Chartered Institute of Taxation

30 Monck Street
London SW1P 2AP
T: +44 (0)20 7340 0550
E:post@ciot.org.uk

HMRC Consultation - International Tax Enforcement: disclosable arrangements

Response by the Chartered Institute of Taxation

1 Introduction

1.1 The Chartered Institute of Taxation (CIOT) is pleased to provide some comments on the draft regulations[1] which make provision for implementing EU Directive 2018/822 amending Directive 2011/16/EU[2] (otherwise known as DAC 6) into UK law, and to respond to the consultation document[3] which is setting out HMRC's current thinking and approach to interpreting DAC 6.

1.2 We have also met with HMRC on a number of occasions during both the pre-consultation period and the consultation period itself. This written response should be read in conjunction with the comments we have made verbally in meetings with HMRC.

1.3 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.

1.4 Our stated objectives for the tax system relevant to this consultation include:

1. A legislative process which translates policy intentions into statute accurately and effectively, without unintended consequences.
2. Greater simplicity and clarity, so people can understand how much tax they should be paying and why.
3. Greater certainty, so businesses and individuals can plan ahead with confidence.
4. A fair balance between the powers of tax collectors and the rights of taxpayers (both represented and unrepresented).
5. Responsive and competent tax administration, with a minimum of bureaucracy.

[1] The International Tax Enforcement (Disclosable Arrangements) Regulations 2019 DRAFT https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/818844/The_International_Tax_Enforcement__Disclosable_Arrangements__Regulations_2019_-_DRAFT.pdf

[2] COUNCIL DIRECTIVE (EU) 2018/822 of 25 May 2018 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements https://eur-lex.europa.eu/eli/dir/2018/822/oj

[3] HMRC consultation document – International Tax Enforcement: disclosable arrangements https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/818842/International_Tax_Enforcement_-_disclosable_arrangements__consultation_.pdf

2 Executive summary

2.1 Our main concern is that there could be a very large number of transactions requiring disclosure, with many being trivial and/or benign, creating additional burdens on businesses and taxpayers, and on HMRC which will have to process the information. Additionally, there may be unnecessary disclosures where intermediaries and taxpayers take a very precautionary approach in order to avoid the risk of penalties. We recognise that the Government is constrained by what is legally required by the Directive, but we would encourage HMRC to take a pragmatic approach to implementing the rules, where possible, in order that they can be manageable and workable in practice for everyone concerned.

2.2 We support HMRC's proposals to update their guidance iteratively after it is introduced. This will be helpful in understanding the scope of the rules and reducing uncertainty around whether a disclosure is required or not. We also note that HMRC are intending to share a draft of their guidance with stakeholders by the end of 2019. The CIOT would be pleased to comment on the draft.

2.3 With the uncertainty continuing around Brexit and the possibility remaining that the UK will be leaving the EU on 31 October 2019 without a withdrawal agreement, it is essential that HMRC provide clarification as soon as possible with regard to the implementation of DAC 6 in the UK. The previous government had consistently said that implementation would go ahead regardless of Brexit, and on the assumption of there being a withdrawal agreement and a transitional period, but the position is now much less clear. Advisers potentially affected by the measure want certainty. We make some further specific points regarding Brexit's effect on the implementation of the Directive in response to Question 22.

2.4 The consultation refers to there being a standard schema or template on which reports will need to be made (paragraph 6.4). We understand that HMRC have recently received the technical specifications from the EU. Can these please be shared with interested parties/firms as soon as possible, so they can have time to develop their systems to ensure they are compatible?

2.5 We note that on 27 June 2019 the Organisation for Economic Co-operation and Development (OECD) published the administrative and operational framework[4] for exchange of information on Common Reporting Standard (CRS) avoidance or opaque offshore structures collected under the mandatory disclosure rules. Part I of the document contains a draft multilateral competent authority agreement for exchanges under the mandatory disclosure rules, while Part II contains the XML schema and user guide. The plan appears to be that this framework will be used for disclosure of information about structures that avoid the CRS or opaque offshore structures from 1 January 2021. It will be interesting to see whether the EU drops the part of its own Mandatory Disclosure Rules (DAC6) which overlaps with this OECD framework, so as to share data internationally rather than just within the EU.

3 Q1. Do you have any suggestions about how HMRC can provide more clarity about when an arrangement will concern multiple jurisdictions?

3.1 We think some clarity is required as to when an arrangement between an employer and an employee will involve multiple jurisdictions. For example, where (i) an employer is based outside the UK and (ii) an employee is working in the UK then it would appear that we have a cross-border arrangement (paragraphs 2.2. and 9.7).

[4] http://www.oecd.org/tax/oecd-releases-international-exchange-framework-for-crs-related-mandatory-disclosure-rules-updates-xml-schemas-for-exchange-of-crs-cbc-and-tax-ruling-information.htm

This might apply, for example, because the UK entity is a branch of a non-UK entity such as a bank. Is this the case? We think it's important we get clarity in this respect.

4 Q2. Are there any people who might be caught by this approach to defining 'intermediary', who you think should not be caught?

4.1 It would be helpful for HMRC to confirm that a 'service provider,' such as a tax adviser or accountant, would not fall within the definition of 'intermediary' if they only subsequently become aware of a reportable cross-border arrangement after it has been implemented, for example whilst preparing a tax return for a client (similar to the 'auditor' example in paragraph 3.9 of the consultation document).

4.2 Could a professional adviser that assists an employer in, say, setting up a share scheme be regarded as an 'intermediary' if that share scheme includes employees who are resident in a state other than the state the employer is resident in? If so, would the 'normal' reporting of that scheme, for example in compliance with HMRC's Share Scheme reporting requirements, be sufficient to meet that the requirements of the DAC? (NB. This might also be relevant to Question 7 – Reporting obligations).

4.3 Also, where a tax adviser provides advice on, say, the tax consequences of a termination payment to an employee where the employer and employee are not resident in the same state, would the tax adviser be outside the scope of the 'intermediary' rules if their advice is asked for after the decision to terminate the employee's employment has been made (paragraph 3.9 refers).

4.4 A UK based adviser may sometimes receive unsolicited e-mails from, say, the US, offering some investment advice. Sometimes this includes eg the opening of a US bank account. In that situation, the US person has neither a place of business, a permanent establishment etc in the UK nor is a member of a professional body so is not an intermediary, and the arrangement may well have an effect of circumventing CRS so may be a reportable cross-border arrangement. Having received an unsolicited offer, because there is no intermediary, at what point might the recipient have a duty to report it? If no action is taken by the recipient and because it was an unsolicited e-mail, presumably there is no obligation on the recipient to report anything?

4.5 The DOTAS (Disclosure of Tax Avoidance Schemes) definition of promoter has some sensible carve-outs for second-opinions; non-tax advisers; benign tax-advice and ignorance. Perhaps the UK regulations and /or guidance (so far as the Directive allows it) could broadly say that anyone who falls within one of these exceptions will (generally) not be treated as an intermediary. If the Directive does not allow this, it would be helpful if these (and any other) differences between DOTAS (with which advisers will be familiar) and DAC6 could be publicised in the guidance.

5 Q3. Does this definition of intermediary risk not catching certain types of intermediary who should be caught?

5.1 No comments.

6 Q4. Do you identify any particular practical challenges with regard to HMRC's approach to identifying intermediaries, and what information they have in their knowledge, possession or control?

6.1 **Promoters and service providers, and the knowledge defence**

The consultation envisages two distinct types of intermediaries; those who design, market, organise, make available for implementation or manage the implementation of a reportable cross border arrangement ('promoters'), and those who provide aid, assistance or advice in relation to the designing, marketing, organising or implementing of reportable cross border arrangements ('service providers'). However, we are not sure that this distinction will always be clear-cut.

6.2 For instance, it is possible that a lawyer may have been involved in drafting a trust deed which it only later transpires is part of a wider arrangement. In these cases, the lawyer would argue that they are a 'service provider' since they did not know and could not reasonably have been expected to know at the time that they were involved in a reportable arrangement (paragraph 3.3.1). However, is it possible that because, for example, they made some changes to the drafting of the trust deed, they could in fact be a designer (and therefore a promoter), and so the knowledge defence is not available?

6.3 The knowledge defence is available to an intermediary who is a 'service provider', but what level of due diligence is 'normal' for the transaction or arrangement concerned (paragraph 3.6). It would be helpful if some examples teasing out potential 'dividing lines' between 'promoters' and 'service providers', as well as 'normal' and 'significant extra' due diligence, are included in the guidance, as we are not sure that the distinctions are as clear as the consultation makes out.

6.4 We note that there are some examples in HMRC's guidance[5] on the Enablers of Defeated Tax Avoidance legislation (Sch 16 Finance (No 2) Act 2017) which may be instructive in interpreting the extent of the 'knowledge condition' defence for 'service providers' in the Regulations.

6.5 As a general point, will the level of knowledge be looked at across the organisation or at an individual level?

7 Q5: Do you have any other comments about the definition of intermediary and who will be caught under the proposed rules?

7.1 **Residence – registered with a professional association**

We note that an intermediary will have to make a report to HMRC if it is registered with a professional association relating to legal, taxation or consultancy services in the UK (fourth bullet point in paragraph 3.14 and also 3.17 of the consultation document) and none of the preceding three conditions in paragraph 3.14 are met. A professional association, as defined, will include the CIOT, including individual members who are 'CTAs' (Chartered Tax Advisers), or students, and those who are 'International Tax Affiliates of the CIOT' holding our ADIT (Advanced Diploma in International Tax) qualification, or who are registered as ADIT students.

7.2 Whilst many of our members will in practice be employees of a firm, so that it will be the employing firm which is the intermediary and which is required to report (as detailed in paragraph 3.10 and Regulation 13), many may not, so they may still have to make reports if they are sole-traders or not otherwise employed by a firm.

[5] https://www.gov.uk/guidance/tax-avoidance-enablers-who-is-classed-an-enabler#knowledge-condition

7.3 Additionally, many of these individuals may not be resident in the UK or the EU, nor employed by firms resident in the UK or another EU member state, meaning that even if these individuals are employees of a firm, the firm may not be required to make a report in either the UK or another EU member state. In this scenario, we believe the reporting obligation will fall on the individual. We do not know how common such a scenario will be in practice, or indeed whether the individual would have enough information to know what to report. However, as a sensible precaution, we intend to update our guidance for members once the Regulations come into force.

7.4 On the wider point of UK qualified employees and partners of overseas firms we can envisage that this creates a difficult position for those individuals given the timescales for reporting. As a practical matter, one way of addressing this in networks of firms is to ensure that the relevant firm operating in the EU is involved and makes the appropriate reports. However, in practice it can take a significant length of time to reach a reporting conclusion and, allowing for different firm's operating styles, the deadlines are extremely tight. In paragraph 2.1 above, we ask HMRC to take a pragmatic approach to the application of the resulting law. A useful application of this would be in relation to the application of the reporting deadlines. Compliant organisations will make the necessary reports. Doing so on a timely basis, particularly where cross-border collaboration is involved, will be more of a challenge and it seems unfair to penalise employees for matters beyond their personal control.

7.5 **Partial disclosures**

It is likely that there will be many examples of 'service providers' only being aware of their own (possibly small) part in a reportable arrangement. Can HMRC confirm whether they expect partial disclosure reports to be made? Presumably, the smaller the part the 'service provider' has in an arrangement, the more likely they are to be able successfully to argue that they could not reasonably have been expected to know that they were involved in a reportable arrangement, and so have no obligation to report.

7.6 **Definition of 'makes available'**

Many advisers will be 'service providers' rather than 'promoters'. One consequence is that these service providers are likely to have to report the part of the transaction on which they advise before the promoter is required to report. This appears to frustrate the intention behind DAC6, which is that the main promoter (if there is one) would make a comprehensive disclosure of the whole arrangement, rather than lots of partial disclosures from service providers.

7.7 **Legal Professional Privilege**

Paragraphs 3.18 and 3.19 of the consultation document discuss legal professional privilege (LPP). Paragraph 3.18 starts: *'…[legal professional privilege] does not exempt lawyers from making reports at all, as other information that is not legally privileged may still need to be reported*'. Whilst this is correct in theory, taken with what comes after, it could be misleading.

7.8 Paragraph 3.18 continues (emphasis added): 'In providing aid, **advice** or assistance in relation to an arrangement, it is likely that much of the information that would need to be reported will **not** be covered by legal professional privilege, because it will be **factual** in nature.'

7.9 This appears to be a misunderstanding about legal professional privilege which, we understand, is not limited to non-disclosure of the legal advice that was given. It is our understanding that a lawyer cannot disclose either the substance or the subject matter of confidential communications made or received for the purposes

of seeking or giving legal advice. The Law Society's guidelines for DOTAS make clear legal professional privilege would encompass facts or details of a proposal contained within such communications between a lawyer and a client (even if they are available from other sources) and, consequently, a lawyer may not disclose this information without the consent of the client.

7.10 The consultation document continues (paragraph 3.19): 'For example, the names of relevant taxpayers and other intermediaries are highly unlikely to be legally privileged and so a lawyer would still need to make a report covering that information'. Our understanding of the position is that, if the names have been disclosed to the lawyer for the purpose of obtaining legal advice about the transaction, and it is not obvious what other purpose there would be in the client disclosing them to the lawyer, then the disclosure is privileged.

7.11 Also in paragraph 3.19: 'Similarly a description of the transactions that are to be undertaken as part of the arrangements would not normally be subject to legal professional privilege, and so would have to be reported, even if certain elements of the advice the lawyer provided were exempt from reporting due to legal professional privilege.' It is our understanding that this is not a correct summary of the law of legal professional privilege as determined by the UK Courts and that a description of the transactions for the purposes of obtaining legal advice is covered by legal professional privilege (*R (Morgan Grenfell & Co Ltd) v Special Comr of Income Tax [2003] 1 AC 563* and *Three Rivers No 6 [2005] 1 AC 610*).

7.12 It would be helpful if these aspects could be corrected in the guidance. We recall that similar criticisms of HMRC's approach were made when DOTAS was introduced in July 2004 and amending regulations[6] were laid after the Committee Stage over the summer. It is our understanding that DOTAS has worked perfectly well from an LPP perspective.

8 Q6. For the purposes of the ongoing requirement on relevant taxpayers, do you agree that a relevant taxpayer should be regarded as participating in the arrangement in any year where there is a tax effect or where it could reasonably be expected that there would be a tax effect in a subsequent year?

8.1 The issue may be more fundamental than that suggested in the consultation document. Supposing there is an intra-group disposal (into the UK) to which Hallmark C4 (or E3) applies. The effect is that a UK company now has a source of UK taxable income which it did not previously have. The regulation seems to say that so long as there is a tax effect the arrangement needs to be reported. This could be indefinitely if the asset is held for a considerable length of time.

9 Q7. Do you agree that the amount of evidence required for intermediaries and taxpayers to satisfy themselves and HMRC that all the necessary information has been reported is appropriate?

9.1 It seems probable that intermediaries will be less likely to try to satisfy themselves that a report has been made by another intermediary (paragraph 6.1) and that the information they would have to report has already been reported (paragraph 6.2), and will be more likely to make their own report. Partly this will be

[6] Tax Avoidance Schemes (Promoters and Prescribed Circumstances) Regulations SI 2004/1865 reg. 6 inserted by the Tax Avoidance Schemes (Promoters, Prescribed Circumstances and Information) (Amendment) Regulations SI 2004/2613 reg 2, with effect from 14 October 2004 and amended by SI 2012/1836, reg 18 with effect from 1 September 2012.

because of their own risk management procedures, but also because the tight reporting deadlines could mean there is insufficient time for another intermediary to provide a reference number.

9.2 The procedure seems to rely on the relevant tax authority making the reference number available. Whilst we understand that HMRC intend to issue reference numbers instantaneously, other authorities may be less quick, for example we have heard that the Polish tax authority (whose regime is already operational) takes several weeks to issue the reference number.

9.3 If no report is required in the UK but one is required in another EU member state, will it be necessary to include the reference number from the other member state on UK tax returns?

9.4 Regulation 11 Provision of Information –

- there does not appear to be any provision for appeal against an HMRC officer's decision that information or documents are 'reasonably required'. There should be a right of appeal here.
- the requirement to provide the information and documents requested within 'no less than 14 days' is too tight. This is only 10 working days. In our opinion, it will be extremely difficult to meet this deadline in practice. Assuming it runs from the date HMRC issue their request, as well as factoring in postal delays (it often takes 2 weeks or longer for a letter from HMRC to arrive to the right person in the receiving organisation) and the time it might take to understand the impact of the letter and find the information (it may take 2-3 weeks to conduct a thorough search to collate, then check and despatch the information requested; longer if key staff are away), the taxpayer may need to obtain legal advice (which might take another 2-3 weeks). At least 56 days (ie 40 working days) is more reasonable.

9.5 Where an arrangement involving an employer and an employee is potentially caught it is not obvious who is responsible for the reporting. For example, an employee's employment is terminated and as a result they receive a termination payment, exercise rights from shares schemes and take benefits from pension arrangements. If the employee receives a tax advantage from arranging the timing of those payments so that the employee is resident in a particular state, or in different states for particular events, is the employer, share scheme administrator or pension scheme administrator responsible for reporting? If so, how would they necessarily know that a tax advantage was obtained by the employee?

10 Q8. Do you think that the approach to defining the main benefit test and tax advantage is proportionate?

10.1 In the context of applying these rules to transactions/arrangements involving UK land, we note this is an area which has been subject to an intense period of legislative change in the last few years. The stated purpose of these changes is to 'level the playing field' between UK and non-UK residents in relation to the taxation of UK land. Given that the taxing rights (in relation to income and gains) of the territory in which the land is located are safeguarded under double tax treaties, the scope for obtaining a tax advantage in relation to 'cross border arrangements' in respect of UK land is significantly limited. Given these recent changes, and the clear policy intent behind these changes, we would expect that the criteria regarding whether or not there is a 'tax advantage' (as defined in Regulation 12(1) (a)) arising from a cross border arrangement (as defined for these purposes and further elaborated on in paragraph 7.7 of the consultation document) can be applied with certainty in most cases in relation to the taxation of UK land. However, as there are a number of hallmarks which do not have a 'main benefit test', we set out below some examples of typical commercially driven

arrangements involving UK land, where the position may be less clear (see paragraphs 13.2, 16.1, 16.2 and 19.2 below).

10.2 Can HMRC confirm that normal and innocuous commercial transactions involving employees do not give rise to a 'tax advantage' (as defined in Regulation 12 (1) (a)), because they are not inconsistent with tax principle or policy? We note some examples of such transactions involving employees in the following paragraphs.

10.3 In an employer/employee situation there will be situations where employees exercise share options or receive termination payments or make payments into pension arrangements etc. There are rules in the UK for establishing how these events are taxed. Other states have different rules and Double Tax Treaties may also apply to arbitrate and, for example, provide for only one state to tax the event. In a cross-border situation this can result in less tax being paid as a result of the employee being resident in one state rather than another when the event occurs. Is this within the definition of gaining a 'tax advantage'? If there is a tax advantage in timing an event so that the employee is resident in one state rather than another, or as a result of the natural consequence of the employee moving from one state to another, would the 'benefit' of that arrangement be considered to be within the definition of 'main benefit or one of the main benefits'?

10.4 Another example might be where an individual benefits from Overseas Workday Relief (OWR). OWR is restricted to non-UK domiciles and is available for the tax year they become UK resident and the following two tax years where the individual works partly in the UK and partly overseas. It treats the overseas earnings as foreign earnings and only taxes them when they are remitted to the UK. Is this gaining a 'tax advantage'? If so, would the main benefits test be passed?

10.5 We think that the lack of an 'intention' test is problematic. In an employer/employee context the interaction of different states' tax rules can mean that less tax, and in some cases no tax, is paid as a result of the employee's state of residence at the time of the event. In many cases there will have been no intention to 'avoid' tax. In others, there may have been advice as to the consequences of the timing of the payment. In all cases, events arising from share schemes, pensions, terminations etc are usually the result of 'normal' commercial arrangements between the employer and the employee and are 'not contrived' arrangements. We think that there is a difference between arranging the best tax treatment for Internationally Mobile Employees (IMEs) receiving payments as a result of events involving share schemes, pension schemes, termination payments, etc and contriving to be paid in, for example, platinum bars, fine wines, etc in order to reduce ones liabilities to tax.

11 Q9. Do you have any comments on the approach set out for hallmarks under Category A?

11.1 No comments.

12 Q10. Do you have any comments on the approach set out for hallmarks under Category B?

12.1 In the context of Hallmark B(2) – Income into capital or other categories of revenue which are taxed at a lower level or exempt (paragraphs 9.4 to 9.9 refer), paragraph 9.7 refers to share options and notes where there is conversion of income into gains they are *'a legitimate commercial choice to remunerate employees'* (unless arrangements are *'contrived, or are not normal commercial practice'*). This is a welcome clarification and we think it would be helpful to incorporate this in HMRC guidance. Similarly, will contributions into registered

pension plans which are tax deductible for the contributor and tax exempt in the plan be regarded in the same way? If so, we think this should be incorporated into guidance too. Furthermore, where transfers are made from registered plans into Qualifying Registered Overseas Pension Schemes (QROPS), in accordance with the prescribed rules, it would also be helpful to have confirmation that no reporting is required (or in what circumstances reporting may be required).

12.2 Additionally, what is the position of employee termination payments in relation to Hallmark B(2)? For example, for those repatriating from the UK then, depending on when payments are made, whether they are contractual or non-contractual, and how any applicable treaty applies etc. it may be that a better or worse tax treatment applies in the UK/home country. It would be normal for tax advisers to assess the position and advise the employee (and employer) accordingly. For example, as a result of advice it may be that a termination payment that benefits from foreign service relief in the UK is also not taxed in the country of residence if the payment is made at one point rather than another. Confirmation that such advice is not reportable would be helpful - or if it might be then in what circumstances. If it is reportable in some circumstances, then examples would be helpful to illustrate this.

12.3 The same applies to distributions from unregistered pension plans such as employer financed retirement benefit schemes (EFRBS). Again, confirmation that such advice is not reportable would be helpful – or if it would be then in what circumstances (and can examples be included in guidance to illustrate this).

12.4 Another common situation is application of the remittance basis for those who are non-UK domiciled where, for whatever reason, the amounts may not be taxable overseas. This arises not because the situation is contrived but merely because of the legislation applicable in that territory. Again, we presume that such advice is not reportable under hallmark B(2) but confirmation of this will, in our view, be vital. Many non-domiciled individuals are advised by smaller advisers who may not be well equipped to deal with DAC6 (whereas in the corporate sphere advisers are generally larger and better prepared).

12.5 And what happens where, for example, an assignee (employee) becomes non-UK resident on returning to their home state and then disposes of shares where, for whatever reason, no Capital Gains Tax (CGT) applies in the home state, for example, because the country concerned does not impose CGT. This is not contrived, and we presume that Hallmark B(2) does not apply but confirmation of this would be welcome.

13 Q11. Are there any points in the definition of associated enterprise which you think require clarification or explanation in guidance?
Q12. Do you think the above approach will prevent unnecessary reporting of benign activities, while avoiding loopholes that could enable intermediaries and/or relevant taxpayers to avoid their reporting obligations? If you foresee problems with this approach, please provide details of possible solutions.
Q13. Do you think that this approach will also work for dealing with Collective Investment Schemes? Alternatively, what other approaches do you think would be better?

13.1 Hallmark C(1) captures arrangements where there is a deductible cross border payment made between two associated enterprises where certain conditions are met. (Paragraphs 10.3 onwards refer.) If, for example, a regional / global employment company is established in a country with a 'preferential tax regime' and it takes on employees previously employed in the UK and charges a commercial mark-up there will be deductible cross border payment made between two associated enterprises that potentially falls to be disclosed under

Hallmark C(1) condition (d). Is it the intention of the regulations that this arrangement should trigger reporting? If not, it would be helpful to have confirmation of this in guidance.

13.2 i. A typical commercially driven arrangement involving UK land might concern a widely held real estate fund which is established in the form of a Limited Partnership which holds the shares in a company which then acquires a UK investment property. A loan is made by the partnership to the company to fund the acquisition of the property. From 6 April 2020 the company will be subject to UK corporation tax in respect of its UK property rental business and the corporation interest restriction/anti-hybrid rules will apply where appropriate.

ii. Based on the comments in paragraph 10.7 of the consultation document, in determining whether any of the hallmarks (within category C1) apply, if the partnership is treated as 'transparent' for the purposes of determining who is taxable on receipt of the interest, it is necessary to determine the status of that person to the extent that they and the company are treated as 'associated enterprises'.

iii. As a widely held real estate fund it is possible that one or more of the investors may be resident in a non-cooperative tax jurisdiction (per hallmark C1(b)(ii)), be a person who is not resident for tax purposes in any jurisdiction (per hallmark C1(b)(i)), or resident in a jurisdiction which does not treat the partnership as transparent and therefore arguably it is the partnership which is regarded as the recipient (and therefore hallmark C1(a) may apply). Given that the fund manager is likely to have information regarding the residence of the investor, it cannot be assumed that the fund manager would not be aware of the potential application of these hallmarks.

iv. However, as noted above, the hallmarks in C1 only apply in relation to cross border payments made between two or more associated enterprises. The question is therefore whether or not the partners in a widely held real estate fund would be regarded as an associated enterprise of a fund and the entities in the fund.

v. Per Article 1(1)(b) of the DAC 'For the purposes of Article 8ab, 'associated enterprise' means a person who is related to another person in at least one of the following ways:

> (a) a person participates in the management of another person by being in a position to exercise a significant influence over the other person;
>
> (b) a person participates in the control of another person through a holding that exceeds 25 % of the voting rights;
>
> (c) a person participates in the capital of another person through a right of ownership that, directly or indirectly, exceeds 25 % of the capital;
>
> (d) a person is entitled to 25 % or more of the profits of another person.

vi. If more than one person participates, as referred to in points (a) to (d), in the management, control, capital or profits of the same person, all persons concerned shall be regarded as associated enterprises. If the same persons participate, as referred to in points (a) to (d), in the management, control, capital or profits of more than one person, all persons concerned shall be regarded as associated enterprises. For the purposes of this point, a person who acts together with another person in respect of the voting rights or capital ownership of an entity shall be treated as holding a

participation in all of the voting rights or capital ownership of that entity that are held by the other person.'

vii. In this particular case, there may well be an investor who, as a 'seed investor' initially has a 25% stake in the fund and, more generally, in applying this test the question is whether all of the investors 'act together' given that, in the case of a collective investment vehicle, it will be the fund manager eg the general partner of the partnership who will be managing the fund on behalf of the investors. Clearly, as potentially indicated in questions 12 and 13 in the consultation document, the definition of associated enterprise to collective investment vehicles does require some further guidance/clarification to avoid 'unnecessary reporting of benign activities'. Also as noted in the examples at paragraphs 17.1, 17.2 and 20.2 below, it may be the case that it is only for UK tax purposes that the payment of the interest is relevant.

14 Q14. Do you think particular guidance is needed in respect of hallmark C(3)?

14.1 It was expected that HMRC would exclude the need to report cases where there is double income and double tax relief (DTR). For example, where a company in country A has a permanent establishment (PE) in country B and receives income from a third country under deduction of tax, both the head office (assuming no branch exemption) and the PE would claim DTR. There appears to be no policy reason for requiring this to be reported. Similar situations arise where DTR is claimed by a direct recipient, and its parent (if the recipient is a controlled foreign company (CFC)).

15 Q15. Do you agree that this hallmark should refer to the amount treated as payable for tax purposes? What do you think are the advantages and disadvantages of this approach, and of any other suggested approaches?

15.1 No comments.

16 Q16. Do you have any general comments about the approach to hallmarks under category C?

16.1 A typical commercially driven arrangement involving UK land might concern the sale of shares in a company owning UK land by a UK tax resident company to a third party non-UK tax resident company for a fixed price plus 'overage' payments: the 'overage' payments being unascertainable if they are dependent on future planning permission being obtained in respect of the land and/or any potential development profits realised. In relation to the disposal by the UK tax resident company, depending on the specific facts and circumstances, it will be necessary to carefully consider the treatment of any capital gain in relation to the consideration and whether the Transactions in UK land provisions apply. This would impact on the amount treated as consideration on the disposal of the shares and how this amount would be taxed. However, in relation to the purchaser, who as a non-UK resident may be within the charge to UK tax on a subsequent disposal if the company is UK property rich, the amount which is treated as payable in consideration for the shares (if relevant) may be different. It is unlikely that the seller or their advisers will have any detailed knowledge of the tax position of the buyer (or vice versa) in respect of such transfers.

16.2 In theory, Hallmark C4 (transfer of assets with material difference in consideration in the jurisdictions) could apply. However, it is assumed that paragraph 3.12 of HMRC's consultation document ('To be reportable by an intermediary, information must be in its knowledge, possession or control') would apply here, even if there is no intermediary and the buyer/seller would otherwise need to disclose? Also, as noted in the example at paragraph 20.2 below, it may be the case that it is only for UK tax purposes that the consideration is relevant. Please would HMRC confirm whether our interpretation is correct, or not?

17 Q17. Do you have any comments about the approach to hallmarks under Category D?

17.1 No comments.

18 Q18. Where an arrangement relates to companies which are resident for tax purposes in jurisdictions where corporate tax applies at the group level, should hallmark E(3) similarly apply at the level of the sub-group located in that jurisdiction or at the company level? What would be the particular advantages or disadvantages of applying the rules at the group level?

18.1 No comments.

19 Q19. Do you have any comments about the approach to hallmarks under Category E?

19.1 It is unclear from the consultation document whether Hallmark E(3) Cross Border Transfers (paragraph 12.11 onwards) applies to an intra-group transfer of shares. Both the heading and the context, including the references to '*arrangements involving an intragroup cross-border transfer of functions and/or risks and /or assets*' suggests that the hallmark is targeting cases where part of a business is carved out and transferred to a company in another territory. However, the words seem capable of being applied to a transfer of shares; notwithstanding that there are difficulties, e.g. how does earnings before interest and taxes (EBIT) apply to such cases; how do you apply the projected earnings test to dividends, given that normally companies do not project dividend income from their subsidiaries. Given that neither disposals of shares nor dividend income are within the scope of transfer pricing, and Hallmark C4 targets such transfers, could HMRC make it clear that Hallmark E(3) does not apply to share transfers? Without this there would be significant numbers of disclosures, probably swamping everything else, in most of which no tax was at stake.

19.2 i. A typical commercially driven arrangement involving UK land might concern a transfer within a group of a UK investment property from a company resident in one territory to a company resident in a different territory. The rental income is subject to UK tax both before and after the transfer, and any capital gain on the transfer is also within the charge to UK tax (although no gain or loss would arise if, as is likely, the provisions of section 171 TCGA 1992 would apply). To the extent that either company is not tax resident in the UK, it is unlikely that there would be any tax impact in the territory in which it/they are resident (either because it is not subject to tax, the tax rate is zero, there is a domestic relief, or the provisions of a double tax treaty apply). Whilst such a transaction may not result in any 'tax advantage', or have any tax consequences in a territory other than the UK, consideration would have to be given as to whether or not such an arrangement falls within Hallmark E3 (applicable, inter

alia to cross border transfers of assets) assuming the condition regarding the projected annual EBIT is satisfied.

ii. The definition of 'cross border arrangement' specifically includes situations where there is activity in one jurisdiction (ie in this case the UK) by a participant (in this case one or both of the companies concerned) which is not resident in that jurisdiction (ie the UK) (article 3(18) of the DAC). In paragraph 2.4 of the consultation document it is stated that 'HMRC is of the view that in order for the arrangements to 'concern' multiple jurisdictions, those jurisdictions must have material relevance to the arrangement'. Presumably in the circumstances set out above (where there are only UK tax consequences of the transfer), the only jurisdiction that would be required to be taken into account is the UK, and therefore the hallmark would not be satisfied? Please would HMRC confirm whether our interpretation is correct, or not?

20 Q20. Do you have any suggestions for how the penalty regime could be improved?

20.1 Regulation 14 (1) states that daily penalties of £600 per day will be imposed for failures to comply with certain provisions of the Regulations. In our view, the penalty should be a one-off charge, subject to mitigation provisions similar to those in Schedule 24 Finance Act 2007. Daily penalties seem inappropriate in this context because the failure might be a consequence of an active decision by an intermediary or taxpayer not to make a return, rather than an ongoing failure. In other words, the intermediary or taxpayer will have taken the view that a return is not required, so if there is a failure it is really a failure to take reasonable care not simply a failure to file a return by a certain deadline.

20.2 In view of the high level of uncertainty around the application of the rules, and the fact that 'benign' transactions are likely to be caught, the level of penalties appears disproportionate, given that daily penalties can quickly add up. We would encourage HMRC to take a 'light touch' approach to penalties, particularly in the early days of the regime.

20.3 We also note that Regulation 15(4) states that the amount of the penalty under Regulation 14(1) is to be arrived at after '*taking account of all relevant considerations*'. It would be helpful if some indication of how this will be interpreted by HMRC is included in the guidance.

21 Q21. Do you have any particular comments about the commencement rules, and HMRC's approach to dealing with the backdated reporting requirements?

21.1 We welcome the statement from HMRC in paragraph 14.4 of the consultation document that '*Where a failure relates to an arrangement where the first step of the implementation predates the publication of this consultation document and the draft regulations, and the failure was due to a lack of clarity around the obligations or interpretation of the rules, which could not reasonably have been inferred from the DAC itself, it is likely that the person will have a reasonable excuse for the failure. Where a person has a reasonable excuse, no penalty will be due*'. We trust that HMRC will take a pragmatic approach to applying penalties in these circumstances.

22 Q22. Are there any particular areas of DAC 6 that you would like HMRC to provide guidance on, which are not covered elsewhere in this consultation?

22.1 **Brexit**

Will the definition of a cross border arrangement be changed to cover at least one of (i) a member state and (ii) the UK, or will our obligation to disclose remain only where a member state is involved (so that a transaction between the UK and a third country after Brexit will not be disclosable in the UK under EU DAC6 and its UK implemented version)?

22.2 If the UK leaves the EU without a deal on 31 October 2019, how will this impact on the UK's access to the shared central EU database? It is not clear whether the UK will continue to be able to access the database once it has left the EU, particularly in a no-deal scenario. It would appear that in the event of a no-deal Brexit the UK might only be able to implement reporting in the UK, and that sharing information with EU member states via the EU database will not be possible, given the EU General Data Protection Regulation (GDPR) and the fact that the UK will not be part of the EU. If this is indeed the position, might there be alternatives ways of sharing information under existing rules, such as exchange of information?

23 Acknowledgement of submission

23.1 We would be grateful if you could acknowledge safe receipt of this submission and ensure that the CIOT is included in the List of Respondents when any outcome of the consultation is published.

24 The Chartered Institute of Taxation

24.1 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 18,500 members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

The Chartered Institute of Taxation

11 October 2019