

EXPLANATORY MEMORANDUM TO

THE DOUBLE TAXATION DISPUTE RESOLUTION (EU) REGULATIONS 2020

2020 No. 51

1. Introduction

- 1.1 This explanatory memorandum has been prepared by Her Majesty's Revenue and Customs (HMRC) on behalf of Her Majesty's Treasury and is laid before the House of Commons by Command of Her Majesty.
- 1.2 This memorandum contains information for the Select Committee on Statutory Instruments.

2. Purpose of the instrument

- 2.1 These Regulations are for the implementation of Council Directive (EU) 2017/1852 of 10 October 2017 on tax dispute resolution mechanisms in the European Union ("the Directive"). The Regulations introduce new mechanisms to resolve tax disputes between the United Kingdom and other Member States of the European Union which arise from the interpretation and application of tax agreements and conventions between the United Kingdom and other Member States that provide for the elimination of double taxation on income and on capital (where applicable). The Regulations also set out the rights and obligations of taxpayers seeking to invoke these mechanisms.

3. Matters of special interest to Parliament

Matters of special interest to the Select Committee on Statutory Instruments

- 3.1 These Regulations will have retrospective effect in order to meet a requirement in Article 23 of the Directive. In particular the Regulations have effect in relation to any income earned, or capital gained, in respect of a tax period commencing on or after 1 January 2018 (see regulations 2 and 3). There is an express power to make provision having effect in relation to periods before the regulations come into force in section 128A(3) of the Taxation (International and Other Provisions) Act 2010 (c.8) ("the Act").
- 3.2 These Regulations make provision about things done, or to be done, in territories outside the United Kingdom pursuant to section 128A(3) of the Act to the extent necessary for the purposes of implementing the Directive (see, for example, regulation 10(3) and (4) which have the effect of terminating certain proceedings which may take place in whole or in part in territories outside of the United Kingdom). But, notwithstanding that power, these Regulations do not prevent dispute resolution mechanisms operated in accordance with the Directive in a territory outside of the United Kingdom. Although that was not stated in the draft for consultation (see section 10 of this explanatory memorandum regarding the consultation), it has been expressly provided for in regulation 10(9) to clarify the position following technical feedback during the consultation and to assist the Commission of the European Union and competent authorities of other Member States.

- 3.3 These Regulations modify the effect of primary legislation pursuant to the power in section 128A(3) of the Act. That modification is limited to the purposes of these Regulations. In particular, section 6 of the Act has effect in the context of the instrument as though it is subject to regulation 10 (see paragraph (8) of that regulation). That modification is to clarify that section 6 of the Act cannot be relied on to allow proceedings under double tax arrangements, or the European Union Arbitration Convention, to continue where regulation 10(3), and Article 16(5) of the Directive, require that they are terminated. It is noted that section 128A(5) of the Act only refers to amendments or repeals of primary legislation, and a distinction is drawn between an amendment and a modification in section 128A(3)(f) of the Act. For that reason it is not considered that section 128A(5) of the Act applies to these Regulations, with the effect that they are subject to the negative resolution procedure.
- 3.4 These Regulations come into force after the date specified by Article 22(1) of the Directive and that fact has been communicated to the Commission of the European Union. It is not expected that an affected taxpayer would suffer any, or any major, detriment as a result of the late transposition for the following reasons. The instrument has retrospective effect to the extent mentioned in section 3.1. Any complaint which could have been brought but for the late transposition can be brought on the coming into force of these Regulations. Such a complaint could have been brought under alternative arrangements mentioned in section 7.3.

Matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business (English Votes for English Laws)

- 3.5 As the instrument is subject to negative resolution procedure there are no matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business at this stage.

4. Extent and Territorial Application

- 4.1 The territorial extent of this instrument is the whole of the United Kingdom.
- 4.2 The territorial application of this instrument is the whole of the United Kingdom.

5. European Convention on Human Rights

- 5.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

6. Legislative Context

- 6.1 These Regulations are made under section 128A of the Act which was inserted by section 83 of the Finance Act 2019 (c.1).
- 6.2 As noted, these Regulations are for the implementation of the Directive. The United Kingdom fully participated in the shaping of the Directive.

7. Policy background

What is being done and why?

- 7.1 Double taxation occurs when two States tax the same income. For example, an individual who builds up a pension pot while resident in State A may then retire to State B and begin drawing their pension. State A may tax the pension income on the basis that the pension was earned in that state and State B may tax the pension income

in that state on the basis that the individual is a resident of State B when drawing the pension. The individual is then subject to double taxation on the same income. Double taxation can create serious obstacles for businesses and individuals operating across borders by creating excessive tax burdens leading to inefficiencies and an economic disincentive to trade, investment, employment and freedom of movement. A harmonised tax dispute resolution framework will help to alleviate the issue of double taxation.

- 7.2 These Regulations provide for extended tax dispute resolution mechanisms within the European Union, delivering greater legal certainty for taxpayers and Member States.
- 7.3 The convention on the elimination of double taxation in connection with the adjustment of profit of associated enterprises (90/436/EC), commonly referred to as the European Arbitration Convention, established a procedure to resolve tax disputes where double taxation occurs between associated enterprises of different Member States. Typically, the double taxation will arise when a tax audit by a Member State of an enterprise leads to an increase of that enterprise's taxable profits. While most bilateral tax agreements and conventions included a provision for a corresponding downward adjustment of profits of the associated enterprise concerned, they did not generally impose a mandatory and binding obligation on the Contracting States to eliminate the double taxation.
- 7.4 The European Arbitration Convention provided for the elimination of double taxation by agreement between the Member States including, if necessary, by reference to the opinion of an independent arbitration panel. Following a review in 2015, it was concluded that the tax dispute resolution mechanisms currently provided for in bilateral tax agreements and conventions between Member States could create situations where there was varying interpretation and application of the provisions of the European Arbitration Convention. As a result, this could obstruct the effective resolution of double taxation disputes in a timely manner. Consequently, the Directive was adopted to build on existing tax dispute resolution mechanisms within the European Union. Note, as the European Arbitration Convention is a free-standing international agreement between its signatories rather than a European Union instrument, the adoption of the Directive cannot amend the European Arbitration Convention. The Directive therefore operates as an additional mechanism, albeit a claim brought under the Directive has the effect of terminating proceedings brought under the European Arbitration Convention.
- 7.5 The scope of the European Arbitration Convention is limited to cases involving enterprises conducting cross-border business with connected parties. The Directive has a wider scope as it applies to the interpretation and application of tax agreements and conventions that provide for the elimination of double taxation. Businesses will not be restricted to only submitting complaints on a question in dispute which relates to transfer pricing or permanent establishment but may also, for example, submit complaints relating to withholding tax or company residence. In addition, individual taxpayers will be entitled to submit a complaint on a question in dispute regarding their personal tax affairs such as double taxation on pension income.
- 7.6 These Regulations also introduce, in relation to the United Kingdom, greater clarity for taxpayers regarding their obligations and an improved framework for Member States to resolve disputes. It provides taxpayers with limited appeal rights where the double taxation occurs regarding the admissibility of complaints and failures by the Member States involved to meet their obligations in a timely manner.

- 7.7 The measure includes streamlined processes for smaller undertakings, being any person (other than an individual) which is not a large undertaking for the purposes of Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, or part of a large group for the purposes of that Directive, and individuals in order to minimise the administrative burden on those taxpayers.
- 7.8 It is difficult to provide a precise estimate of the number of complaints which will be submitted under these Regulations. The action which can create double taxation may occur in the United Kingdom or in another Member State and the taxpayer submitting a complaint may be resident in the United Kingdom or resident in another Member State. However as a broad indicator, the number of new cases in relation to double taxation admitted by the United Kingdom in the 3 years to 31 December 2018 where the tax treaty partner was another Member State is as follows:

	2016	2017	2018
Individuals	27	149	154
Businesses – Transfer Pricing	36	73	64
Businesses – Other cases	20	33	8

- 7.9 These Regulations are expected to impact on a very small percentage (<1%) of the United Kingdom’s taxpaying population. HMRC expects taxpayers will continue to make use of other tax dispute resolution mechanisms already available in the United Kingdom, namely bilateral tax treaties and the European Arbitration Convention.

8. European Union (Withdrawal) Act/Withdrawal of the United Kingdom from the European Union

- 8.1 This instrument does not relate to withdrawal from the European Union.

9. Consolidation

- 9.1 No consolidation will occur as a result of this measure.

10. Consultation outcome

- 10.1 HMRC ran a public consultation from 1 July 2019 to 27 August 2019 seeking views on draft Regulations. One response was received from a representative body. In summary, the respondent sought to understand, among other things, why HMRC had elected to produce detailed regulations transposing the contents of the Directive into domestic law rather than produce shorter regulations which stated that the Directive ‘shall have effect’. HMRC noted that the Directive specifically required Member States to bring into force the laws, regulations and administrative provisions necessary to comply with the Directive. As no such laws, regulations and administrative procedures were in existence in the United Kingdom, and the Directive itself provides certain options for implementation, HMRC’s approach is necessary to demonstrate that the United Kingdom has effectively transposed the Directive. This is in line with the approach taken in other Member States.

10.2 The respondent also raised a small number of technical queries regarding how HMRC had transposed specific text in the Directive into this measure. The respondent also offered a number of wider observations and opinions about the operation of this measure. HMRC engaged directly with the respondent. Following the consultation exercise, HMRC made some minor technical amendments to the language in the draft Regulations for the purposes of clarification.

11. Guidance

11.1 The rights and obligations of taxpayers are clearly set out in this measure. HMRC's existing guidance (<https://www.gov.uk/hmrc-internal-manuals/international-manual/intm423000>) regarding tax dispute resolution mechanisms will be updated in 2020 to reflect the addition of this new mechanism.

12. Impact

12.1 There is no, or no significant, impact on business, charities or voluntary bodies.

12.2 There is no, or no significant, impact on the public sector.

12.3 A Tax Information and Impact Note covering this instrument will be published on the website at <https://www.gov.uk/government/collections/tax-information-and-impact-notes-tiins>.

12.4 This measure is not intended to generate revenues for the Exchequer. These Regulations are intended to facilitate the elimination of double taxation. The Regulations will affect a very small number of taxpayers.

13. Regulating small business

13.1 The legislation applies to activities that are undertaken by small businesses.

13.2 Small businesses (employing up to 50 people), as well as individuals and medium sized businesses, resident for tax purposes in the United Kingdom will be entitled to communicate with Her Majesty's Commissioners for Revenue and Customs (or their authorised representative) who will then be obliged to communicate with other relevant Member States on behalf of the small business.

13.3 The basis for the final decision on what action to take to assist small business is to alleviate the administrative burden connected with contacting two or more tax administrations of Member States concerned with regards to a complaint on a question in dispute.

14. Monitoring & review

14.1 In accordance with section 28(3) of the Small Business, Enterprise and Employment Act 2015, as this is a tax measure it is exempt from the duty to review regulatory provisions in secondary legislation. In addition, it is noted that Article 22 of the Directive requires the European Commission to complete an evaluation of the implementation of the Directive and to present a report to the Council of the European Union within 5 years of 30 June 2019.

15. Contact

- 15.1 Martin O'Rourke at HMRC Telephone: 03000 515912 or email: martin.o'rourke@hmrc.gov.uk can be contacted with any queries regarding the instrument.
- 15.2 Andrew Page, Deputy Director for Business Assets and International, Transfer Pricing, at HMRC can confirm that this Explanatory Memorandum meets the required standard.
- 15.3 The Rt Hon Jesse Norman MP, Financial Secretary to the Treasury can confirm that this Explanatory Memorandum meets the required standard.