Bird & Bird

Profit Diversion Compliance Facility ("the PDCF")

On 10 January 2019, HMRC announced a new voluntary disclosure facility that gives companies an opportunity to disclose and correct any tax inaccuracies relating to profits diverted out of the UK. The PDCF is being framed as the last chance for businesses with cross border arrangements to correct their tax affairs or face higher penalties in the future.

Introduction

Despite the Diverted Profits Tax being introduced in 2015, HMRC believe many multinational companies are still avoiding paying the correct amount of tax in the UK by using transfer pricing policies to divert their UK profits.

HMRC recognise that these mistakes or inaccuracies can be due to policies being out of line with the OECD guidelines or a result of businesses changing and transfer pricing policies not being updated. However HMRC also believe that some mistakes may be deliberate. In many cases, businesses may not be aware that a problem may exist.

The PDCF encourages companies to review their current cross border arrangements and provides them with the opportunity to bring their UK tax affairs up to date by making a disclosure and paying any tax liabilities and penalties where errors are identified.

Businesses that fail to register for the facility and are subsequently found to be non-compliant with their UK tax responsibilities will face higher penalties, a possible criminal investigation and may be named and shamed if the behaviour is seen to be deliberate.

Who is the PDCF aimed at?

The PDCF is aimed at multinational groups with subsidiaries located in low or no tax jurisdictions. In particular, HMRC are targeting technology and e-commerce companies which generate a significant profit from intellectual property assets that are based overseas.

It is understood that HMRC have already compiled a list of companies they believe to be at risk of diverting profits and plan to contact each of the companies to encourage them to consider their position in light of the PDCF.

How does the PDCF work?

Companies have until 31 December 2019 to register for the PDCF. A company registers its intention to make a disclosure by completing a specific registration form which is submitted to HMRC. Once registered, the company then has six months from the date of registration to submit a full disclosure report.

HMRC's guidance contains a detailed description of what the disclosure report should contain and how it should be set out. The key sections to the report are:

Relevant facts and evidence - the report should provide a detailed description of all the relevant facts and should refer to the evidence from which they are derived.

Application of tax law to the facts - a detailed analysis should be provided on how tax law has been applied to the facts and the conclusions that have been reached.

Behaviours and conclusions on penalties - a detailed analysis should be provided on the behaviours investigated and the conclusions reached on the application of penalty provisions.

Proposal - the report should set out the proposal the company is making to settle its outstanding tax liabilities, plus any penalties and interest.

Declaration - the report must contain a completed declaration signed by a senior responsible officer.

Supporting documents - an annex listing all the evidence that supports the facts referred to in the report should be provided together with the relevant documents.

The report must be full and accurate and all endeavours must be made to determine the correct amount of tax due. All liabilities (including interest and penalties) must be paid at the time the report is submitted.

It is also important to note that there is no amnesty element to the PDCF. Therefore, HMRC could in theory still decide to commence a criminal investigation after the report is received. However, in their guidance, HMRC state they are highly unlikely to start a criminal investigation for a tax-related offence if a company makes a full and accurate disclosure.

Companies that register for the PDCF may meet with HMRC before they submit their report at a pre-submission meeting. This will give the company the opportunity to present its draft report and explain the conclusions. HMRC can then point out any immediate concerns for the company to consider so that amendments can be made prior to submission.

Once submitted, the report will be considered by a team of international tax specialists. If HMRC believe a report does not include a full and accurate disclosure or an explanation has not been provided for the inaccuracies or failure to notify for Diverted Profits Tax, they will want to understand why. This will involve a review which could lead to a more fundamental investigation if HMRC consider it necessary. If HMRC believes it has been deliberately misled, a criminal or civil investigation into suspected tax fraud may be commenced.

What are the advantages of using the PDCF?

- HMRC will not start an investigation into any company registered for the PDCF before its disclosure is submitted;
- The disclosure will be treated as unprompted and the company will therefore receive lower penalties;
- If a deliberate inaccuracy is disclosed, HMRC will not publish details of any corporate entities involved;
- The PDCF enables companies to bring their tax affairs up to date in an open and efficient way;
- It is an accelerated process - HMRC aim to respond to submitted reports within three months; and
- Although the PDCF does not provide automatic immunity from criminal investigation, HMRC have made it clear that they are unlikely to start a criminal investigation if a full and accurate disclosure is submitted.

Why Bird & Bird?

Bird & Bird is considered to be one of the world's leading law firms in technology and intellectual property. Given HMRC's focus on targeting businesses in the technology and e-commerce sectors, we are well placed to provide bespoke advice in this area.

As there is no amnesty with the PDCF, there is a risk of further, more serious investigations being conducted by HMRC following the submission of the disclosure if it is deemed to be deficient. Therefore, businesses should seek external legal advice in order to:

- Conduct an initial triage exercise to assess whether there may be potential for unexpected DPT liabilities or other errors giving rise to a disclosure being required;
- Conduct a detailed review of the company's cross border tax arrangements;
- Gather facts and evidence in support of transfer pricing agreements;
- Conduct any investigations, under legal privilege, into behaviours that gave rise to a tax error; and
- Prepare and submit, if necessary, a disclosure to HMRC.

We are a specialist tax disputes and investigations team with a wealth of experience leading complex and factual tax projects and supporting clients through HMRC disclosure facilities. We have previously assisted clients making disclosures under all of the major HMRC disclosure facilities including the Liechtenstein disclosure facility, the Crown dependency disclosure facility and the contractual disclosure facility.

We also have a specialist transfer pricing team that work with innovative technology to provide technical support on complex issues. Through our network, covering more than 20 countries worldwide, we can provide expertise on tax, legal, valuation and accounting implications associated with multi-jurisdictional projects.

Who to contact?

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