

Draft Legislation on the UK Transfer Pricing Documentation Requirements

What Are the Key Takeaways and Next Steps?

As part of the Organisation for Economic Cooperation and Development's (OECD) Base Erosion and Profit Shifting (BEPS) Action Plan 13, a three-tiered approach for transfer pricing documentation was developed which consists of a Master File, Local File and a Country-by-Country Report (CbCR). The UK has already implemented the Country-by-Country reporting requirement without the requirement for taxpayers to prepare transfer pricing documentation in a specified format (such as Master File or Local File), as requirements for transfer pricing record-keeping were already in place.

In March 2021, Her Majesty's Revenue and Customs (HMRC) held a public consultation on introducing more specific transfer pricing documentation requirements in the UK. Following the consultation, in November 2021, the UK Government published its intention to introduce a requirement for the largest multinational enterprises (MNEs) with a presence in the UK to maintain (and provide upon request) a transfer pricing Master File and Local File in line with the OECD recommended approach. In addition, the UK Government announced its intention to introduce the Summary Audit Trail (SAT), which would document the work undertaken by the taxpayer in arriving at the conclusion in their transfer pricing documentation.

It was assumed that as UK taxpayers had already been required to keep sufficient records to demonstrate that intercompany transactions had been undertaken at arm's length, this change would only affect the format in which these records are kept.

On 20 July 2022, the Government published the draft legislation in relation to UK transfer pricing documentation requirements which is expected to take effect for accounting periods starting on or after 1 April 2023.

Key changes

The draft legislation provides for regulations to be introduced that would require taxpayers to produce transfer pricing documentation in a specified format in line with the OECD recommended approach.

The consultation document initially stated that the intention is for this legislation to only apply to the largest companies, although the term "largest" was not defined. As it currently reads, the draft legislation does not define a threshold and makes no other statement that would exclude any taxpayers (other than small and medium enterprises) from the requirement to prepare transfer

pricing documentation in the format of Master File and Local File. However, HMRC has confirmed in our recent discussion with them that the threshold will be introduced in the regulations accompanying the legislation, requiring only MNEs falling within the CbCR regime (i.e. companies with a consolidated group revenue of more than €750 million) to prepare standardised documentation as recommended by the OECD Guidelines.

There is also draft legislation allowing specified transfer pricing documents to be requested by HMRC outside of an enquiry. From discussions with HMRC, these will only be documents needed to undertake an informed risk assessment, and we are anticipating that regulations will limit what will be requested to documents such as the Master File and Local File. HMRC has advised that there will be a consultation on the final regulations before Christmas.

In addition, whereas taxpayers were previously required to provide records to HMRC that they had in their possession, this has now been broadened to include transfer pricing records that are in the possession of any other entity of an MNE group. For the purpose of this change, an MNE group refers to companies falling within the CbCR regime.

The draft legislation reinforces the importance of preparing robust transfer pricing documentation. This is further reflected in the changes to the penalties regime. Where there are any inaccuracies in documents submitted by taxpayers (e.g. tax returns) and the MNE group falls within the CbCR regime, HMRC will now presume that such inaccuracies are careless unless evidence can be presented that reasonable care was taken by the taxpayer to avoid an inaccuracy in the submitted document. This may therefore increase the level of penalties. Robust transfer pricing documentation prepared prior to the submission of a tax return may therefore serve as a protection from this change.

Next steps

The standardised approach may give taxpayers more clarity in relation to the preparation of UK transfer pricing documentation. Most of the largest MNE businesses have already implemented the standardised OECD documentation format and therefore this legislation will have minimal impact on those entities.

Although the content of the SAT is not yet known, HMRC has confirmed that it will be in the form of a questionnaire that will document the work undertaken by the taxpayer in arriving at the conclusions in their transfer pricing documentation. HMRC has also confirmed that the SAT will not be submitted in an electronic format; hence it will not require taxpayers to introduce any new systems to produce this document. Taxpayers will need to keep the records used to fill in the questionnaire and present them to HMRC upon request.

It is expected that the draft regulations and the draft SAT will be published in late September or early October and will be open for consultation for a period of eight to ten weeks.

If you have any questions about the above or would like to discuss how these changes would affect your business, please do not hesitate to contact the authors listed below.

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