



UK transfer pricing documentation

Draft legislation released

In brief

On 23 March 2021 HMRC released a [public consultation document](#) setting out some proposed changes to UK transfer pricing documentation requirements and on 30 November 2021 published its [consultation outcome](#), summarising the representations it received, providing government comments and setting out a way forward, including further consultation on draft legislation and guidance in 2022.

The [first tranche of draft legislation](#) has now been published, on 20 July 2022, as part of the “L-day” release of the draft Finance Bill 2022-2023. This includes primary legislation to permit the issuance in the future of more detailed regulations to establish “specified relevant transfer pricing records” and the form and manner in which they need to be kept and preserved. Those regulations are expected to include confirmation of:

- the requirement to prepare and maintain OECD format Master File and Local File documents where the taxpayer group meets the CbCR consolidated revenue threshold of €750 million; and
- the requirement for a "Summary Audit Trail" (SAT), described in the materials accompanying the draft law as a questionnaire "detailing the main actions [the business has] taken in preparing the transfer pricing local file document".

The draft primary legislation confirms a start date of 1 April 2023 (accounting periods beginning on or after).

Whilst all of that is as expected, there are also some particularly noteworthy and significant changes to information powers and penalties for transfer pricing, including:

- a presumption of carelessness where a taxpayer fails to do the work necessary to maintain or to produce relevant records on request, with associated implications for penalties;
- the right for HMRC to request transfer pricing documents outside of a transfer pricing enquiry; and
- the removal of the requirement for documents to be in the "power and possession" of a UK entity when they are in the "power or possession" of another group entity.

In detail

“Relevant transfer pricing records” (specified or of a description specified)

In the draft legislation, records are defined to be “relevant transfer pricing records” if “the Commissioners for Her Majesty’s Revenue and Customs reasonably consider that the records may relate to the calculation of profits or losses in accordance with [UK transfer pricing law]”. This in itself is a new, targeted and broad definition which could extend far beyond the Master File / Local File / SAT suite of documents which has to date been the focus of the consultation process.

Regulations will then determine the “form or manner” for keeping specified records “by reference to things specified in the OECD Guidelines”. As the SAT is one departure from the OECD Guidelines, it remains to be seen whether other modifications will be made in the detailed rules.

Summary Audit Trail (SAT)

Whilst there is currently little detail on the SAT, its introduction is in line with the general trends we are seeing from HMRC in terms of how it expects taxpayers to demonstrate and confirm that they have appropriate tax processes, governance and documentation in place to ensure their returns are correct and complete. This can be seen in a number of obligations brought in over recent years, such as the Senior Accounting Officer, Corporate Criminal Offence and Uncertain Tax Treatment regimes, as well as the increased focus on governance and processes as part of an HMRC Business Risk Review. It is also in line with what is seen in HMRC enquiries, where HMRC has a strong focus on the need for documentation and evidence to support positions taken.

Penalties

The changes to the penalties for inaccuracies legislation make it clear that the failure to create and maintain complete transfer pricing documentation has penalty implications for taxpayers. There is a very high risk that companies not complying with the new requirements will be penalised unless they can clearly demonstrate that they have taken reasonable care. The amounts may be significant, and can have real outward cash implications, so the need to demonstrate compliance with the new documentation requirements is therefore of critical importance.

Information notices for transfer pricing documents

Proposed revisions to Schedule 36 of the Finance Act 2008 are intended to ensure that an information notice can specify transfer pricing information or documents, as well as the means by which, and the form in which, these are provided. Changes have also been made to ensure that the relevant transfer pricing documents can be requested outside an enquiry, the first time this will apply in the area of corporation tax (and bringing transfer pricing into line with VAT and employment taxes).

Power and possession

There was already a clear expectation on the part of HMRC in the 30 November 2021 outcome summary that a Master File can be provided, notwithstanding the questions of whether one is already prepared elsewhere in the group and if so, whether it is in the power or possession of the UK taxpayer. The Master File information is viewed by HMRC as a necessary element of the application of the arm's length principle, and its absence would suggest that “the entity may not have been able to establish that it has made a correct return”.

The draft legislation both formalises and extends this expectation by including a further amendment to the provisions in Schedule 36 of the Finance Act 2008, in relation to the concept of “power and possession”. The existing rule is that a taxpayer is not required to provide a document to HMRC that is not in the power and possession of the UK company. For information notices relating to transfer pricing, Finance Bill 2022-23 proposes to remove that exemption where the document is in the power and possession of another member of the multinational group.

If passed into law, this would represent a significant change. UK companies receiving a relevant information notice might find themselves in the position of being placed under a legal obligation (to provide a document to HMRC) that it is not within that company's ability to fulfil. There would also be potential implications in respect of HMRC's Exchange of Information powers, whereby HMRC is spontaneously exchanging information with other tax authorities, which means that there is the potential for these documents to be shared more widely.

Still to come

With the devil as always being in the detail, there is still some distance to go in terms of absolute clarity in the rules, adequate guidance on interpretation and compliance, and the process of enactment into UK law. Amongst other things, the detailed regulations and guidance will need to:

- set out the format and content of the SAT in its newly announced questionnaire form, with guidance on key points and the level of detail needed for completion to HMRC's satisfaction
- identify any other areas of divergence between the new UK "form and manner" for keeping records and the OECD's Action 13 templates
- address issues of materiality and administrative burden including confirmation of HMRC's previously stated position that UK-UK transactions will generally fall outside the scope of the new rules and the consideration of other OECD consistent measures such as limiting requirements to material transactions and allowing for a level of aggregation
- clarify the expected timing of preparation of the "relevant transfer pricing records" and confirm the 30 day deadline for provision following an HMRC request

The takeaway

The changes proposed in the draft legislation to a variety of tax administration aspects send the overwhelming message that HMRC expects taxpayers to comply with the new legislation / HMRC's tougher position in terms of the minimum standards it expects taxpayers to adhere to in relation to transfer pricing documentation, and that there will be consequences for those who do not.

It is key that businesses take the opportunity to make representations where appropriate, including in relation to the new points on the administration of the new documentation requirements, and in due course on the detailed regulations and guidance which are expected later in the year. In particular the additional SAT requirement will need clear guidance on expectations with regard to the "sufficiency" of process and the documentation of the audit trail itself to ensure this can be prepared in a pragmatic and cost effective manner, especially important given the new presumption of carelessness and its impact on the amount of any penalties.

Businesses should also continue to assess their transfer pricing reporting systems and processes, and their current approach to achieving appropriate levels of documentation and other (broadly defined) transfer pricing records and supporting evidence. All taxpayers that are required to apply transfer pricing are encouraged by HMRC to take the same approach to documentation, reflecting HMRC's view that the Master File and Local File approach represents best practice. In practical terms, the new rules set the standard for HMRC expectations for transfer pricing documentation for all UK businesses within the scope of transfer pricing, not just for those groups which meet the legal requirement threshold.

Further information

For further information, please get in touch with your usual PwC transfer pricing contact.

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