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Weekly Tax Matters

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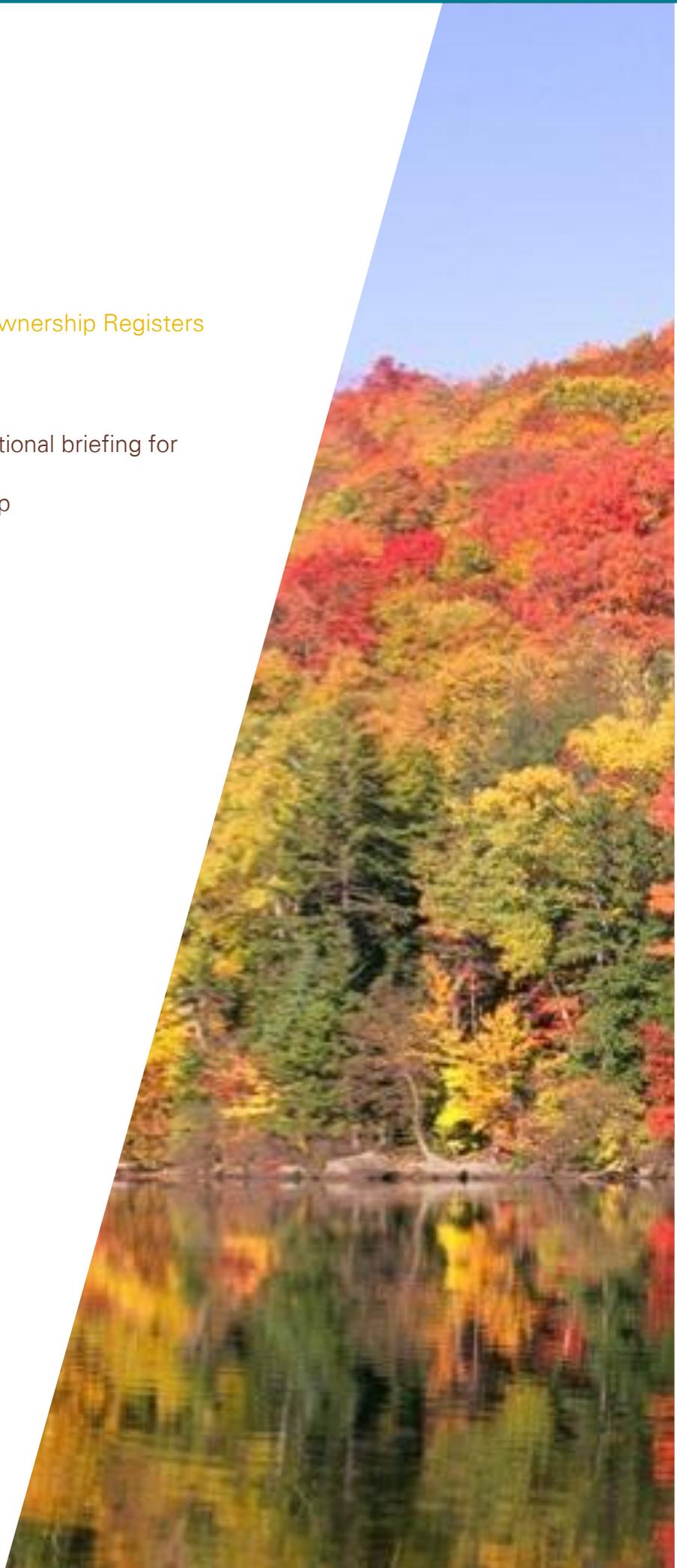


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Draft Finance Bill 2016

The draft Finance Bill clauses will be published on Wednesday 9 December.

With (in tax terms) a reasonably quiet Autumn Statement out of the way, the last big tax event of the year will be the publication of the draft Finance Bill 2016 clauses on Wednesday 9 December 2015. The clauses will contain more information on some of the tax announcements at both the Summer Budget and last week's Autumn Statement. We expect this to include legislation on changes to the domicile rules, the Apprenticeships Levy, hybrid mismatch arrangements and large business compliance. We may also see the Government publish its response to earlier consultations, for example on changes to the domicile rules and on the restriction of travel and subsistence relief for those engaged through intermediaries (both of which should come alongside draft legislation) and potentially changes to the IR35 regime (where consultation is at an earlier stage).

The draft clauses will make up the majority of next year's Finance Bill, to be published after the Budget, which we now know will take place on Wednesday 16 March 2016.

KPMG in the UK will be preparing a detailed commentary on the key measures in the draft Finance Bill clauses – look out for your copy next Friday. Our commentary will also be available from our dedicated Autumn Statement page, where you can already find all our comment and analysis of the Autumn Statement itself.

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CORPORATE TAX



Updated Diverted Profits Tax (DPT) guidance issued by HMRC

On 30 November HMRC issued updated DPT guidance to clarify their interpretation of the legislation and proposed administrative practice.

On 30 November, HMRC issued [updated Diverted Profits Tax \(DPT\) guidance](#), to replace all previously published guidance.

Overall, the guidance has been subject to a comprehensive review and rewrite to improve its clarity and practical application, and the increase in the number of pages (from 88 pages to 108 pages) does not fully reflect the scale of the changes.

Some highlights from the revised guidance include:

- Both the Insufficient Economic Substance Condition (IESC) and the 'design test' in section 86 FA 2015 (avoidance of UK taxable presence) require an element of contrivance. In relation to the design test in section 86, the arrangements have to differ in some material way from those that would have been expected to be made had there been no consideration around the permanent establishment (PE) threshold.
- In relation to sections 80 and 81 FA 2015 (involvement of entities or transactions lacking economic substance), even where there is an Effective Tax Mismatch Outcome (ETMO) and the IESC is met, there will be taxable diverted profits only where either the transfer pricing is in dispute or it is reasonable to assume, very broadly, that the material provision would not have been made in the absence of the ETMO.
- Although there is no clearance procedure for DPT, HMRC may be able to provide a view on whether transactions are likely to be subject to DPT. However, HMRC will do so only where there are particular reasons for expending the resources.
- HMRC will carry out risk reviews of businesses it considers may fall within the scope of DPT. Such risk reviews will consider challenges to structures that divert profits from the UK also for periods before DPT came into force, for example challenges on the basis that there was an undeclared PE or that the transfer pricing was incorrect.

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Currency used to prepare the tax computation

The recently enacted Finance Act makes changes to the definition of functional currency and designated currency elections.

In the final of our series of articles looking at the changes being made as a result of the consultation on the taxation of loan relationships and derivative contracts, we look at changes relating to the currency used to prepare a company's tax computation.

The basic rule is to use sterling, to determine the currency in which its income is to be calculated for corporation tax purposes. However, where the company's functional currency, or designated currency, is a currency other than sterling that non-sterling currency is, broadly, used instead.

Finance (No. 2) Act 2015 makes changes to the definition of functional currency and the way that a designated currency election will apply. This gives rise to new opportunities to hedge a company's foreign exchange position as well as introducing new risks that an unhedged foreign exchange exposure may arise. In particular, care will need to be taken where an investment company with a foreign branch or an interest in a foreign partnership has made a designated currency election. In certain cases consideration may need to be given to causing an existing election to cease to have effect.

All the changes have effect from 1 January 2016 regardless of a company's period of account.

KPMG in the UK's Treasury Tax team have prepared a more detailed note on these changes which can be found [here](#).

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Patent Box: Action may be required before 31 December 2015

HMRC have suggested UK to UK intra-group transfers of IP after 31 December 2015 may not benefit from the grandfathering rules.

As regular readers will be aware, new Patent Box rules are being introduced from July 2016 and draft legislation will be published on 9 December when draft clauses for Finance Bill 2016 are released. This legislation will include safeguarding rules which will prevent companies from benefiting from grandfathering of the existing rules to 2021 if intellectual property (IP) is transferred into the Patent Box after 31 December 2015. It had previously been expected that these safeguarding rules would only apply to intra-group, cross border transfers of IP from countries which do not have an IP regime. However, we now understand from HMRC that UK to UK intra-group transfers could potentially be caught unless the IP is currently benefitting from an IP regime (such as the UK Patent Box).

The position will not be certain until the legislation is finalised (which is likely to be March 2016). Therefore, groups that are currently considering transferring IP intra-group ahead of 30 June 2016, and hoping to benefit from the grandfathering rules may wish to review their position now. Any IP that is currently not benefitting from the Patent Box (or an overseas regime) may need to be elected into the regime or transferred ahead of 31 December 2015.

Please speak to your usual Tax & Pensions contact for further advice.

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HMRC's view on company residence in the UK/Jersey and other treaties

HMRC have announced a change of view on the interpretation of the residence articles in 16 Double Taxation Agreements.

On 30 November [HMRC announced](#) that they had reached an agreement with Jersey about the interpretation of the company residence provisions in the 1952 Jersey-UK Double Taxation Agreement (DTA). This agreement reflects a change in view, with their interpretation now being that the treaty includes a tie-breaker clause to decide where a company is to be treated as resident for the purposes of the DTA. HMRC's previous view was that a dual-resident company was not a resident of either jurisdiction under the terms of the provisions and so was outside the scope of the DTA.

This could impact companies incorporated in the UK but managed and controlled in Jersey. Such companies will now be treated as residents of Jersey under the DTA. As a result they will also be treated as non-UK resident under UK domestic law (by virtue of section 18 CTA 2009). *Prima facie*, results could include the preclusion of UK group relief surrenders by the company (where the 'dual resident investing company' rules were not previously considered to apply) or even a taxable migration of the company out of the UK (presumably at any time management and control was transferred to Jersey).

HMRC have also reviewed other DTAs with identical or similarly-worded provisions (these tend to be older treaties) and have concluded that these also include a tie-breaker clause to decide where a company is to be treated as resident. This change in interpretation affects 16 DTAs in total including Guernsey, the Isle of Man and Greece.

Please speak to your usual Tax & Pensions contact if you have concerns about the implications of this change in view.

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European Parliament developments on Corporate Taxation

Two recent reports have recommended a number of measures aimed at making corporate tax systems in the EU fairer and more transparent.

On 25 November the EU Parliament voted and passed a resolution approving a report issued by the Special Committee on Tax Rulings and Other Measures Similar in Nature or Effect (TAXE Committee). The TAXE Committee is a temporary group set up by the European Parliament to investigate Member States' tax ruling practices and examine ways to end unfair tax competition and combat tax evasion within the EU. Then on 1 December, a legislative report drafted by the Parliament's permanent Economic and Monetary Affairs Committee (ECON) was approved by that Committee. A plenary vote on this report is expected to take place on 16 December.

There was some overlap in the recommendations made in the two reports including support for the introduction of country by country reporting and the introduction of a Common Consolidated Corporate Tax Base (CCCTB), with the ECON report suggesting a two stage approach with a common tax base being introduced first which should become consolidated later on. Some other recommendations in the reports were the development of common definitions for terms such as 'economic substance' and 'permanent establishment' and the introduction of a 'Fair Tax Payer' label and a common European Tax Identification Number. The European Commission will now be under pressure to act on these recommendations.

Further information has been prepared by KPMG's EU Tax Centre on the TAXE Committee's report [here](#) and the ECON report [here](#).

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First-tier Tribunal decision on unallowable purpose

The FTT has rejected the taxpayer's appeal against the application by HMRC of the unallowable purpose rule to deny loan relationship debits.

[The First-tier Tribunal \(FTT\) has rejected](#) the taxpayer's appeal against the application by HM Revenue & Customs (HMRC) of the unallowable purpose rule to deny loan relationship (LR) debits arising to two group companies as a result of tax planning arrangements.

As part of a commercial reorganisation, the taxpayer group had claimed a deduction under section 91B Finance Act 1996 in respect of the reduction in fair value of a shareholding in a group company deemed to represent a loan relationship. The deeming arose because the shares, in combination with a total return swap, were designed to produce an interest-like return. The reduction in fair value resulted from a non-arm's length transaction with another group company (the novation of intra-group loan liabilities without payment of consideration).

Interest debits in respect of the transferred loans were also disallowed.

The case is interesting for a number of reasons:

- It involved a taxpayer group seeking to turn an anti-avoidance rule to its advantage but being denied this result on appeal to the FTT.
- It also involved the taxpayer group suffering a further disallowance of related tax deductions, leaving the group worse off in tax terms than if it had not engaged in the planning at all.
- [Before the FTT](#), HMRC pursued [only](#) the 'unallowable purpose' argument, having, it is assumed, decided not to pursue other potential challenges.
- In reaching its decision to disallow these deductions, the FTT made a number of observations on how the unallowable purpose rule should operate, in particular (i) how the rule should be applied to 'deemed' loan relationships and (ii) how one should determine the debits to be disallowed applying the 'just and reasonable' attribution test, which may be of wider application (if followed by other courts).
- The judgment also contains (i) observations by the FTT accepting that a taxpayer's 'purpose' in holding particular assets can change over time and (ii) confirmation that HMRC's position is that the burden of proof is on the taxpayer to provide evidence sufficient to rebut an unallowable purpose challenge.
- The FTT favoured an analysis not put forward by counsel for either party in the case.

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Changes to the CT instalment payments regime

Very large companies will now have to pay their CT instalment payments earlier.

Currently, large companies (companies with taxable profits of more than £1.5 million in an accounting period), must pay their corporation tax in quarterly instalments. It was announced in the Summer Budget 2015 that changes would be made to the regime so that 'very large' companies (those with taxable profits of more than £20 million in an accounting period) would have to pay their instalment payments earlier.

HMRC have now [published](#) a guidance note on the proposed changes, along with draft legislation and an explanatory memorandum and a [Tax Information and Impact Note](#). The draft legislation and explanatory memorandum are open for consultation until 26 February 2016.

Under the proposed changes, very large companies would have to pay their instalment payments four months earlier than large companies, with a very large company needing to make their first instalment payment two months and 14 days after the beginning of a standard 12 month accounting period. Interestingly, the guidance does not appear to deal with the practical issue of how companies should estimate what their annual taxable profit should be before the end of their first quarter. We would assume that HMRC expect taxpayers to make a 'best

estimate' and update it as the year progresses, with no negative repercussions as long as a bona fide attempt at forecasting the taxable profit is made , and we would encourage HMRC to clarify this in the final guidance.

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R&D Advance Assurance for small companies

HMRC have issued further information on the Advance Assurance scheme for small companies claiming R&D relief.

As [previously announced](#), as part of the Government's plan to boost access to research and development (R&D) tax relief for smaller companies, the Advance Assurance scheme has been introduced from November 2015. The scheme allows certain companies to claim for R&D tax relief with the assurance that HMRC will not open any enquiries into their claims for the first three accounting periods.

Advance Assurance is open to companies who haven't claimed R&D before, and with annual turnover of less than £2million and less than 50 employees. Changes to a successful application for Advance Assurance won't be allowed, but certain changes to the R&D activities covered will be.

HMRC have now published [further guidance](#) on the operation of the scheme and how to apply, along with the [form needed](#) to apply for Advance Assurance.

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CJEU confirms dates in important cases

The CJEU has updated its diary, confirming dates in some important cases including the UK referrals on card handling services.

The Court of Justice of the European Union (CJEU) has updated its diary, confirming dates in some important cases. These include:

- *Bookit (C-607/14) & National Exhibition Centre (C-130/15)* – Hearing Wednesday 16 December - Whilst these cases have not been joined, they are being heard in the same chamber at the same time. These cases concern card handling services and whether they fall within Article 13B(d)(3) of the Sixth Directive, now Article 135(1)(d) VAT Directive, which exempts ‘transactions, including negotiation, concerning deposit and current accounts, payments, transfers, debts, cheques and other negotiable instruments, but excluding debt collection.’

Given the questions were only published in February and May this year, the hearing has come relatively quickly. For information:

- on *Bookit*, to access the First-tier Tribunal (FTT) decision click [here](#), to access the reference click [here](#).
- on *NEC* to access the Upper Tribunal (UT) decision click [here](#), to access the reference click [here](#).
- *Air France – KLM (C-250/14) & Hop!-Brit Air (C-289/14)* – Judgment date confirmed for 23 December - These officially joined cases concern airline ‘no-shows’. The taxpayers are arguing that amounts retained for no shows are not subject to VAT. Whilst all our flights are zero rated, in some Member States, certain non-international flights are subject to VAT. For information:
 - on *Air France - KLM (C-250/14)* to access the reference click [here](#).
 - on *Hop!-Brit Air (C-289/14)* to access the reference [here](#).

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Mercedes-Benz Financial Services – Court of Appeal Judgment

The Court of Appeal has issued its Judgment on the VAT treatment of the taxpayer’s ‘Agility’ arrangement, and has proposed a reference to the CJEU.

This case concerns the treatment of a specific motor vehicle finance agreement called ‘Agility’ offered by Mercedes-Benz Financial Services (MBFS). The Agility product is recommended to customers who are undecided as to whether they want to own the car or want to keep open the option of whether to purchase or not. MBFS considered that Agility is a rental agreement with an option to purchase that is not contractually binding and, therefore, treated its supplies as services for VAT purposes. HMRC disagreed and considered that because there is the possibility that title to the goods would pass, there is a supply of goods. The original FTT found for HMRC. However, the UT focused on Article 14(2) of the VAT Directive. Noting that the customer is not committed to purchase and that the final balloon payment is optional, the UT found for the taxpayer that there was a supply of services.

At the Court of Appeal, HMRC ran a number of grounds of appeal. These included the argument that the economic cause test used by the UT was the wrong tool to use and the UT’s interpretation of ‘in the normal course of events’ was incorrect.

The Court did not give its views on each ground, but reached the view that the UT was wrong not to refer the matter to the CJEU, noting that there is little certainty as to the interpretation of the phrase "in the normal course of events". The Court also made reference to further guidance on the economic purpose of the contract outlined by the AG's opinion in *Mirror Group* (C-409/98).

Whilst inviting the parties to liaise with the court with a view to agreeing the questions, the court added that it envisaged that reference will consider HMRC's argument about timing. This is around the point that Article 14(2)(b) catches every hire contract where the customer is able to acquire title by **no later** than the final instalment payment, which the court stated 'seems to us to have some obvious attraction in terms of legal certainty.' To read the Judgment click [here](#).

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PERSONAL TAX



Update: Beneficial Ownership Registers

UK Government publishes implementation plan for company beneficial ownership registers.

Following the G20 Leader's St Petersburg commitment to lead by example, the UK Government has publicly reinforced its commitment to transparency in relation to beneficial ownership of companies by issuing a detailed statement outlining how it plans to achieve the G20 High Level Principles on Beneficial Ownership Transparency.

The [Government's Beneficial Ownership Implementation Plan](#), a one page summary, confirms the previous announcement that the UK company beneficial ownership register will be publicly accessible from June 2016. There is an existing requirement for UK companies to maintain a beneficial ownership register from April 2016.

It is interesting to note this plan confirms that whilst trusts are not to be subject to public scrutiny (this has in the past been an area of uncertainty), those trusts that generate UK tax consequences will be obliged to supply their beneficial ownership details to a central register which, whilst not a public register, will be available to Financial Institutions performing due diligence and Domestic Competent Authorities, giving access to detailed information in relation to the trustee(s), settlor(s) and beneficiaries. The basis for the participants in the trust register is likely to be tax filings, including filings for automatic exchange of information purposes.

The implementation plan also includes a commitment to consult on extending beneficial ownership transparency to foreign companies investing in high value property or bidding on UK public contracts. It is anticipated that this would take the form, for example, of a register of UK property owned by foreign companies.

It is noted that whilst most Overseas Territories and Crown Dependencies have indicated that they do not wish to have public central registries, the onus is on them to suggest alternative ways of delivering the UK authorities with the information they require.

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INTERNATIONAL STORIES



Tax Journal – international briefing for November

Chris Morgan's latest summary of international developments.

In the [latest](#) of his regular articles for *Tax Journal*¹, Chris Morgan (Head of the EU tax group at KPMG in the UK) rounds up recent international developments. This month's article looks at:

- UK consultations on the patent box and interest expense following the release of the OECD's base erosion and profit shifting (BEPS) deliverables;
- The European Commission (EC) State Aid decisions relating to transfer pricing rulings in the Netherlands and Luxembourg;
- The introduction of an increased corporation tax rate on restitution interest;
- Amendments to the 'fiscal unity' regime in the Netherlands;
- The repeal of the EU Savings Directive;
- Proposed tax measures for 2016 in Luxembourg; and
- The implementation of Italy's patent box regime.

¹ First published in *Tax Journal* on 27 November 2015. Reproduced with permission.

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International round up

This week: Sri Lanka 2016 Budget; AG opinion on Netherlands "crisis levy"; EU infringement proceedings against Spanish overseas assets reporting requirements; new VAT legislation in Belgium; and FATCA update.

Every week, KPMG member firms around the world publish updates on developments in their country. In *Weekly Tax Matters* we'll highlight a selection that may be of interest to our readers. The complete collection of TaxNewsFlash can be found [here](#).

Asia Pacific

Sri Lanka – The **2016 Budget** was [presented](#) on 20 November 2015.

Europe

Netherlands - According to a November 2015 [opinion](#) of the Advocate General (AG), the **"crisis levy"** imposed on employers in 2013 and 2014 violates certain provisions of EU law.

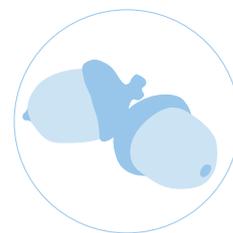
Spain – The EU has [opened](#) infringement proceedings against Spain in relation to requirements for **individual taxpayers to file a form reporting their assets and rights located abroad**.

Belgium – New **VAT legislation** has been [passed](#).

FATCA update

Final regulations implementing the common reporting standard (CRS) have been [published](#) in the Isle of Man. In addition, it has been announced that the existing intergovernmental agreement (IGA) between the Isle of Man and the UK will be superseded by CRS, and that 2016 will be a transitional year.

OTHER NEWS IN BRIEF



A round up of other news this week

This week: FRC review of company tax reporting; NICs rate ceilings bill moves to Third Reading in the House of Lords; SI on standard meal allowances for the new business expenses exemption; and regulations on the tax rules for intra-group transfers of long-term insurance business.

The Financial Reporting Council (FRC) [announced on 1 December](#) that it is intending to conduct a thematic review of companies' tax reporting to encourage more transparent recording of the relationship between the tax charges and accounting profit. The FRC will be writing to a number of FTSE 350 companies prior to their year-end, informing them that a review will be carried out of the tax disclosures in their next published reports.

The National Insurance Contributions (Rate Ceilings) Bill reached committee stage in the House of Lords on 30 November. Unusually, there were no amendments proposed and so the Bill moves directly to Third Reading (no date for which has been announced).

The statutory instrument setting the level of the standard meal allowances for the purposes of the new business expenses exemption (which takes effect from 6 April 2016) has been published and can be found [here](#).

[The Insurance Companies \(Amendment to Section 129 of, and Schedule 17 to, the Finance Act 2012\) Regulations 2015](#) were published on 2 December. These regulations, which have been subject to previous consultation, are intended to address some of the uncertainties identified in the tax rules for certain intra-group transfers of long-term insurance business introduced by Finance Act 2012. They are intended to ensure that tax neutrality is maintained for all assets and liabilities transferred and that any tax attributes transfer with the part of the business that gave rise to them. Further guidance is awaited from HMRC to provide more clarity on other aspects of the insurance business transfer rules.

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