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Reform of UK law in relation to transfer pricing, permanent establishment and Diverted Profits Tax
Response by the Chartered Institute of Taxation

1 Executive Summary

1.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the UK for advisers dealing with all aspects of taxation. We are a charity and our primary purpose is to promote education in taxation with a key aim of achieving a more efficient and less complex tax system for all. We draw on the experience of our 19,000 members, and extensive volunteer network, in providing our response.

1.2 We welcome the overarching theme of the proposed changes in the consultation on *Reform of UK law in relation to transfer pricing, permanent establishments and Diverted Profits Tax*, which is to align the UK's domestic legislation with equivalent international OECD standards to ensure consistency of application. Differences from the agreed international guidelines complicate compliance for taxpayers and reduces the benefit of having reached a global consensus as to what the rules should be. The updated rules could provide greater certainty, assist in the settlement of mutual agreement procedures (MAP) and enhance the attractiveness of the UK. However, the areas under consideration are complicated and care will be required to ensure the objectives are met.

1.3 Broadly we welcome the proposed changes to the transfer pricing rules. We suggest that consideration is given to how the rules could be written so as to not inevitably include joint ventures, and automatically treat these as connected when developing the tests of connectedness. We strongly support a change to the UK rules to align with international standards and to allow the consideration of implicit support and guarantees in determining the amount and terms of debt available at arm's length.

1.4 We are undecided about the proposals to align the UK domestic definition of permanent establishment (PE) with Article 5 in the 2017 OECD Model. Doing so would be a simplification, for both taxpayers and tax administrators, and we support the principle of aligning with the OECD Model. However, the concerns expressed by businesses about the potential impact of the changes to Article 5 (that the changes would cause less certainty and, potentially, lead to a proliferation of PEs) remain valid; insufficient time has passed to conclude that they are not giving rise to the problems foreseen.

1.5 We agree that a closer alignment of a diverted profits charge assessment to the Corporation Tax (CT) enquiry framework would be a welcome simplification and that bringing Diverted Profits Tax into CT would be

beneficial. In particular, it would bring Diverted Profits Tax within the scope of double tax treaties, including access to MAP for resolving disputes.

2 About us

2.1 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. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.

2.2 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.

2.3 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.

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

3 Introduction

3.1 We welcome the consultation on *Reform of UK law in relation to transfer pricing, permanent establishments and Diverted Profits Tax* published in June 2023[1]. The government had said in April that it would consult on updating the legislation in these areas to ensure consistency with 'underlying policy intention, international standards and the UK's bilateral treaties', and we are pleased to be able to respond to this consultation. Representatives of the CIOT attended the consultation meetings held by HMRC at the end of June/early July and our comments reflect what we understand to be the government's views as a result of the discussions at those events. Abbreviations used in the consultation document are used in our response below.

3.2 We welcome the overarching theme of the proposed changes, which is to align the UK's domestic legislation with equivalent international OECD standards to ensure consistency of application. Our stated objectives are for a tax system that includes greater simplicity and clarity, so people can understand how much tax they should be paying and why, and greater certainty, so businesses and individuals can plan ahead with confidence, alongside a responsive and competent tax administration, with a minimum of bureaucracy. The proposed reforms set out in the consultation document should help to create a simplified, streamlined, and modernised domestic law while promoting tax certainty. Many of the government's proposals would provide welcome clarity. As a general principle, alignment with the OECD Model and bilateral tax treaties reduces the compliance work for businesses, and the administrative burden for tax authorities. Each incidence of countries doing things differently to the agreed international guidelines reduces the benefit of having reached a global consensus as to what the rules should be.

3.3 The timetable suggested is further informal technical consultations in Autumn 2023, followed by legislation at either an Autumn Budget in 2023, or a Spring Budget in 2024. Accepting that the timetable relies on the scheduling of future fiscal events, we also note that the consultation is broad in its scope. In

[1] Reform of UK law in relation to transfer pricing, permanent establishment and Diverted Profits Tax - GOV.UK (www.gov.uk)

light of this, different aspects of the proposals may progress at different rates following the end of the consultation period. As there is not currently no fixed timetable for the implementation of any of the reforms, we encourage the government to move forward with different aspects of the reforms where it can, rather than necessarily waiting for the package as a whole to be settled. We would also caution against rushing to meet a specific fiscal event, especially for next year's Finance Act. Proposals for a reform such as this should go through all five stages of the consultation process to ensure that the final solution does not have to be revisited in subsequent Finance Act(s).

3.4 While these reforms may take some time to finalise and implement, if they result in final legislation that achieves HMRC's stated aims and the new framework corresponds more closely to current international principles and case law, that would be welcome. In particular, updated rules could provide greater certainty, assist in the settlement of mutual agreement procedures (MAP) and enhance the attractiveness of the UK. However, great care will be required to reach outcomes that achieve the stated objectives, given the complexity of the areas under discussion.

4 Transfer pricing

4.1 **Question 1**: The government welcomes respondents' views on the term 'provision' within s. 147 TIOPA 10. Specifically, is this term commonly understood, does it provide anything more than 'conditions' per Article 9 of the OECD Model, and do respondents encounter any practical difficulties which result from the difference in terminology between UK domestic law and the Treaty?

4.2 We welcome the proposed change to replace the use of the term 'provision' with the OECD Model term 'conditions' in order to ensure alignment with the international model. We do not anticipate that this change would substantively affect HMRC's application of the transfer pricing rules in practice, because the guidance (in HMRC's International Manual) states that 'provision' should be interpreted as broadly equivalent to 'conditions' as used in the OECD Model. Ensuring consistency of language would provide an increased level of certainty and is likely to be helpful in MAP.

4.3 **Question 2**: The government welcomes respondents' views on the participation condition, and experiences of the application of other jurisdictions' laws in that regard.

4.4 Simplification and clarification of the UK rules for the participation condition would be welcome. We do not have strong views as to which type of test for assessing control, or connectedness.

4.5 However, we suggest that consideration is given to how the rules could be written so as to not inevitably include joint ventures (through their treatment as automatically connected) but instead reflect the commercial reality. Currently, joint ventures are treated as connected, with the result that a transaction between a joint venture and a participant being treated as a controlled transaction. In reality, participants in a simple joint venture (say 50/50 ownership) often very robustly negotiate transactions between them and the joint venture, meaning that these are on arm's length terms. It is unnecessarily burdensome to have to treat these transactions as controlled transactions, and then have to demonstrate why they are on arm's length terms, particularly as these transactions are often hard to bench mark. Treating it as a controlled transaction also prevents it from being a comparable uncontrolled price.

4.6 Automatically bringing these transactions within scope of the rules adds an extra piece of transfer pricing work. It would be preferable if the consideration of the arm's length relationship could come at the earlier stage of determining whether the parties are connected. We appreciate that it may not be possible to demonstrate an arm's length relationship where there are more complicated joint venture arrangements, and/or many transactions between the relevant parties. The legislation should be framed so that more complex arrangements are brought within the rules, or if it is not possible to demonstrate an arm's length

relationship. But a rebuttal presumption around connectedness would be welcome to take out of scope those transactions where the relationship itself can clearly be demonstrated to be at arm's length.

4.7 Demonstrating that the parties participating in the joint venture are doing so on an arm's length basis, is often a more straightforward transfer pricing analysis (for taxpayers and tax authorities) than the work that has to be done if the transactions are deemed to be controlled (which would then involve bench marking and profit split analysis). This approach would also mean that the price of the underlying arm's length transaction may be available to be used as a comparable uncontrolled price, and available as evidence, within the rest of the group.

4.8 **Question 3:** The government welcomes respondents' views on the 'one-way street': how frequently do tax disadvantages arise, and do taxpayers commonly amend underlying contracts to avoid the unfavourable outcomes? Is the purpose of the 'one-way street' fully understood and how does it compare with comparable rules in other jurisdictions? How does the 'one-way street' factor in commercial decision making (if at all)?

4.9 We would welcome further clarity and guidance around the 'one-way street', its general purpose and application. It particular, greater certainty around its operation at the level of a provision (which must be between two persons) and on a chargeable period basis. The concept of a domestic mechanism for unilateral (downwards) corresponding adjustments without having to go through MAP would be a welcome simplification. But we appreciate the difficulties of devising ways to relax the one-way street approach without creating a risk of double non-taxation.

4.10 **Question 4:** The government requests respondents' views on UK:UK transfer pricing. Is it onerous and to what extent, and would providing a general exemption materially reduce the compliance burden? Do respondents have any views on the practical application of a general vs specific exception to the general exemption?

4.11 What is proposed in the consultation document seems a sensible change in principle, but deciding whether there is a tax advantage can be less than straightforward. For example, in the context of the loan relationships unallowable purpose test, what constitutes a tax advantage is a point subject to ongoing litigation.

4.12 In practice, many multinational enterprises (MNEs) have robust controls and pricing arrangements in place for all (or at least common and/or material) transactions between their related parties, and (in particular) to the extent that the character of a UK-UK transaction is similar to those found between international connected parties in the group, it may not be overly onerous to apply the same the standards to transactions between UK parties. Further, if it is not beyond doubt whether there will (or could, even theoretically in the future) be some advantage gained from not applying an arm's length price to a transaction, then the work would need to be done anyway to determine this (and it would be less burdensome to perform that analysis contemporaneously than when a return is enquired into). In some cases the advantage may not even occur until (for example) an adjustment or corresponding adjustment is required at a later date as a result of a dispute or assessment. Accordingly, we would expect many groups to find limited benefit from an exemption where there remains a proviso that it could not be applied where an advantage was gained.

4.13 UK-UK transfer pricing can be an issue for infrastructure project finance transactions, in that it introduces uncertainty, even when a disallowance in one entity does not occur. More recent rules, such as the corporate interest restriction rules, mean there is less danger to the UK Exchequer from UK-UK transfer pricing advantages. A general exemption would materially reduce the compliance burden, and the corporate interest restriction rules, plus the restriction on brought forward losses, would prevent companies from 'excessive' deductions in any one period. A specific exemption would necessitate more detailed legislation, and would not be a simplification.

4.14 **Question 5**: The government welcomes respondents' views on Commissioners' Sanctions. Do they provide assurance and are they valued by taxpayers?

4.15 We do not have any particular comments on Commissioners' Sanctions.

4.16 **Question 6:** The government welcomes the views of respondents on the repeal of ss. 152 to 154 and 191 to 194 TIOPA 10 and their replacement by a more directly drafted rule. Specifically, what practical issues does the current legislation present, and what benefits should be retained? Are there any alternative options which respondents see which would achieve the aims as stated above?

4.17 We strongly support a change to the UK rules to align with international standards and to allow the consideration of implicit support and guarantees in determining the amount and terms of debt available at arm's length. There is currently a contradiction in the UK legislation, which, on the one hand says the rules should be interpreted consistently with the OECD Model and, on the other hand prohibits consideration of implicit support and guarantees. We understand that commercially lenders and credit agencies do take into account guarantees and other forms of implicit support; so the current position under UK legislation is inconsistent with the arm's length principle, as well as with the new Chapter X in the OECD's Transfer Pricing Guidelines.

4.18 Consideration should be given to transitional rules to support a significant change to the rules such as this, as debt put into place under the current regime may be of (for example) a five or ten year duration.

4.19 **Question 7**: The government welcomes views on the clarity or otherwise of the resultant impact on the application of other rules. Are there any specific interactions which cause difficulties? **Question 8**: The government welcomes respondents' views on the current formulation of the rules at Part 8 CTA 09 which govern the taxation of intangibles transactions between related parties and the proposal to simplify ss. 846 and 849 CTA 09. **Question 9**: Would a move towards a single valuation standard in cases where transfer pricing otherwise applies reduce compliance burdens? **Question 10**: Do respondents foresee any problems having different valuation standards for those subject to transfer pricing and those not subject to transfer pricing (such as many SMEs); or for different transactions – such as, capital transactions (which are subject to MV rules) and transactions in intangibles? **Question 11**: The government also welcomes respondents' views on whether other UK tax rules which impose an obligation to undertake multiple separate valuation standards are burdensome in practice. **Question 12**: The government welcomes views from respondents on whether there are any concerns in relation to these rules – whether they are understood, whether they adequately achieve their desired function, and whether any practical difficulties in application exist. **Question 13**: The government welcomes views on the tax treatment of adjustments to foreign exchange movement gains and losses which arise following the application of Part 4.

4.20 We do not have any specific comments on questions 7 to 13, but would reiterate our view that it is helpful, so far as possible, for the UK's rules on transfer pricing to align with international standards. Any deviation by a jurisdiction from the international standards increases the compliance burden for businesses and the administrative burden for tax authorities.

5 Permanent Establishments

5.1 **Question 14**: The government welcomes general observations from respondents regarding the perceived advantages and disadvantages of each option for amending the PE definition. **Question 15**: Do respondents foresee any issues with the UK limiting this definition to fixed place of business and dependent agent PEs? **Question 16**: Do respondents foresee any specific issues with the UK changing its domestic law position in terms of the definition of a dependent agent PE? Do respondents foresee any specific issues with the UK changing its domestic law position in terms of the definition of an independent agent?

5.2 We do not have a preference for either option a or option b as described in the consultation document in terms of how to legislate for potential amendments to the permanent establishment (PE) definition. In either

case the consultation document is not clear whether the options would retain the requirement to be 'trading' in the UK as a first step for there to be a UK PE, or whether there would be a change to the OECD Model standard wording of 'fixed place of business through which the business is wholly or partly carried on.' This should be clarified. However, the key question is how and whether to amend the underlying definition itself, in particular the extent to which the 2017 changes to Article 5 of the OECD Model should be reflected in the UK's domestic legislation.

5.3 In some respects, aligning the UK domestic PE definition with Article 5 in the 2017 OECD Model would be a simplification, for both taxpayers and tax administrators. Generally, we support the principle of aligning with the OECD Model, because if each country does things differently to the agreed international guidelines, it complicates compliance for taxpayers and reduces the benefit of having reached a global consensus as to what the rules should be. That said, it is notable that these changes to the OECD Model did not achieve full international consensus and were agreed as optional outcomes of the base erosion and profit shifting (BEPS) project. As noted in the consultation document the UK, alongside many other OECD Member countries chose not to adopt the changes into its double tax treaties through the multilateral instrument.

5.4 HMRC have previously sought views on the potential impact of the changes to Article 5. Our view remains the same as when we responded to an informal consultation on this by HMRC in September 2022[2]. We noted that the provisions in Article 5 and, in particular, the new 'preparatory or auxiliary' activities listed have not had much time to bed in. Therefore, it is premature to conclude that they are not giving rise to the problems foreseen. In our view the concerns expressed by businesses in 2016 (that the changes would cause less certainty and, potentially, lead to a proliferation of PEs) remain valid. We also noted that it is important to put these rules into context. The rules set out in the OECD Model apply to all business, and not just the largest multinationals for whom the new rules were designed.

5.5 The outcome of amending the definition of PE within UK law to reflect the Article 5 changes depends on whether there are jurisdictions who are, or are likely to, take an expansive view of the effect of the Article 5 changes (particularly the change to Article 5(5)) to assert UK companies have PEs in their jurisdiction. Such an approach would cause compliance issues (potentially for very little additional tax) for those businesses and a potential increase in disputes having to be addressed through MAP.

5.6 This implication for outbound PEs is relevant in the context of considering changes to UK domestic rules, because the UK may be weakening its treaty negotiation position if it accepts the expanded definition of PE into UK law. This is discussed in response to Question 17 below.

5.7 In addition, we remain of the view that the terms within the new Article 5 are less clear than the current definition. Thus an extension would widen scope for potential disagreement. The new rules would require guidance from HMRC to explain the new rules and also clarify the extent to which the OECD Commentary will be used to interpret any UK domestic law implementing Article 5. This is particularly true of the wording 'habitually plays the principal role', because of the uncertainty about roles of different employees (who may be spread across the globe) in relation to some transactions, in particular in relation to lending transactions.

5.8 Similar issues would arise if the UK were to adopt the narrowing of the independent agent exception. HMRC could consider providing more guidance on the meaning of broker, along the lines of the investor management exemption (IME) in order to balance the position and achieve greater certainty.

5.9 Taking the impact on the treaty negotiation position and the inherent uncertainty within the extended definition into account, it is less clear that there are benefits from incorporating the new Article 5(5) and (6) into the UK's domestic law. Given that HMRC have other tools to counter pre-BEPS structures that were a

[2] 220905 Review of treaty policy positions - CIOT response.pdf

concern, it is not clear that extending the definition of PE would raise revenue, and may simply result in a proliferation of filing obligations (with associated compliance costs) without much extra tax.

5.10 In any event, consideration should be given to ensuring that the same PE concept is also applied to Income Tax in section 6 of Income Tax (Trading and Other Income) Act and for Capital Gains Tax in section 1B of Taxation of Chargeable Gains Act 1992.

5.11 **Question 17**: Do respondents foresee any issue with the UK potentially changing its negotiating position, so that UK tax treaties might include these provisions?

5.12 We recognise that flexibility when negotiating treaties is important and that, generally, treaties are to be welcomed. It is probably not always the case that the PE rules will be the critical point for multinationals, including smaller ones, when considering a double tax treaty as a whole. It will depend on the treaty and what else is potentially on the table for negotiation. For example, we recognise it may be of value for HMRC to concede the PE point when negotiating a new treaty if it facilitates lower withholding tax rates on items like dividends, interest and royalties. Overall, whether it is a benefit to have a treaty, rather than no treaty as a result of holding firm on the changes to Article 5, depends on its finally agreed terms. The risk of undermining stability and predictability, in particular, the risk of creating a proliferation of very small PEs where the administrative burden and cost would outweigh the tax potentially at stake (the key concerns raised by businesses and other stakeholders in 2016) as a result of the new OECD provisions in Article 5, should therefore be weighed against the benefits that would be provided by the treaty in question.

5.13 As the UK currently has the narrower pre-BEPS definition of a PE in our domestic law, adopting the 2017 model version of Articles 5(5) and (6) in treaty negotiations is something that the UK can accept in suitable cases as part of its negotiations with a particular treaty partner. The UK is in a position to do this (on a case-by-case basis) without adopting the 2017 version as the UK's preferred approach in tax treaties. Importantly, however, as things currently stand, the UK can choose not to adopt the 2017 version in those cases where the other jurisdiction's tax authority is likely to take an aggressive line on the scope of the new Articles 5(5) and (6), which might expose UK businesses to modest PEs with consequential administrative burdens and potential disputes requiring resolution through the MAP. We are not clear as to why HMRC considers it difficult to defend its current position of not having implemented in domestic law this element of the BEPS proposals in treaty negotiations. If treaty partners are using it to justify not adopting other BEPS measures that the UK wishes to see in a double tax treaty with them, adopting the new Articles 5(5) and (6) is something that can be accepted by the UK as part of the negotiations for the treaty with that jurisdiction. Having a blanket policy of adopting the 2017 model version of Articles 5(5) and (6) (which would seem to automatically follow from implementing the changes into our domestic law definition of a PE) appears to us to deprive the UK of adopting a negotiating position in suitable cases. What may be in the best interests of UK businesses may depend on the identity of the treaty partner and the level and nature of UK business activity in that treaty partner's jurisdiction.

5.14 **Question 18**: Do respondents foresee any issues with the UK aligning the domestic legislation on PE attribution either directly with the relevant double taxation treaty or with Article 7 of the OECD Model supported by the Commentary and the OECD Report on the Attribution of Profits to PEs?

5.15 Generally, we support the principle of aligning UK domestic rules with the OECD Model. However, there are jurisdictions who have treaties with the UK that pre-date the Authorised OECD Approach (AOA) to profit attribution, and which may be reluctant to adopt the AOA. Accordingly, the pre-AOA commentary on Article 7 will remain relevant in relation to these jurisdictions. This may result in some issues because of the pre-AOA's different approach to allocating profit to the PE jurisdiction. Accordingly, there is inevitably a degree to which HMRC, and some businesses, will have to operate two sets of rules for attributing profit to the UK;

adopting the current OECD model version of Article 7 (or the applicable treaty provision) in domestic law will not necessarily eliminate this duplication.

5.16 **Question 19**: Would removing any particular aspects of the legislation in Chapter 4 CTA 09 be problematic? **Question 20**: The government welcomes respondents' views about possible unforeseen and/or unhelpful consequences or interactions with other parts of UK tax legislation which are not addressed in the above proposals. **Question 21**: The government also welcomes any specific additions, exceptions or exemptions which respondents deem helpful to identify or add in at this stage. **Question 22**: The government welcomes comments from respondents on the potential impact of the reforms contemplated in this consultation on the UK asset management sector. **Question 23**: Do respondents foresee any issues with the removal of specific independence criteria for Lloyd's agents (currently at section 1151 CTA 10)?

5.17 We do not have any specific comments on questions 19 to 23.

6 Diverted Profits Tax

6.1 **Question 24**: The government welcomes respondents' views as to whether this closer alignment of a diverted profits charge assessment to the CT enquiry framework would be a welcome simplification.

6.2 We agree that a closer alignment of a diverted profits charge assessment to the Corporate Tax (CT) enquiry framework would be a welcome simplification.

6.3 **Question 25**: The government invites respondents' views on bringing Diverted Profits Tax into the CT framework as a standalone CT charge at a higher rate in respect of arrangements designed to inflate expenses, reduce income, or avoid a UK PE.

6.4 Bringing Diverted Profits Tax into CT would be beneficial, in particular bringing it within the scope of double tax treaties, including access to MAP for resolving disputes. We recognise that the government considers the core features of Diverted Profits Tax, such as its higher rate, are what makes the tax an effective tool to counter behaviours aimed at diverting profits from the UK and avoiding paying tax on profits that have been generated from activities in the UK. However, aligning the Diverted Profits Tax with CT so far as possible would be a simplification and provide clarity around points noted in the consultation document: that profits are only charged to tax once, subject to one tax geared penalty and that amendments to a CT return will reduce the amounts subject to a diverted profits charge.

6.5 However, we are compelled to note that a key feature of Diverted Profits Tax was that taxpayers could not rely on treaties to avoid it (that is to say that in cases where it was the application of a treaty that created a concern which could not be mitigated through changes to the domestic CT rules). While it is welcome that the UK's concerns in this regard have been mitigated by international changes such as the Multilateral Instrument (MLI) and updates to the OECD Transfer Pricing Guidelines, as well as behavioural changes in MNEs, if there are scenarios where the structures targeted by Diverted Profits Tax would still be frustrated by application of a bilateral tax treaty that has not been appropriately amended, it should be borne in mind that moving the provisions within the CT regime would expose the UK to these risks.

6.6 **Question 26**: The government welcomes respondents' views as to whether it would simplify the legislation not to directly replace s. 86 and instead use a diverted profits assessments on UK entities to challenge arrangements which would currently fall under s. 86 and any other comments any other comments in respect of s. 86 and avoided PEs.

6.7 Changes to the international tax framework since the introduction of Diverted Profits Tax (including the outcome of the BEPS project and updates to the OECD Transfer Pricing Guidelines) mean that the profit

diversion and structures that Diverted Profits Tax was introduced to tackle now largely fall within scope of the PE and transfer pricing rules. We understand that HMRC's approach is to seek to reach transfer pricing based outcomes when considering diverted profits, meaning that s. 86 is less utilised.

6.8 As noted in the consultation document, the arrangements targeted by s.86 can be challenged in line with Article 9 of the OECD Model. We would welcome an approach to this reform that simplifies the UK's legislation so far as possible and avoids duplication. The revised international tax framework should be reflected in the framing of the new rules within the CT framework, with the charging provisions for the higher rate charge for targeted diverted profits aligning with the PE and transfer pricing rules. A single set of rules within the UK's legislation to deal with non-arm's length would be a valuable simplification.

6.9 **Question 27**: The government welcomes the views of respondents as to whether amending the definition of reduction in income in s. 107(3) FA 15 and changing the definition of 'qualifying loss relief' would bring clarity and would welcome any other comments in respect of the functioning of the ETMO. **Question 28**: The government welcomes respondents' views as to whether amending the provisions for the calculation of the taxable diverted profits would bring clarity on the application of the legislation to loss-making companies. **Question 29**: The government welcomes respondents' views on options to clarify the scope of the IESC and amending the legislative definition of the tax reduction, to improve the functioning of the IESC. **Question 30**: The government welcomes respondents' other comments how to modify the IESC to improve its functioning, and the areas that cause the most complexity.

6.10 Generally, it would be helpful for the charging concepts within UK tax law to align so far as possible with the international rules and OECD Model. The departures from the arm's length principle in the economic substance area have the potential to cause disputes.

6.11 **Question 31**: The government welcomes respondents' views on this change to the circumstances in which an amending notice can be issued and the scenarios where they consider such a policy should apply.

6.12 The proposed change would be welcome.

6.13 **Question 32**: The government welcomes respondents' views on amending the definition of the material provision to ensure that it identifies the arrangements actually entered into by the relevant parties and any other comments in respect of the material provision. **Question 33**: The government welcomes respondents' views on amending the definition of the RAP to the arm's length provision and would welcome any other comments in respect of the RAP. **Question 34**: The government welcomes respondents' views on whether the legislation currently at s. 85 would be sufficient to enable calculation of diverted profits charges in all cases if the RAP is updated as described. **Question 35**: The government welcomes respondents' views on whether (if the actual provision condition is retained) updating the inflated expense condition would improve the operation of the diverted profits regime and would welcome any other comments in respect of the inflated expense condition.

6.14 We do not have any specific comments on questions 32 to 35.

7 Acknowledgement of submission

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

The Chartered Institute of Taxation
10 August 2023