Transfer Pricing

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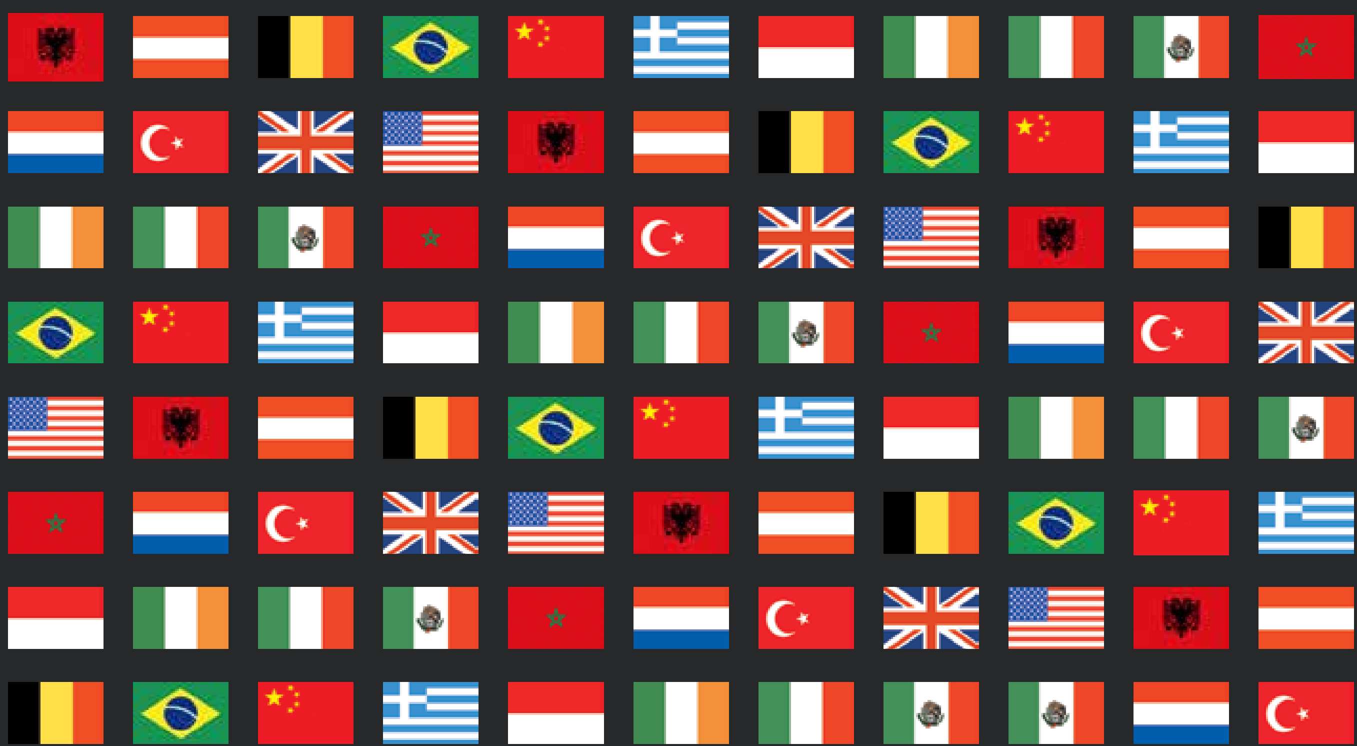

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GETTING THE DEAL THROUGH

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Transfer Pricing 2018

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Overview

1 Identify the principal transfer-pricing legislation.

The UK's main transfer pricing rules are set out in Part 4 of the Taxation (International and Other Provisions) Act 2010 (TIOPA). These are accompanied by provisions relating to advance pricing agreements (APAs) in Part 5 TIOPA.

Other relevant provisions are the diverted profits tax rules introduced by Part 3 of the Finance Act 2015 and the new interest barrier rules which are expected to replace the worldwide debt cap regime, previously found in Part 7 of TIOPA. The new interest barrier rules are expected to be enacted in autumn 2017 and will be effective (retroactively) from 1 April 2017. They are designed to implement BEPS (base erosion and profit shifting) Action 4 in the UK.

Other legislation to be aware of includes the double-tax relief provisions in Part 2 TIOPA, the provisions relating to permanent establishments in the Corporation Tax Act 2009 and the controlled foreign companies rules in Part 9A TIOPA.

2 Which central government agency has primary responsibility for enforcing the transfer pricing rules?

Transfer pricing rules are enforced by Her Majesty's Revenue & Customs (HMRC).

3 What is the role of the OECD Transfer Pricing Guidelines?

Section 75 of the Finance Act 2016 amends section 164 TIOPA so that it refers to the latest version of the Transfer Pricing Guidelines (Guidelines), automatically incorporating amendments to the rules made throughout the OECD's BEPS programme. This amendment was effective from 1 April 2016 for corporation tax purposes and 1 April 2017 for income tax purposes.

A new version of the OECD's Guidelines were published in 2017 and Section 164 of TIOPA specifically states that the UK legislation is to be construed in light of them. Domestic legislation therefore essentially incorporates the Guidelines, and updates are generally enacted through secondary legislation.

4 To what types of transactions do the transfer pricing rules apply?

The rules apply if the following conditions are met:

- a 'provision' has been entered in to by two persons through a transaction or series of transactions;
- the 'participation condition' is satisfied;
- the provision differs from the arm's-length provision which would have been made between independent enterprises; and
- a potential UK tax advantage arises as a result of that difference.

There is no definition of 'provision' in the legislation and it is therefore interpreted in accordance with the Guidelines. HMRC practice is to interpret it widely, including 'arrangements, understandings and mutual practices whether or not they are, or are intended to be, legally enforceable'. The case of *DSG Retail and others v HMRC* confirms that there may be a provision between two connected parties, even when the transactions were not directly entered into between those two parties.

The 'participation condition' is satisfied if either the same persons directly or indirectly participate in the management, control or capital of the parties, or one of the parties directly or indirectly participates in the management, control or capital of the other. This condition will be met if one person has voting control of the other, but also in a number of other circumstances, for example:

- a person would have voting control if all of the rights of people connected with them together with all future rights of that person and those rights which can be exercised for that person's benefit or at their direction are aggregated;
- a person has at least a 40 per cent share of a joint venture; or
- for financing arrangements, a person has acted together with others to provide financing to another person, and would have voting control of that person if their rights were aggregated together with the rights of those with whom they acted together in arranging the financing.

Determining the arm's-length provision (or lack of provision, as the case may be) is the key to all transfer pricing analysis.

5 Do the relevant transfer pricing authorities adhere to the arm's-length principle?

HMRC adheres to the arm's-length principle as enshrined in article 9 of the OECD Model Treaty in applying the transfer pricing legislation. However, other legislation – eg, the diverted profits tax and the interest barrier mentioned above – may restrict deductibility or impose a tax charge on a basis that is inconsistent with the arm's-length principle.

6 How has the OECD's project on base erosion and profit shifting (BEPS) affected the applicable transfer pricing rules?

From 1 April 2016 (for corporation tax purposes) and 1 April 2017 (for income tax purposes) UK law incorporated revisions to the Guidelines made as a result of the BEPS project.

The OECD published their final reports in respect of BEPS Actions 8 to 10 in July 2017 and their effect is to translate the BEPS amendments into the Guidelines. Since the TPG are incorporated into UK domestic law, these amendments are considered to be effective in the UK.

In addition the new interest barrier rules, referred to above, are intended to implement the OECD's recommendations on BEPS Action 4.

Pricing methods

7 What transfer pricing methods are acceptable?

HMRC accepts all OECD transfer pricing methods. Although no absolute hierarchy exists within the Guidelines, HMRC considers that in all cases the comparable uncontrolled price (CUP) method is generally preferred and expects sufficient efforts to be made to identify a suitable CUP. If both traditional transaction methods and transactional profit methods can be applied with equal reliability, the Guidelines express a preference for traditional transaction methods which are considered to be more direct.

If a reliable CUP cannot be found, then, in line with the Guidelines, HMRC places emphasis on choosing the most appropriate method for the particular type of transaction, rather than establishing a rigid hierarchy of methods. For tangible property transactions, such as retail and manufacturing, the resale minus method is considered by the OECD to be the most useful. For semi-finished goods (for instance, the transfer of goods from a supplier to a related party) and services transactions, the cost-plus method is most useful. The profit split and transaction net margin methods are considered to be useful for complex trading relationships involving highly integrated operations where it would otherwise be difficult to split the relationship into separate transactions to which the analysis can be applied. Following BEPS, we are noticing an increasing acceptance of and reliance on the profit split methods.

8 Are cost-sharing arrangements permitted? Describe the acceptable cost-sharing pricing methods.

HMRC follows the Guidelines in relation to cost-sharing arrangements or 'cost contribution arrangements' (CCAs). CCAs arise where:

- participants have the expectation of mutual benefit from an activity and agree to share the contributions to that activity in proportion to the benefits they each expect to obtain; and
- each participant has an ownership interest in the property acquired and can exercise that interest without payment of further consideration.

HMRC recognises that although CCAs are uncommon in most sectors, when they do arise they can be genuine and based on good commercial reasons. Nevertheless, HMRC will consider CCAs carefully to ensure that the methods employed do not differ from those which would have been agreed between independent parties and that any required adjustments are made. However, HMRC notes that the Guidelines caution against making minor adjustments and considers that it will only be appropriate to disregard the terms of a CCA in exceptional circumstances.

9 What are the rules for selecting a transfer pricing method?

There is no strict hierarchy of methods; rather, HMRC follows the Guidelines' 'natural hierarchy'. Generally, the CUP method is preferred and in practice HMRC expects sufficient efforts to be made to identify a suitable CUP. If both traditional transaction methods and transactional profit methods can be applied with equal reliability, the preference is for traditional transaction methods.

If a reliable CUP cannot be found, then, in line with the Guidelines, HMRC places emphasis on choosing the most appropriate method for the particular type of transaction.

For more complex transactions, HMRC is open to exploring other methods if it is considered that they provide a stronger case for application of the arm's-length principle.

10 Can a taxpayer make transfer pricing adjustments?

Transfer pricing adjustments in the UK should be self-assessed on the income tax or corporation tax return of the person who obtains the potential tax advantage. For companies, at present such tax returns generally need to be filed a year after the end of the accounting period in which the relevant transaction took place. Income tax returns currently need to be filed at the end of January in the year following the financial year to which they relate. However, HMRC is modernising its systems and introducing a new digital 'tax account' programme and by 2020 the need for most tax returns is expected to fall away.

We would note that transfer pricing adjustments can only be made where there is a potential UK tax advantage, so adjustments which reduce profits or increase losses are not permitted. However, where a potentially disadvantaged person is also subject to UK corporation tax, it can usually make a compensating adjustment to its taxable profits. It can do so by making a claim to HMRC within two years after the potentially advantaged person has filed their tax return showing the adjustment.

Generally, transfer pricing adjustments may not be made through a company's accounts. As noted at question 35, the government consulted on whether to introduce a secondary adjustments rule into the UK transfer pricing legislation back in May 2016, while the consultation closed in August 2016 the formal results have not yet been published. We do not expect this measure to be introduced in the near to medium future.

11 Are special 'safe harbour' methods available for certain types of related-party transactions? What are these methods and what types of transactions do they apply to?

Most small and medium enterprises (SMEs) are exempt from the requirement to apply transfer pricing in the UK. The definition of an SME corresponds with the EU's definition: broadly, a small enterprise has fewer than 50 employees and either turnover or gross assets of less than €10 million, and a medium enterprise has fewer than 250 employees and either turnover of less than €50 million or gross assets of less than €43 million.

SMEs can, however, be subject to transfer pricing in certain circumstances. The exemption does not apply if the SME transacts with an entity in a 'non-qualifying territory' (ie, if that territory's double-tax agreement with the UK does not contain a non-discrimination article). HMRC may also notify a medium-sized enterprise that it must apply transfer pricing for a particular period. Finally, an SME may elect for the exemption not to apply, which it may wish to do in order to claim a corresponding adjustment in a jurisdiction which has a higher tax rate.

Disclosures and documentation

12 Does the tax authority require taxpayers to submit transfer pricing documentation? What are the consequences for failing to submit documentation?

HMRC has not issued any specific requirements relating to transfer pricing documentation. Transfer pricing adjustments should be made on the relevant income or corporation tax returns. However, taxpayers are expected to 'prepare and retain such documentation as is reasonable given the nature, size and complexity (or otherwise) of their business or of the relevant transaction . . . but which adequately demonstrates that their transfer pricing meets the arm's-length standard'. This includes, for instance, primary accounting records, tax adjustment records, records of transactions with associated businesses, and evidence to demonstrate that an arm's-length result was achieved.

If an error is made in a tax return, the taxpayer may be subject to penalties. The level of the penalty is linked to the reasons for the error, on the basis that taxpayers are expected to take reasonable care in maintaining records that allow them to provide a complete and accurate tax return. For lack of reasonable care, the penalty is generally between 0 per cent and 30 per cent of the extra tax due. For deliberate errors the maximum penalty is 70 per cent of potential lost revenue for HMRC, and 100 per cent of potential lost revenue for deliberate and concealed errors. Penalties can in some circumstances be reduced if the taxpayer tells HMRC about the error.

Going forward, businesses will also have to comply with country-by-country (CbC) reporting, which was implemented in the UK by way of regulation on 18 March 2016. The regulations apply if the consolidated group turnover meets the threshold of €750 million.

13 Other than complying with mandatory documentation requirements, describe any additional benefits of preparing transfer pricing documentation.

As there are no formal mandatory documentation requirements, the main benefit of preparing and keeping proper transfer pricing documentation is that it would assist in resolving any future transfer pricing enquiries by HMRC. In particular, it shifts the burden of proof to HMRC and in general helps the taxpayer to achieve and maintain a lower tax risk rating with HMRC.

Additionally, HMRC has the power to impose penalties on taxpayers if that taxpayer's inaccurate tax return, which was caused by careless or deliberate conduct, results in a loss of tax in the UK. Maintaining good transfer pricing documentation would help to demonstrate that the taxpayer had taken reasonable care in making any transfer pricing adjustments to its tax return, were this to be enquired into in future.

14 When must a taxpayer prepare and submit transfer pricing documentation to comply with mandatory documentation requirements or obtain additional benefits?

No additional documentation needs to be submitted to support an adjustment on the tax return, unless HMRC requests it. HMRC has information powers and may make formal requests for information if such information is not forthcoming in response to an informal request.

As mentioned above, CbC reporting is now law in the UK and applies to accounting periods commencing on or after 1 January 2016. The CbC regulations apply if the consolidated group turnover meets the threshold of €750 million.

15 What content must be included in the transfer pricing documentation? Are a separate 'master file' and 'local file' required? What are the acceptable languages for the transfer pricing documentation?

There are no formal requirements for transfer pricing documentation in the UK. HMRC's guidance on transfer pricing documentation refers to the OECD Guidelines at Chapter V, which contains recommendations in this regard. HMRC will also accept any documents prepared in accordance with the EU's Code of Conduct on transfer pricing documentation. Businesses that wish to follow this code, must write to HMRC to inform it of this.

Despite the lack of formal requirements, HMRC generally prefers transfer pricing information to be in the form of a full transfer pricing report written by a professional adviser. HMRC will accept documentation prepared on a global or a regional basis as long as the analysis can properly be applied to the UK transactions.

16 Has the tax authority proposed or adopted country-by-country reporting? What, if any, are the differences between the local rules adopting country-by-country reporting and the consensus framework of BEPS Action 13?

CbC reporting was implemented in the UK for accounting periods commencing on or after 1 January 2016. On 26 February 2016, HMRC announced a new measure requiring UK-headed multinational enterprises (MNEs), or UK sub-groups of MNEs, to make an annual CbC report to HMRC showing revenue, profit, and capital figures for each tax jurisdiction in which they do business. There is a threshold of €750 million consolidated group turnover before the regulations apply.

Adjustments and settlement

17 How long does the tax authority have to review an income tax return?

HMRC may enquire into a transfer pricing filing through its normal enquiry procedure for tax returns. This means that HMRC has one year from the date on which the return is filed to open any enquiry. Once the enquiry is formally opened, there is no time limit imposed on HMRC for concluding the enquiry, although HMRC's own guidance manual states that 'unreasonable delay' is to be avoided. The taxpayer may apply to the First-tier Tribunal (Tax Chamber) (Tribunal) to close an enquiry if necessary.

If an enquiry results in a transfer pricing adjustment but the disadvantaged person has already submitted their return for the relevant period, they will be permitted to amend their return in line with the adjustment. As noted at question 35, HMRC has issued a consultation document on the proposed introduction of a secondary adjustments rule in the UK.

18 If the tax authority asserts a transfer pricing adjustment, what options does the taxpayer have to dispute the adjustment?

If a settlement is not reached through the enquiry process, or if HMRC issues a closure notice containing a determination with which the taxpayer disagrees, the taxpayer may ask HMRC to review the point. Alternatively, HMRC or the taxpayer may appeal to the Tribunal for a determination as to the correct adjustment. The UK's most substantive transfer pricing case in recent times was *DSG Retail and others v HMRC*, which was decided by the Tribunal in 2009.

In cases where the UK has a comprehensive double-tax treaty with the other jurisdiction, and the taxpayer considers that the transfer pricing adjustment is incorrect, it may be able to apply for relief under the mutual agreement procedure (MAP). This would involve the taxpayer approaching the competent authority of the other jurisdiction and asking it to intervene. HMRC ought to cooperate with the other competent authority in attempting to reach a resolution.

Judicial review may also be an option where a taxpayer considers that one or more of the grounds for review are met: for instance, the taxpayer had a 'legitimate expectation' that HMRC would act in a certain way, and HMRC failed to do so. Other grounds include procedural impropriety, or irrationality. Judicial review applications may be made to the Tribunal.

Relief from double taxation

19 Does the country have a comprehensive income tax treaty network? Do these treaties have effective mutual agreement procedures?

The UK has a comprehensive double-tax treaty network – one of the largest in the world – and the vast majority of the UK's double-tax treaties have effective MAP clauses. More recent UK double-tax treaties also tend to include mandatory binding arbitration clauses, and it is hoped that these provisions will prove more effective at resolving disputes.

20 How can a taxpayer request relief from double taxation under the mutual agreement procedure of a tax treaty? Are there published procedures?

HMRC has published a Statement of Practice (1/2011, updated in April 2016) that sets out the procedure a taxpayer should follow in order to apply for relief under the MAP of a double-tax treaty. It is noted that in the UK there is no set form of presentation of a case; however, other countries may have different requirements and the taxpayer should ensure that the procedures of both jurisdictions are followed in making its application.

21 When may a taxpayer request assistance from the competent authority?

Where the MAP is invoked under a UK tax treaty, it must generally be presented before the expiration of six years following the end of the chargeable period to which the case relates (unless stated otherwise in the relevant tax treaty).

HMRC may also use its discretion to unilaterally relieve some or all of the double tax if it concludes that the taxation applied by its treaty partner is in accordance with the relevant double tax treaty.

22 Are there limitations on the type of relief that the competent authority will seek, both generally and in specific cases?

There are no such limitations.

23 How effective is the competent authority in obtaining relief from double taxation?

While HMRC does emphasise that there are no guarantees that the MAP will result in a binding agreement, it is generally considered to be effective at obtaining relief using this procedure. In the year 2014–15, HMRC resolved 25 cases and admitted a further 78. On average, such cases took 20.5 months to resolve.

Advance pricing agreements

24 Does the country have an advance pricing agreement (APA) programme? Are unilateral, bilateral and multilateral APAs available?

The UK has had an APA programme since 1999. Unilateral, bilateral and multilateral APAs are all available. Unilateral APAs are possible, but HMRC's preference is for bilateral APAs.

25 Describe the process for obtaining an APA, including a brief description of the submission requirements and any applicable user fees.

The business seeking an APA initiates the process, using the procedure set out by HMRC in its Statement of Practice 2/2010. HMRC requests that businesses considering seeking an APA contact HMRC first with an 'expression of interest' to discuss their plans before submitting a formal application. The intention is that HMRC can agree a timetable with the business. In many cases this will involve meeting with HMRC to discuss the issues. Such preliminary discussions may take place anonymously. Once HMRC has indicated that it is willing to consider the APA, the business may make a formal application. HMRC will then evaluate the application and seek further information from the business if required. Businesses should be prepared to grant HMRC open access to relevant documents and enter into an open dialogue with HMRC about the key issues. No fees are payable to HMRC.

Update and trends

The main UK highlights can be summarised as follows.

Brexit

The tax and transfer pricing impact of Brexit is yet to be fully determined, but is potentially far-reaching. We anticipate that business restructurings as a result of Brexit will result in more transfer pricing scrutiny in the UK. In practical terms, HMRC continues to embrace a risk-based approach to testing for compliance with the transfer pricing rules and focuses its resources on businesses that it considers to be less open and transparent about transfer pricing. HMRC also focuses its scrutiny on large and complex businesses, with statistics showing that while 391 reviews were started in the year to March 2015 (down from 450 in the previous period), two-thirds of the UK's largest 800 businesses were under active investigation. This is promoting new trends in transfer pricing documentation with businesses increasingly seeking to prepare and explain transfer pricing policies on an ex ante basis as opposed to ex post basis in the hope that this will help identify and resolve transfer pricing disputes more quickly and easily. Aligned with this, the BEPS project is partly responsible for an increasing acceptance of the profit split method by HMRC, in that there is an emphasis on measuring transfer pricing outcomes on the basis of the economic inputs relative to value contributions when assessing transactions. Such an emphasis is not always satisfied through traditional transactional methods, particularly in instances where differences between controlled and uncontrolled transactions cannot be reliably adjusted for. One traditional concern with the profit split method is that it is perceived as being responsible for increasing transfer pricing disputes although the new dispute resolution mechanisms proposed by BEPS may help alleviate that concern.

Interest barrier

The introduction of the interest barrier is likely to have a significant impact on groups that have annual interest expense/financing costs exceeding £2 million. Groups will need to identify their 'worldwide' group for the purposes of applying the rules and potentially revisit the ongoing structuring of any intra-group or acquisition financing. There have been some protests that the UK interest barrier rules overreach what is required by BEPS Action 4; however, it is yet to be seen how HMRC will approach the initial enforcement of these complex rules.

Whilst this is UK legislation, groups that are headed by a foreign entity may well still be tripped up by these rules where, for example, they issue debt to fund UK sub-groups.

Dispute resolution

HMRC continues to explore alternative dispute resolution as a means for resolving disputes and sees this as playing a greater role in its overall strategy going forward.

26 How long does it typically take to obtain a unilateral and a bilateral APA?

HMRC aims to complete the APA process within 18 to 21 months of submission of the formal application, and it acknowledges that unilateral APAs may be completed much more quickly. The timeline in relation to bilateral and multilateral APAs will depend also upon the procedures of the relevant administrations in the other country (or countries). Data released for the year ending 14 March 2014 indicate that the average time taken to reach agreement was 27.8 months, with 50 per cent of APAs being agreed within 19.7 months.

27 How many years can an APA cover prospectively? Are rollbacks available?

The business should propose a term for the APA in the application. Typically, this will be three to five years, depending on the length of time for which it is reasonable to suppose that the transfer pricing methods will remain appropriate. Rollbacks are available: the taxpayer may request this, or HMRC may propose that the roll-back of the APA would be an appropriate way of resolving enquiries into previous tax returns. The use of an APA in this way is subject to the agreement of other administrations in the case of bilateral or multilateral cases.

28 What types of related-party transactions or issues can be covered by APAs?

As set out in HMRC's Statement of Practice 2/2010, the potential scope of an APA is flexible and it may cover any number of a business's transfer pricing issues. Thin capitalisation issues are generally dealt with separately through a separate, similar, procedure. Generally HMRC will only consider agreeing an APA where the issues involved are complex, or where there is a high risk of double taxation, or where the business proposes to use a highly tailored method for its transfer pricing.

29 Is the APA programme widely used?

The latest publicly available statistics (released in 2015) show that 43 applications for APAs were made in 2013–14. During the same year, no applications were turned down, nine were withdrawn and 29 were agreed. HMRC considers that interest in the APA programme remains high. HMRC has not published any updated figures for subsequent years after 2015.

30 Is the APA programme independent from the tax authority's examination function? Is it independent from the competent authority staff who handle other double tax cases?

HMRC has a dedicated APA team that handles the APA process. Other HMRC employees who deal with the taxpayer's affairs and who already have knowledge of its business may also become involved in the process, particularly where a rollback is proposed to settle an enquiry.

31 What are the key advantages and disadvantages to obtaining an APA with the tax authority?

The key advantage for a business in obtaining an APA is that it provides certainty to the business that (if the terms of the APA are complied with) HMRC will accept the treatment of the business's transfer pricing issues for the term of the agreement. Bilateral and multilateral APAs are more useful in this regard as they provide similar assurances in respect of the other jurisdiction's tax administration, minimising the risk of double taxation.

A key disadvantage to the procedure is the time and cost involved in negotiating APAs. While HMRC's latest figures suggest that it agrees 50 per cent of APAs within 19.7 months, it can take a lot longer than this. The protection an APA provides is also limited to certain 'critical assumptions' about the reliability of the method, and compliance by the business with the terms of the APA. If HMRC considers that the critical assumptions no longer apply or that the taxpayer has not complied with the terms of the APA it may nullify or cancel an APA.

Special topics

32 Is the tax authority generally required to respect the form of related-party transactions as actually structured? In what circumstances can the tax authority disregard or recharacterise related-party transactions?

HMRC's guidance follows the OECD's Guidelines on this point. There are two broad circumstances where it may be appropriate to not recognise the structure of a related party transaction and to recharacterise it:

- where the economic substance of a transaction, viewed in its totality, differs from its form; and
- where the arrangements made with regard to the transaction are different from those that would have been made by independent entities behaving in a commercially rational way in comparable circumstances thereby preventing determination of an arm's length price.

33 What are some of the important factors that the tax authority takes into account in selecting and evaluating comparables? In particular, does the tax authority require the use of country-specific comparable companies, or are comparables from several jurisdictions acceptable?

HMRC sees internal comparables as preferable (ie, those from within the business itself with an unconnected third party). HMRC's practice suggests that for UK companies, it generally makes sense to consider UK comparables only at first. It acknowledges that the aim is to compare 'like with like', so the focus is on whether territorial boundaries actually create market differences. There are no set rules on the types of comparables which are acceptable and the focus is on how similar the transactions truly are, and whether reliable adjustments can be made to counter any differences.

34 What is the tax authority's position and practice with respect to secret comparables? If secret comparables are ever used, what procedures are in place to allow a taxpayer to defend its own transfer pricing position against the tax authority's position based on secret comparables?

HMRC will be aware of other similar companies' transfer pricing, but it does not use secret comparables in an enquiry for setting an arm's-length price.

35 Are secondary transfer pricing adjustments required? What form do they take and what are their tax consequences? Are procedures available to obtain relief from the adverse tax consequences of certain secondary adjustments?

HMRC launched a consultation on whether to introduce secondary adjustments into the UK's domestic transfer pricing legislation on 26 May 2016. This consultation closed on 18 August 2016. HMRC has not formally published the results of this consultation however, it is widely understood that they are not currently seeking to push forward with the implementation of secondary adjustments into UK domestic legislation.

36 Are any categories of intercompany payments non-deductible?

The introduction of the interest barrier rules (implementing BEPS Action 4) is likely to have a significant impact on how certain corporate groups manage their intercompany payments. HMRC published updated draft legislation and guidance regarding the implementation of the interest barrier rules on 13 July 2017.

The rules are expected to apply from 1 April 2017. Periods straddling this date are treated as two notional periods with the old 'worldwide debt cap' rules (previously found in Part 7 TIOPA 2010) applying to periods up to 31 March 2017 and the new interest barrier rules applying after this date.

The rules operate to restrict the extent to which a corporate group can claim deductions for interest expense and other financing costs to an amount that reflects the group's activities taxed in the UK. Whilst the rules apply to all companies within the charge to corporation tax, groups with less than £2 million of annual net interest expense and financing costs will not suffer any restriction as the rules only bite above that amount. Note that the £2 million de minimis threshold applies to the group as a whole rather than to each company within the group.

These rules are complex and their application to a group will need to be analysed on a case-by-case basis. However the broad principles are:

- a UK group is permitted to deduct a total of £2 million worth of interest expense/other finance costs per year without restriction;
- above this £2 million de minimis, groups must either apply the 'fixed ratio' or the 'group ratio'. The fixed ratio is the default position however groups may opt to apply the 'group ratio' if it gives a more favourable result (ie, higher level of deductions); and
- amounts which are disallowed in one accounting period may be carried forward and in certain circumstances be deducted in a subsequent period.

The latest guidance published by HMRC in relation to the interest barrier rules is 489 pages long, an indicator of how complicated the application of these rules can be.

37 How are location savings and other location-specific attributes treated under the applicable transfer pricing rules? How are they treated by the tax authority in practice?

HMRC applies the OECD's TPG in this regard.

38 How are profits attributed to a branch or permanent establishment (PE)? Does the tax authority treat the branch or PE as a functionally separate enterprise and apply arm's-length principles? If not, what other approach is applied?

The profits attributed to the PE are those which it might be expected to make if it were a separate enterprise, dealing independently with the enterprise. Profits are therefore calculated on an arm's-length basis.

39 Are any exit charges imposed on restructurings? How are they determined?

No specific exit charges are imposed on restructurings, although a transfer pricing adjustment may be applied within the normal course of transfer pricing, if certain aspects of the restructuring are considered not to be arm's-length. A UK taxpayer that restructures its business by moving assets out of the UK or migrating its tax residence to another jurisdiction will be subject to an exit charge unless a deferral or other relief applies.

40 Are temporary special tax exemptions or rate reductions provided through government bodies such as local industrial development boards?

Northern Ireland sets its own corporation tax rate and is committed to matching the Republic of Ireland's 12.5 per cent corporation tax rate for trading businesses by 2018.

There are a number of tax reliefs to encourage investment, eg, the enterprise zones scheme (which offers business rate reliefs and enhanced capital allowances). There are also enhanced reliefs for smaller businesses such as the enterprise and seed enterprise investment schemes, the venture capital trust scheme and enhanced research and development tax credits.

The UK also has a 'patent box' regime that allows companies to apply a lower (10 per cent) rate of corporation tax to profits from its patented inventions. This regime may change in line with BEPS implementation.

Individual investors may benefit from a reduced 10 per cent rate of capital gains tax (with a lifetime limit of £10 million) if they satisfy the conditions required to obtain entrepreneur's relief (for employees and office holders) or the new investor's relief (for others).

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