



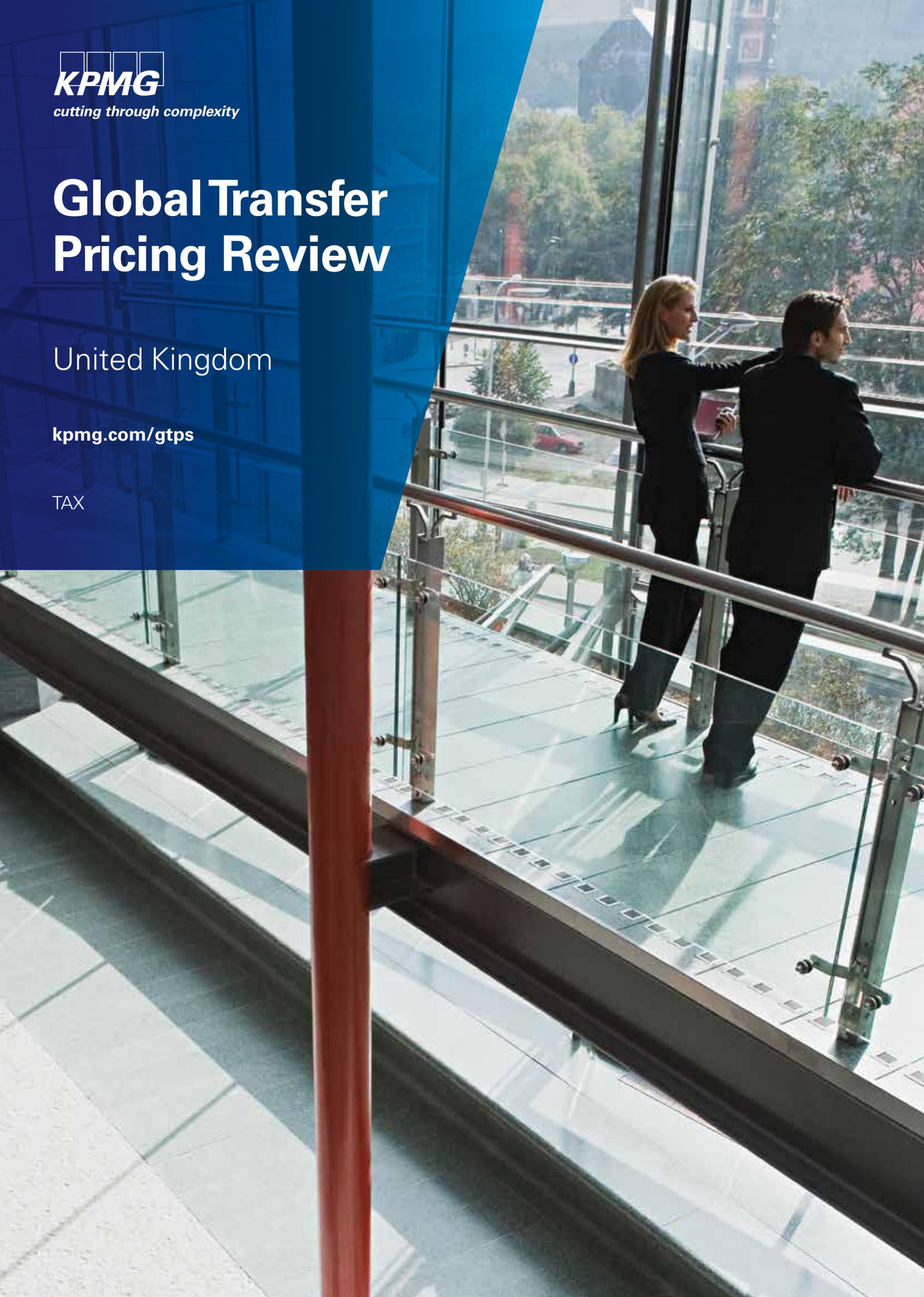
*cutting through complexity*

# Global Transfer Pricing Review

United Kingdom

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TAX



# United Kingdom



## KPMG observation

Her Majesty's Revenue and Customs (HMRC) supports the Organisation for Economic Co-operation and Development's (OECD) Base Erosion and Profit Shifting (BEPS) initiative and the UK is expected to be an early adopter of the recommendations arising from the BEPS Action Plan. The UK transfer pricing legislation already incorporates the 2010 OECD Transfer Pricing Guidelines and KPMG in the UK is starting to see the principles contained in the new draft of Intangibles Chapter VI being raised during HMRC inquiries.

Following BEPS, KPMG in the UK expects to see an increase in Advance Pricing Agreement (APA) applications and Mutual Agreement Procedures (MAP) claims. HMRC recognizes the importance of these tools in making the UK a good place to do business and helping taxpayers manage their double taxation risk. Its willingness to assist taxpayers and enter into negotiations with other tax authorities will continue after BEPS.

## Transfer pricing study snapshot

### The purpose of a transfer pricing study

	Applicable	Thresholds apply/exist
Legal requirements	●	●
Protection from penalties	●	
Reduce risk of adjustment	●	
Shifts burden of proof	●	

## Basic information

### Tax authority name

HMRC (Her Majesty's Revenue and Customs).

### Citation for transfer pricing rules

For years ending before 1 April 2010, Schedule 28AA ICTA 1988. For years ending on or after 1 April 2010, the relevant legislation has been rewritten as Part 4 of the Taxation (International and Other Provisions) Act 2010. The changes were merely an attempt to present the legislation in a more logical and accessible format.

### Effective date of transfer pricing rules

1 July 1999.

### What is the relationship threshold for transfer pricing rules to apply between parties?

Ownership between 40 percent and 50 percent; based on voting power, share capital, or management control. With respect to financing transactions, where the lender has acted together with shareholders to provide funding, the shareholders' stake can be attributed to the lender, meaning a financing transaction may be caught by the legislation where there is no, or a very

small, direct relationship between the lender and borrower.

### What is the statute of limitations on assessment of transfer pricing adjustments?

Four years from tax year-end (except in cases involving fraud or carelessness).

## Transfer pricing disclosure overview

Are disclosures related to transfer pricing required to be submitted to the revenue authority on an annual basis (e.g. with the tax return)?

No.

What types of transfer pricing information must be disclosed?

Not applicable.

What are the consequences of failure to submit disclosures?

Not applicable.

## Transfer pricing study overview

Can documentation be filed in a language other than the local language? If yes, which ones?

Nothing specified in Legislation. Time will be allowed for translation.

When a transfer pricing study is prepared, should its content follow Chapter V of the Organisation for Economic Co-operation and Development (OECD) Guidelines?

Yes, for all transactions.

Does the tax authority require an advisor/tax practitioner to have specific designation in order to prepare or submit a transfer pricing study?

No.

## Transfer pricing methods

Does your country follow the transfer pricing methods outlined in Chapter II of the OECD Guidelines? If exceptions apply, please describe.

Yes.

## Transfer pricing audit and penalties

When the tax authority requests a taxpayer's transfer pricing documentation, are there timing requirements for a taxpayer to submit its documentation? And if so, how many days?

Yes, 45 days.

When the tax authority requests a taxpayer's transfer pricing documentation, are there timing requirements for a taxpayer to submit its documentation? Please explain.

There are no specific deadlines. HMRC will decide on a case-by-case basis but will typically allow 45–90 days.

If an adjustment is proposed by the tax authority, what dispute resolution options are available?

The taxpayer has the right to appeal against a transfer pricing adjustment. Such an appeal will be heard by the Tribunals Service. There is now an additional option of trying to resolve the dispute using mediation to avoid the appeal going to tribunal.

If an adjustment is sustained, can penalties be assessed? If so, what rates are applied and under what conditions?

Under the general penalty regime for incorrect returns, a transfer pricing adjustment may lead to a penalty based on a percentage of actual tax loss. Penalties are up to 30 percent for a failure to take reasonable care; up to 70 percent for a deliberate understatement or over claim; and up to 100 percent for a deliberate understatement aggravated by concealment.

HMRC may apply a lower percentage penalty where there is disclosure, the extent of mitigation depending on whether disclosure is prompted or unprompted. A 10 percent penalty is applied to overstated losses.

To what extent are transfer pricing penalties enforced?

KPMG in the UK is seeing HMRC enforce penalties more strictly in recent years.

What defenses are available with respect to penalties?

In its guidance, HMRC indicates that the existence of appropriate transfer pricing documentation may help to mitigate any tax-gear penalty due as a result of a transfer pricing adjustment. Penalties may also be mitigated through cooperation with HMRC.

What trends are being observed currently?

There has been an increased focus on transfer pricing in the media, which has led to large multinationals being questioned on their transfer pricing practices by the government's Public Accounts Committee. This scrutiny has led to increased funding for HMRC transfer pricing specialists.

HMRC is fully involved in the BEPS project. Principles being debated in the BEPS Actions are regularly raised on audit.

HMRC is willing to work with taxpayers on transfer pricing issues in real-time and provide general opinion on the transfer pricing methodology, but not the price. The only way a taxpayer can get legal certainty about the transfer pricing treatment of transactions is under the formal APA process.

## Special considerations

Are secret comparables used by tax authorities?

No. Secret comparables may be used by HMRC to select companies for audit, but they are not used for setting an arm's length rate.

Is there a preference, or requirement, by the tax authorities for local comparables in a benchmarking set?

Yes. HMRC would prefer to see UK comparables for UK based activity. In practice European comparables are accepted when limited UK companies are available.

Do tax authorities have requirements or preferences regarding databases for comparables?

No. Typically when European activities are being benchmarked Fame would be used for UK searches and Amadeus for European searches. HMRC has access to the databases.

Does the tax authority generally focus on the interquartile range in a TNMM analysis?

No.

Does the tax authority have other preferences in benchmarking? If so, please describe.

HMRC expects sound economic principles to be used in applying database screens. Poor screens could lead to penalties for carelessness if this results in a tax adjustment.

### What level of interaction do tax authorities have with customs authorities?

HMRC was formed in 2005 by the merger of the Inland Revenue and HM Customs and Excise. KPMG in the UK has observed that customs officials sometimes request transfer pricing documentation as part of their review.

### Are there limitations on deductibility of management fees beyond the arm's length principle?

Yes, some. General tax principles require expenses to be incurred wholly and exclusively for the purpose of the trade.

### Are management fees subject to withholding?

No.

### Are there limitations on the deductibility of royalties beyond the arm's length principle?

No.

### Are royalties subject to withholding?

Yes.

### Are taxpayers allowed to file tax return numbers that differ from book numbers?

Yes. Both upward and downward transfer pricing adjustments may be made in the financial statements. If transfer pricing adjustments are invoiced and made in the financial statements, indirect tax implications must also be considered.

Only upward transfer pricing adjustments may be made in the tax computation. Tax computation transfer pricing adjustments may lead to increased analysis of transfer pricing arrangements and increase the likelihood of double

taxation. A transfer pricing adjustment in the tax computation in itself is not an event which creates a customs duty or VAT requirement. However, this might be seen by HMRC as an indication that the original transaction was not in accordance with VAT and customs duty valuation principles and may result in an indirect tax enquiry and adjustments.

### Other unique attributes?

None.

## Tax treaty/double tax resolution

### What is the extent of the double tax treaty network?

Extensive.

### If extensive, is the competent authority effective in obtaining double tax relief?

Almost always.

### When may a taxpayer submit an adjustment to competent authority?

Typically, after an adjustment is proposed to the taxpayer. However, an application can be made and HMRC is prepared to enter into discussions with the treaty partner before an adjustment is finalized.

### May a taxpayer go to competent authority before paying tax?

Yes.

## Advance pricing agreements

### What APA options are available, if any?

Unilateral, bilateral, multilateral.

### Is there a filing fee for APAs?

No.

### Does the tax authority publish APA data either in the form of an annual report or through the disclosure of data in public forums?

Yes.

### Are there any difficulties or limitations on the availability or effectiveness of APAs?

No. The APA program is well-established and very successful in the UK. HMRC has extended the number of countries with which it has concluded APAs, including countries starting up their APA programs.

A taxpayer must demonstrate doubt or difficulty in the application of the UK transfer pricing legislation in order to apply for an APA. Consequently, APAs are not commonly obtained for routine transfer pricing situations.

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