



Chartered
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Taxation
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Ref: EUHR

3 October 2018

Chris Stewart
HMRC

Via email: profitfragmentation.mailbox@hmrc.gsi.gov.uk

Dear Mr Stewart

Profit fragmentation: clause 10, Schedule 6 draft Finance Bill

We are writing to you regarding the draft profit fragmentation provisions contained in the draft Finance Bill clauses published on 6 July 2018. The provisions are included at clause 10 and Schedule 6 of the draft bill.

As an educational charity, our primary purpose is to promote education in taxation. One of the key aims of the CIOT is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation. Our stated objectives for the tax system are that it should include a legislative process which translates policy intentions into statute accurately and effectively, without unintended consequences. We envisage that this includes ensuring that legislation complies with EU law.

As currently drafted, it is our view that the profit fragmentation rules would be in contravention of EU law. We explain the basis for this view below.

We appreciate that Brexit is occurring. However, our understanding is that if a transitional arrangement is agreed it is anticipated that the fundamental freedoms will continue to apply after 29 March 2019. Therefore, we would have anticipated that you would be seeking to enact legislation that is compatible with those principles.

The profit fragmentation rules would potentially result in a different tax treatment when compared with the same arrangements if these were in a purely domestic situation. It is accepted that a fundamental freedom, such as that of establishment, can be restricted if there is a justification for doing so, the measure is proportionate and is reasonably necessary to achieve the stated aim. The heading for the legislation indicates that it is targeted at avoidance and paragraph 7 states that it only applies to arrangements where it would be reasonable to conclude that the arrangements had an

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object of obtaining a tax advantage. However, these tests are considerably broader than the jurisprudence of the European Court of Justice (CJEU) in cases such as *Cadbury Schweppes plc* (Case C-196/04) and *Hornbach-Baumarkt AG* (case [C-382/16](#)) suggests is permissible,

As a result, we consider that the proposed rules on profit fragmentation would be a restriction on the EU fundamental freedom of establishment.

The current draft legislation would seem to us to be at risk of falling into the same type of error of law as is highlighted in the CJEU case of *Hornbach-Baumarkt AG* (case [C-382/16](#)). To be compatible the arrangements would need to be more focused on arrangements that the CJEU has accepted as being abusive. The case law suggests that the mere fact that there may have been a prior transfer on non-arm's length terms to an enterprise carrying on a bona fide business is not sufficient to justify such a finding of abuse.

For these reasons we consider that the profit fragmentation rules would be liable to challenge under EU law.

Yours sincerely

Jeremy Woolf
Chair, EUHR Sub-Committee

The Chartered Institute of Taxation

The Chartered Institute of Taxation (CIOT) is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT's comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

The CIOT's 18,000 members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.