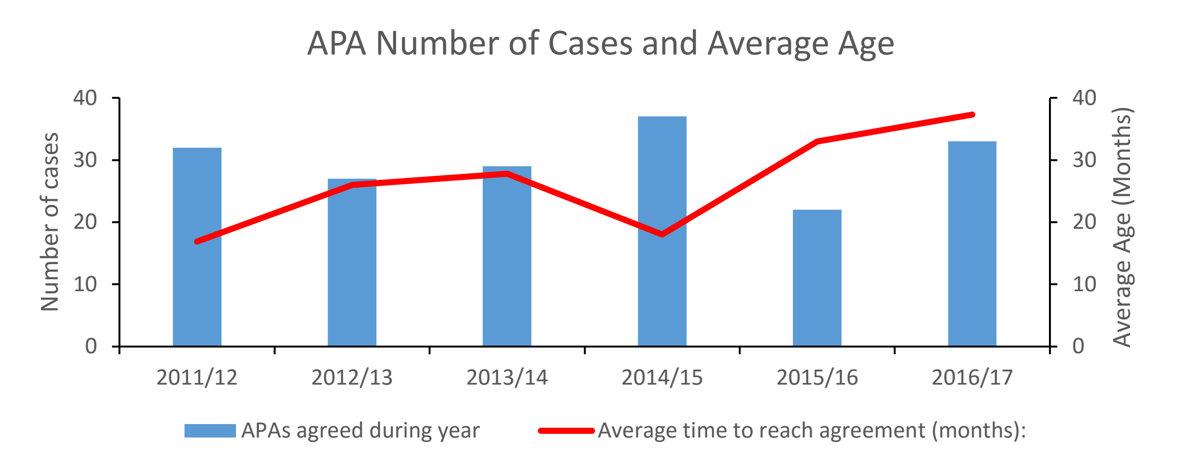
12 months to 31/3	2012	2013	2014	2015	2016	2017
Average age open enquiries (months)	20.8	18.6	18.5	21.5	24.1	27.3
Average age settled enquiries (months)	26.1	24.6	25.3	22.4	27.6	28.8
50% open less than (months)	15.4	15.4	15.3	15.9	17.3	21.4
50% settled within (months)	17.7	20.6	21.0	21.2	24.8	29.4

Since 2008, HMRC has increased the number of staff dealing with international tax risks, including transfer pricing. As at 31 March 2017, there were **82** full time equivalent staff in our specialist transfer pricing group. Our transfer pricing experts work with other expert industry and tax specialists (including around 40 diverted profits tax specialists) to tackle all international risks. We work with other tax authorities, sharing information and expertise, to identify risk and challenge arrangements. **Country by Country reports** will increase the information available to support HMRC's risk assessment processes.

An **Advanced Pricing Agreement (APA)** is a written agreement between a business and HMRC which determines the appropriate transfer pricing method to be applied to certain transactions for a set period and in advance of a tax return being made. APAs are recognised as international best practice by the OECD in managing compliance with transfer pricing rules. They help tax authorities, including HMRC, to establish early on how transfer pricing rules apply to complex cross-border transactions. They provide multinational businesses with greater certainty about their tax liabilities so that they pay the right amount of tax at the right time.

An APA does not provide any special treatment or change the amount of tax due under the law. Where tax administrations in two (or more) countries have an interest in the tax treatment of a particular business transaction between connected companies, an APA clarifies how those tax administrations will view the transaction for tax purposes. In the process of reaching an APA, tax administrations jointly consider the transaction at an early stage, and resolve the correct tax treatment in their respective countries. An APA therefore helps establish the correct tax treatment at an early stage and eliminates the risk that a business will have to pay tax more than once on the same profits.

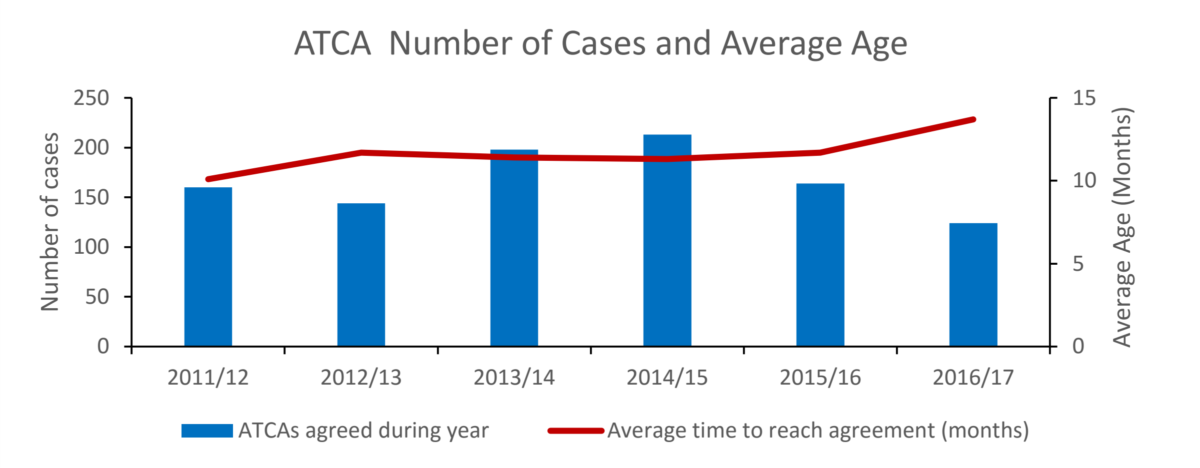
A revised Statement of Practice, published in November 2016, explains how HMRC applies the APA legislation and operates the UK APA programme.



	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
Applications made during year	32	45	43	66	47	32
Applications turned down	0	0	0	2	3	5
APAs agreed during year	32	27	29	37	22	19
Average time to reach agreement (months):	16.9	26	27.8	18.00	33.0	32.8
50% agreed within (months):	10.7	15	19.7	15.6	32.3	34.7

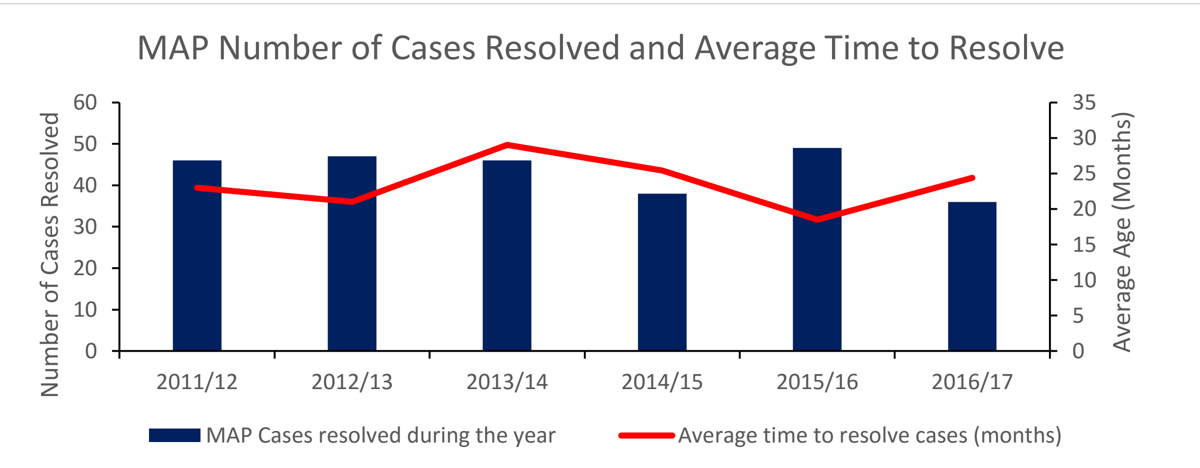
An **Advance Thin Capitalisation Agreement** (ATCA) is an agreement between a business and HMRC which sets out how the transfer pricing rules apply to funding issues, including the appropriate levels, terms and conditions of debt financing between connected parties, so that the UK receives the right amount of tax at the right time. An ATCA is a form of APA and, like all APAs, it enables tax authorities to examine certain transactions and agree the appropriate transfer pricing position earlier than the usual tax return/assessment cycle would allow; it does not change the amount of tax a business must pay.

Statement of Practice 1/2012 explains HMRC's approach. Detailed practical guidance is contained in the international manual



	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
ATCAs agreed during year	160	144	198	213	164	124
Agreements in force during year	279	414	510	577	568	479
Average time to reach agreement: (months)	10.1	11.7	11.4	11.3	11.7	14.9
50% agreed within (months):	7.7	9.7	10.4	10.5	9.7	13.7

Most double taxation agreements include a **mutual agreement procedure** (MAP) article allowing tax administrations to resolve cases of double taxation by consultation and mutual agreement. Statement of Practice 1/2011 outlines HMRC's procedure in relation to the elimination of double taxation under MAP and/or the EU Arbitration Convention. The majority of cases require HMRC to work with tax administrations in other countries to determine each country's taxing rights, which affects the time needed to resolve these cases.



	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
Cases resolved during the year	46	47	46	38	49	36

Cases admitted during the year	45	40	61	71	71	80[2]
Average time to resolve cases (months)	23	21	29	25.4	18.5	24.4

Diverted Profits Tax

The Diverted Profits Tax (DPT) is designed to encourage large companies that try to minimise their tax liabilities through the use of contrived arrangements to change their behaviour, or face paying tax at a higher rate. It is not targeted specifically at any particular sectors or companies, but rather at particular behaviours and arrangements.

Diverted Profits Tax Yield

Year	2015/16	2016/17
Total Amount	£31m	£281m

The figures of DPT yield reflect amounts received as a result of Diverted Profits Tax charging notices issued by HMRC, and additional amounts of Corporation Tax resulting from behavioural change. The amount raised from the first issue of DPT charging notices during 2016/17 was £138 million.

The behavioural change component of DPT yield is comprised of two elements. The first is additional Corporation Tax paid as a result of HMRC intervention to ensure that profits earned in the UK are taxed in the UK.

The second element is the behavioural change where, as intended, businesses have changed their structures or transfer pricing arrangements without an HMRC intervention occurring. This means they pay additional Corporation Tax rather than DPT at the higher rate.

The anticipated Exchequer impact of Diverted Profits Tax at the March Budget 2015 was £25 million in 2015/16 and £275 million in 2016/17, comprising Diverted Profits Tax receipts and additional Corporation Tax arising from behavioural change.

[2] This represents the number of MAP cases HMRC has recorded as beginning during the 2016/17 year. Bilateral work is ongoing to align HMRC's statistics with the UK's double taxation treaty partners in accordance with the OECD's MAP Statistics Reporting Framework.

Diverted Profits Tax Procedures

Notifications

Companies have to notify HMRC if they have arrangements that potentially fall within the scope of the DPT legislation, subject to limited statutory exceptions. More than one company within a multinational group may need to notify.

	2015/16	2016/17
DPT notifications received	48	145

The numbers above are the DPT notifications and analyses HMRC has received from groups where one or more companies within the group have indicated that they are involved in arrangements that may be in scope of the DPT legislation. The obligation to notify does not necessarily mean that a DPT charge will arise.

Notices

Where HMRC believes that diverted profits tax may be due, we first issue a preliminary notice. Depending on the company's response, HMRC may then issue a charging notice setting out the amount of diverted profits tax to be paid by the company within 30 days.

During 2015/16 HMRC did not issue any DPT preliminary or charging notices. Following the introduction of DPT, companies had 6 months to notify HMRC that they were potentially within scope of the legislation. HMRC then has 2 years to investigate to determine whether it is reasonable to issue a DPT preliminary notice. It was expected that HMRC might not issue DPT notices during 2015/16.

In 2016/17 HMRC issued 16 DPT preliminary notices and 14 DPT charging notices.

Differences between the numbers of DPT preliminary and charging notices can be due to timing differences, for example where a preliminary notice is issued at year end, or as a result of successful representations made to HMRC on the specified issues.

The DPT legislation provides a 12 month review period after the notice is issued during which HMRC will continue to work with businesses, to resolve the dispute. If, during the review period, HMRC is satisfied that the amount of DPT charged is excessive or insufficient, it can issue amending notices to reduce, or a supplementary notice to increase, the DPT charged. Businesses have the right of appeal against a DPT charge after the conclusion of the 12 month review period.

The DPT procedures are subject to a strict governance process, and all decisions to issue DPT notices are considered and agreed by a senior governance board.