PLC December 2004 www.practicallaw.com

UK-UK transfer pricing on loans

Is fiscal neutrality a myth?

Jonathan Kandel of **Clifford Chance LLP** and **Gareth Green** of **Transfer Pricing Solutions Ltd** review the impact of the recent changes to UK transfer pricing and thin capitalisation rules.

Illustration: Getty Images

The UK's ***transfer pricing*** (*see Glossary*) rules have recently been extended to cover domestic transactions to address concerns that the UK's transfer pricing legislation was incompatible with the UK's obligations under EC law and its ***double taxation treaties*** (*www.practicallaw.com/A39273*). In particular, the UK's ***thin capitalisation*** rules were thought to be susceptible to a successful challenge by the taxpayer on the basis of the non-discrimination articles of the EC Treaty and certain UK double tax treaties and therefore were repealed leaving the UK's transfer pricing rules as the principal mechanism through which the Inland Revenue will challenge thin capitalisation (*www.practicallaw.com/A39274*).

The UK transfer pricing rules apply to any type of transaction. This article focuses on loans, in particular, as this is one of the most common transactions between related parties that may fall foul of the rules.

TRANSFER PRICING REGIME

The broad requirement of the transfer pricing legislation in the UK and overseas jurisdictions is that arm's length terms are to be used for tax purposes in transactions between related parties. The principal objective of the legislation is to prevent inappropriate pricing from moving taxable profits out of the country in question, whether such pricing arises inadvertently (as is more common) or from deliberate manipulation to move profits to a company in a country with a lower effective tax rate, thereby reducing the combined tax liabilities of connected companies. In calculating the amount of profits that are liable to UK tax, the actual results of the transactions between connected parties are adjusted and conformed to the results that would have occurred had the parties been at arm's length.

Until 31 March 2004, the UK transfer pricing regime generally only applied to cross-border transactions involving a UK party. With effect from 1 April 2004, however, it has been extended to cover transactions between connected UK parties.

For the first time, therefore, multinationals will need to consider the UK transfer pricing implications of loans within the UK part of their group. Further, domestic UK groups with no overseas subsidiaries need to address the new and significant compliance burden in applying the legislation.

Extension of the regime

Recent decisions of the European Court of Justice (ECJ), in particular, *Lankhorst-Hohorst GmbH v Finanzamt Steinfurt,* created uncertainty about the application of transfer pricing and thin capitalisation rules within Europe (*(C-324/00), see also News brief "Non-discrimination: UK tax rules under pressure", www.practicallaw.com/A28108*). Following *Lankhorst*, where the application of the German thin capitalisation rules to a German subsidiary of a parent in another European country was held to be discriminatory, the UK government became concerned that its existing transfer pricing and thin capitalisation legislation was vulnerable. Both pieces of legislation contained an exemption that was based on whether the parties to a transaction were UK taxpayers, and thus the rules generally applied only to cross-border transactions. Arguably, this discriminated against EU businesses, which meant that EU "Freedoms" potentially overrode this legislation in respect of transactions between the UK and the EU.

Group litigation orders are working their way inexorably to the ECJ, to confirm the position for prior years. Given the significant potential for very large refunds of tax, it is expected that the UK government will endeavour to persuade the ECJ that there is a crucial distinction between the UK legislation and the German law considered in *Lankhorst*, but few observers expect success. Certainly, EU governments, in general, are having a very poor strike rate in defending the rash of anti-discrimination cases they have faced in the last few years.

It was therefore expected that the UK government would take steps to protect its tax base, removing the discrimination by extending the UK transfer pricing regime to domestic transactions between related parties. Consequently, the Finance Act 2004 has made the following changes to the UK tax legislation, with effect from 1 April 2004:

The transfer pricing rules, which are set out in Schedule 28AA of the Income and Corporation Taxes Act 1988 (ICTA), have lost their exemption for transactions between two UK taxpayers.

Rather than make similar adaptations to the thin capitalisation rules in section 209(2)(da) of ICTA, these have been repealed in their entirety. Schedule 28AA has been promoted from its former supporting role in relation to thin capitalisation and is now the main UK weapon against thin capitalisation.

Other than these changes, the basic operation of the UK transfer pricing rules is the same as before. However, these fundamental changes have necessitated a number of additions to Schedule 28AA. These fall into two broad categories:

- Schedule 28AA has been equipped with provisions tailored to dealing with thin capitalisation and other transfer pricing aspects of loans.

- The government has introduced a number of measures to mitigate the adverse effects on taxpayers that would otherwise arise from the extension of transfer pricing principles to domestic transactions. These measures include compensating adjustments, balancing adjustments, exemptions for small and medium sized enterprises (SMEs) and dormant companies, and a partial relaxation of penalties for two years (*see further below*).

These measures intend to ensure that no additional tax arises as a result of the new rules for most domestic transactions. However, there are a number of exceptions: in fact it should not be assumed that there will be fiscal neutrality on all domestic transactions. Even on the government's own figures in their regulatory impact review of the likely effect of the changes to the transfer pricing and thin capitalisation rules, the additional tax take over the first three years of the new regime is estimated to approach £100 million (*www.inlandrevenue.gov.uk/budget2004/transfer-pricing.pdf*).

Similarly, although the government has minimised the additional compliance burden, a certain level of compliance is necessary. UK groups would be unwise to assume they can simply ignore these new rules.

As part of the drive to mitigate the compliance burden, the Inland Revenue released 13 draft guidance notes in the months following the 2004 Budget on how the new legislation should be applied (*www.inlandrevenue.gov.uk/international/transfer-pricing.htm*).

What is a "related party"?

Generally, under the transfer pricing rules, Company A (ACo) is related to Company B (BCo) if ACo controls BCo, or BCo controls ACo, or ACo and BCo are under common control (by another company or other person/s). Broadly speaking, "control" of a company arises from voting power of more than 50%, although in some circumstances as little as 40% control can be sufficient. This means that many joint ventures are, if carried out through a corporate vehicle, subject to the rules.

The control need not be direct. For instance, if ACo owns BCo, which in turn owns CCo, then ACo and CCo are related (as are ACo and BCo and BCo and CCo).

The transfer pricing rules could apply to any control relationship where the controlled party is a company or a partnership, and the party that controls that first party is any legal person, for instance, a company, partnership, individual, local authority, charity or trust.

However, one of the draft Inland Revenue guidance notes does confirm that such persons are only caught if they are acting as an "enterprise". This should help to avoid some of the more nonsensical possible transfer pricing issues that might otherwise have arose, such as whether a company is paying an arm's length salary to an employee who is also the majority shareholder.

Arm's length basis for loans

In applying the rules to an intra-group domestic loan it is necessary to consider both the interest rate and the amount of the loan.

Interest rate. The interest rate must reflect the creditworthiness of the borrower. The appropriate rate will therefore vary from loan to loan, but as a general guide the likelihood of challenge is higher if the interest rate is below LIBOR or considerably higher than LIBOR. Interest free loans are ostensibly clearly non-arm's length, because lenders do not normally make loans to unrelated borrowers without charging interest. However, an interest free loan can, in some circumstances, be defended, for example if it can be shown that what is, in legal form, a debt is, in substance, "quasi-equity". That is, its economic role is closer to equity capital than debt.

Amount of loan. The issue here is thin capitalisation. The debt must be less than or equal to the amount that the borrower would have borrowed under arm's length conditions. Interest on debt in excess of this level will not be tax deductible. As with the arm's length interest rate, the arm's length borrowing level will depend on the borrower's creditworthiness. The more creditworthy you are, the more you can borrow. However, the Inland Revenue has long adopted the practice that it is also a question of how much the borrower would, on an arm's length basis, sensibly wish to borrow.

Unless a tax inspector considers that unusually low debt levels are typical of the borrower's business (such as, perhaps, cash-rich retailers), the likelihood of scrutiny will be lower if the borrower meets what are known as the Inland Revenue's thin capitalisation "rules of thumb", namely that the borrower's debt should be no higher than its equity (that is, gearing of no higher than 1:1) and/or its interest burden should be no more than a third of profits (that is, interest cover of at least 3). The "rules of thumb" are not a safe harbour, but those who fall within these thresholds are generally likely to be at a lower risk of challenge than those who exceed them.

Guaranteed loans

It is necessary to consider not only intragroup loans, but also external borrowing. The Inland Revenue has long applied thin capitalisation principles to UK subsidiaries of overseas multinationals even though the loan is from an independent lender such as a bank in circumstances where it considers the UK borrower could not have borrowed as much as it actually has borrowed, were it not for support from the overseas parent (or the rest of the group) in the form of a guarantee or back-to-back loan. This principle now potentially also applies where the guarantor is a UK company.

In practice, the Inland Revenue tends to work backwards. First, it considers if the borrower has borrowed (internally and externally) more than, in its view, what is an arm's length amount. Often, the thin capitalisation "rules of thumb" are the starting point (*see "Arm's length basis for loans" above*). If the company in its view has excessive debt and the lender is external, then the assumption is made that this must indicate there was a parental guarantee. If there was no formal guarantee provided to the lender by the parent (or other group companies), the Inland Revenue assumes that there must have been some other parental support.

This approach has, up until now, been based on the Inland Revenue's interpretation of general principles, but the new legislation contains specific wording that seems intended to give this approach statutory backing. This includes a definition of "guarantee" that encompasses any "relationship, arrangements, connection, or understanding (whether formal or informal)" that would have been likely to have given the lender "a reasonable expectation" that if the borrower defaulted on the loan the parent would step in (*paragraph 1A(7), Schedule 28AA, ICTA*). It is perhaps debatable whether it is legitimate for the government to incorporate this interpretation into legislation, but the Inland Revenue's position is clear.

In addition, it may be necessary to consider whether the guarantor should have charged a guarantee fee for the service of providing the guarantee. In practice, it is relatively unusual for there to be intragroup guarantee fees, but they are specifically referred to in the new legislation, so companies should perhaps give special consideration to whether they ought to introduce fees where guarantees are in place.

EXEMPTIONS

SMEs and dormant companies are exempt from the new rules.

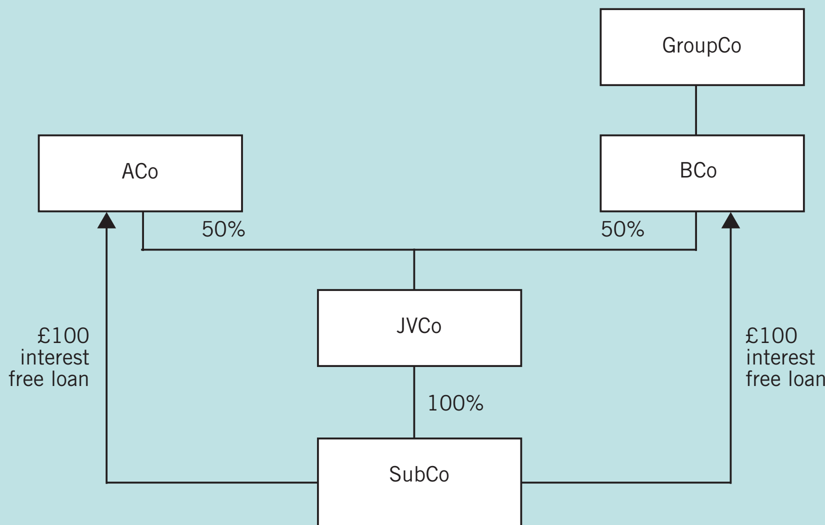
Small and medium sized enterprises

The definition of SMEs is based on EU provisions (*Annex to Commission Recommendation 2003/361/EC of 6 May 2003: www.inlandrevenue.gov.uk/pbr 2003/ct-reform.pdf*) and is broadly as follows: "Small enterprises" are enterprises with fewer than 50 employees and with either turnover or assets of less than €10 million (about £7 million). "Medium sized enterprises" are enterprises that are not small enterprises but which have fewer than 250 employees and either annual turnover of less than €50 million (about £35 million) or assets of less than €43 million (about £30 million).

In calculating the thresholds, members of a group and other related persons are aggregated. This means that no matter how small a company may be, it cannot benefit from the exemption unless its entire worldwide group meets the thresholds on a consolidated basis.

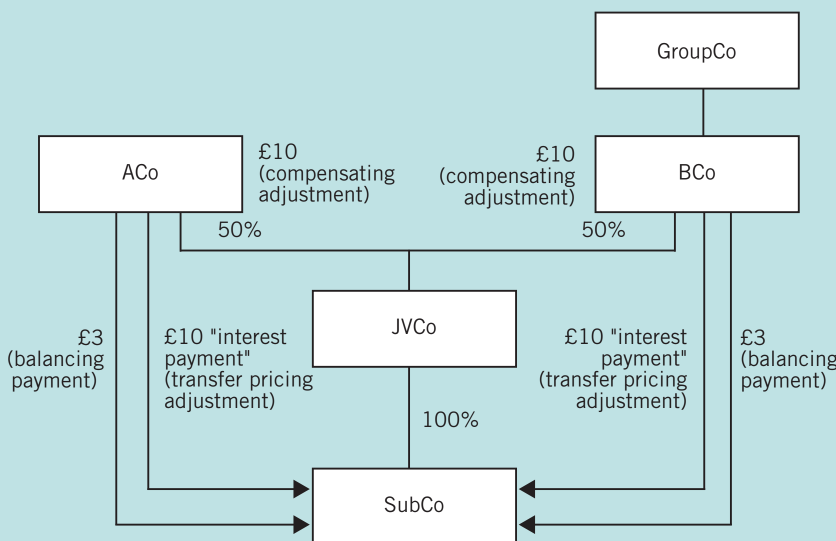
Small enterprises are, from 1 April 2004, exempt from the UK transfer pricing rules whether the transaction is domestic or cross border except where the counterparty to the transaction (or, where there is a series of interlinked transactions, any party to any of those transactions) is resident in a "non-qualifying territory". A "non qualifying territory" is a jurisdiction with which the UK either has no double tax treaty or has a double tax treaty that does not contain a non-discrimination article (*paragraph 5E, Schedule 28AA, ICTA*). Given the UK's extensive double tax treaty network, there are few large economies that are non-qualifying territories. The most significant non-qualifying territories are probably Brazil and Hong Kong.

Joint venture example: pre 1 April 2004



This is a hypothetical joint venture arrangement, where all entities are UK tax resident companies. Since SubCo (a wholly-owned subsidiary of JVCo) does not have "distributable reserves" from which to pay a dividend it lends cash up to ACo and BCo on a tax-free basis. Prior to 1 April 2004, there was an exemption from the transfer pricing legislation for transactions between UK taxpayers.

Joint venture example: post 1 April 2004



This example sets out the adjustments required by the new UK-UK transfer pricing rules assuming none of the exemptions apply.

* Step 1 involves SubCo adjusting its taxable income (by £20) to reflect the receipt of a market rate of interest (which for the purposes of this illustration is 10% per annum) on the interest free loan.

* Step 2 involves ACo and BCo claiming compensating adjustments of £10 each to reduce their taxable income.

* Step 3 involves a balancing payment by ACo and BCo of their saving of £3 each to SubCo to fund its increased tax bill of £6 (that is 30% of £20). The making and receipt of the balancing payment itself is a tax neutral event.

The exemption for medium-sized enterprises operates in the same way, except that the Inland Revenue has the power to withdraw the exemption from medium-sized enterprises where it considers there has been a transfer pricing misstatement involving significant amounts of tax. It would appear that this power has been reserved because of the concern that a few businesses might otherwise treat the exemption as giving them carte blanche to indulge in blatant transfer pricing manipulation to move virtually all their profits out of the UK. It remains to be seen whether this power is applied in practice with the restraint that is being signalled by the Inland Revenue.

The government's regulatory impact assessment suggests that as a result of these exemptions only 50-60,000 businesses will be subject to the new transfer pricing rules (*see "Extension of the regime" above*). It also suggests that the majority of intra-group transactions take place within the 800 groups handled by the Inland Revenue's Large Business Office.

Dormant companies

The exemption for dormant companies is intended to ensure that group companies that are dormant for the purposes of the Companies Act 1985 (1985 Act) are not deprived of this status by virtue of the transfer pricing rules, thereby suffering increased costs, for instance, from having to draw up accounts.

The typical situation at which the exemption is aimed is a group company that has ceased any activity and whose only asset is, for example, a loan to their parent company, on which no interest is charged. Unless the dormant company was in a group that was small enough to claim the SME exemption, the new rules would have required that the dormant company be treated as having charged an arm's length interest rate. The resulting tax liability would have meant the company would have an accounting transaction that had to be recorded in its books, so it would no longer meet the conditions to be dormant for the purposes of the 1985 Act.

This is welcome news for large groups, some of which include many hundreds of

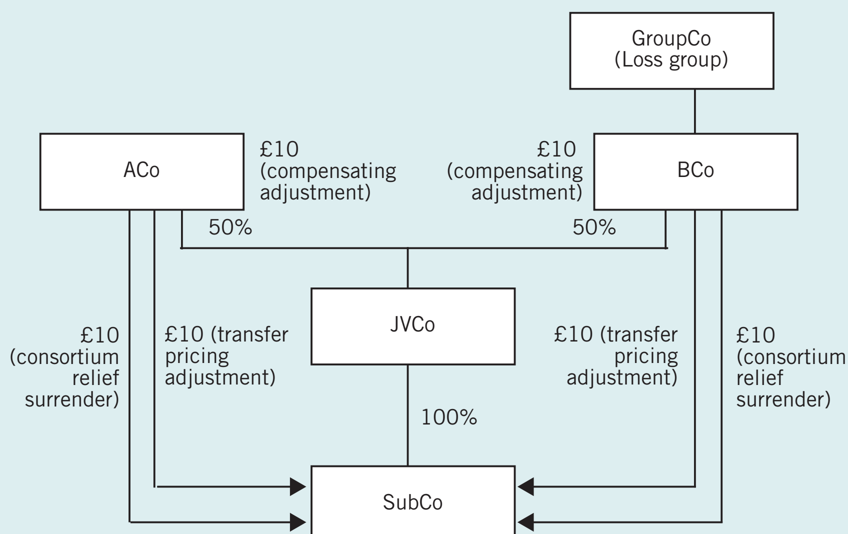
dormant companies. However, the exemption only applies to companies that have been dormant since 31 December 2003 (or 31 March 2003, if the dormant company's year end is 31 March). Companies that become/became dormant later than this are not entitled to the exemption, so it is likely to be less common for future corporate reorganisations to result in a batch of new dormant companies. Previously there may have been a reluctance to wind up inactive companies, but there will now often be a relatively high compliance cost associated with keeping such companies in existence when they are still parties to intragroup transactions.

FISCAL NEUTRALITY?

For most UK groups that have loans between UK companies, transfer pricing rules will therefore apply to those loans unless they are able to rely on the exemptions described above. The legislation does not examine both sides of the transaction at once. What is required is to determine whether any party to the loan would have had higher taxable profits if the loan had been on arm's length terms and conditions. If the answer is yes, then those profits must be increased accordingly, regardless of the position of the other parties to the transaction. For instance, if the interest rate is too low, the lender will be deemed to have received the arm's length amount of interest. If the interest rate is too high, or the amount of debt is too high, the borrower will be denied a deduction for the excessive interest.

It would be unfair to ignore the fact that the profits of the other party to the loan are higher than they would have been on an arm's length basis. In the case of cross border loans, this is taken into account by double tax treaties, which give "corresponding adjustments" in the other country. For instance, if a UK lender suffers a transfer pricing adjustment that increases its interest income, the overseas borrower can usually seek to reduce its taxable income to what it would have been had it paid an arm's length rate of interest. The result is that an amount of profit is treated as reallocated from one country to another, for tax purposes, and is not taxed twice.

Joint venture example: problem A



In practice the joint venture example becomes more complicated if we alter BCo's tax profile and assume that BCo in fact is not tax paying since it has current and carried forward losses. Consequently, it is not able to use the compensating adjustment of £10 to reduce its taxable income. It makes no tax saving and is not in a position to fund a balancing payment.

As a solution, BCo may be able to use the compensating adjustment by making it available for surrender by way of ***group relief*** (*see Glossary*) from GroupCo. In this example ACo and BCo form a consortium with JVCo and SubCo and each of ACo and BCo respectively may be able to make a surrender of £10 to SubCo by way of ***consortium relief***.

Since consortium relief is not available for surrender by BCo if the relevant amounts would otherwise be available for surrender by way of group relief by BCo, this solution will only work if it is assumed that BCo's "group" is loss making and could not claim by way of group relief the compensating adjustment. Timing issues may nevertheless arise with regard to the steps and SubCo will in all likelihood have to fund its tax before the surrender can be claimed from BCo.

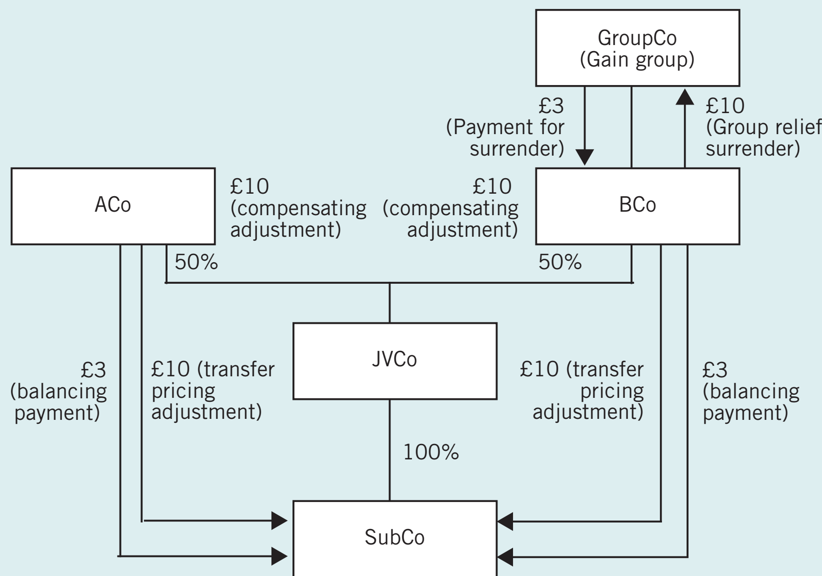
To ensure a similar relief from double taxation on domestic intra-group loans, the legislation includes the right to claim what is termed a "compensating adjustment": a reduction in the taxable profits of the other party to the transaction.

By way of illustration, ACo and BCo are related to one another for the purposes of the transfer pricing rules. Both pay 30% corporation tax. ACo grants BCo an interest free loan of £1,000. If we assume that the arm's length rate of interest would have been 10%, ACo will suffer a transfer pricing adjustment to treat it as if it had received interest of £100. Tax payable by ACo increases by £30. BCo claims a compensating adjustment, reducing its profits by £100, so its tax is reduced by £30. Overall, the combined UK tax they pay is unchanged.

In the case of loans, compensating adjustments may be available also for other UK group companies that are guarantors of the loan. The wide definition of guarantee (*see above*) will apply, so the effect will often be that all creditworthy members of the UK group are potentially guarantors, so can potentially claim a compensating adjustment. This will be helpful in cases where the actual borrower is thinly capitalised, but the UK group as a whole is not.

However, compensating adjustments will leave a mismatch. ACo has paid tax as if it received the interest, but BCo still has the £100 of interest. The legislation

Joint venture example: problem B



If, unlike in the box *"Joint venture example: problem A"*, BCo's "group" is not loss making and could have (even if it did not) claimed the compensating adjustment, the "loss" is not available for surrender to SubCo by way of ***consortium relief*** (*see Glossary*). This is the situation illustrated here.

In such circumstances, fiscal neutrality may only be achievable for SubCo if BCo is able to extract payment from GroupCo for its surrender of group relief that it could in turn use to fund a balancing payment to SubCo. Again, the timing of such steps may create a funding mismatch as SubCo will in all likelihood have to fund its tax before the relevant surrenders can be claimed.

therefore gives the right (but not the obligation) to make a tax free "balancing payment" equal to the compensating adjustment or any lower amount, if preferred. So, BCo could pay £100 to ACo, to put it in the same cash position as it would have been in had it received the interest in the first place. Alternatively, BCo could opt to make a balancing payment of £30, which at least provides ACo with the funds to pay the tax on the transfer pricing adjustment.

In many cases, this will mean that a transfer pricing adjustment on a UK-UK loan will have no net effect on the combined UK tax liability of the group. The extension of transfer pricing rules to cover UK-UK loans should therefore be fiscally neutral. However, this will not always be the case.

An obvious example would be where the parties have different tax rates. For instance, if one of the parties is a partnership, its tax rate is likely to be 40%. Another example may be in the context of UK joint ventures (*see boxes "Joint venture example: pre 1 April 2004"* and *"Joint venture example: post 1 April 2004"*) where the tax profile of one or more of the joint ventures (and their UK group) may restrict the ability of the joint venture to achieve fiscal neutrality (*see boxes "Joint venture example: problem A" and "Joint venture example: problem B"*).

COMPLYING WITH THE NEW RULES

Transfer pricing rules are included in the requirement to self assess, and taxpayers are potentially subject to penalties of up to 100% of any tax adjustment if they fail to comply.

A significant part of transfer pricing compliance arises from the requirement to produce evidence to demonstrate that a result is based on arm's length terms. Without adequate evidence, a company cannot be sure that it is delivering a correct and complete tax return and this can expose it to the risk of a penalty. There is, however, a two-year transitional period, during which no penalties can be imposed for failing to keep or preserve records which adequately demonstrate that any particular transaction satisfies the arm's length principle.

The Inland Revenue has suggested that where the tax at stake is low it does not expect businesses to undertake very detailed calculations in order to establish the correct price. An approach that "gives a broadly correct result" is acceptable. Although this reduces, it certainly does not eliminate, the compliance burden.

Despite the relaxation of penalties for the period up to April 2006, this is in practice less helpful than it first seems since it only applies to a failure to keep adequate documentation to evidence compliance with the arm's length principle. This may help businesses that currently do not apply the transfer pricing rules on any significant scale and which do not have the requisite accounting technology to calculate arm's length pricing on a detailed level; however, penalties may still be imposed for the negligent failure to undertake a proper transfer pricing analysis (that is, failure to apply the arm's length test). The relaxation only applies to the failure to record such an analysis.

The fact that a business may still need to defend the arm's length nature of transactions ultimately means that in practice the prudent approach is to have high quality, comprehensive documentation in respect of material related-party transactions, and so the effect of the relaxation is arguably negligible. In any case, critics are sceptical as to whether a failure to keep or preserve records in itself could, in fact, constitute negligence, meaning the apparent concession serves as little more than an optical device to appease taxpayers.

Compensating adjustments will often mean that any transfer pricing adjustment on a domestic loan is fiscally neu-

tral (*see "Fiscal neutrality?" above*). Taxpayers will therefore protest that applying transfer pricing rules is a waste of time. In cases where there is no net UK tax at stake, the Inland Revenue is likely to have a similar attitude. Why would a tax inspector want to waste time chasing a transfer pricing adjustment, only to give a compensating adjustment which negates its tax effect? It seems safe to assume that the Inland Revenue would far rather be applying transfer pricing rules to cross-border transactions, where there is "real" UK tax at stake.

The issue for the UK government is that it was discriminatory legislation that triggered the new rules and they cannot be seen therefore to replace it with administrative discrimination. The Inland Revenue's proposed solution to this dilemma appears to lie in the draft guidance notes on "Risk Assessment" (*see "Extension of the regime" above*). This guidance states that the Inland Revenue will aim to focus its attention on situations where there is a large amount of tax at stake. They argue that there is a low risk of a UK taxpayer having a large understatement of its profits due to incorrect transfer pricing on a particular transaction if the counterparty has a similar or higher marginal tax rate.

This should mean that the Inland Revenue will devote little attention to most transactions between UK companies, as they will both have a 30% marginal tax rate. Where there is a differential in the tax rate, however, it would follow that there will be a higher level of scrutiny. This would seem to suggest that UK groups should focus their compliance efforts for UK-UK transactions on non-fiscally neutral situations (such as the one described in the *box "Joint venture example: post 1 April 2004"*).

However, if the guidance note is to be believed, the same principle will apply to cross border transactions, provided the marginal tax rate of the overseas party is not lower than that of the UK party. This is presumably intended to deflect accusations of discrimination, but it is difficult to believe this is how the policy will be implemented in practice. After all, most of the UK's major sources of inbound investment and destinations of outbound investment have higher corporate tax rates than the UK: for example, the US (40%), France (34%), Germany (38%), Japan (42%), China (33%). These countries have come in for a large share of transfer pricing scrutiny from the Inland Revenue in the past, and it would be an astonishing turnabout if the Inland Revenue really does intend to focus predominantly on large transactions with related parties in

Glossary

Consortium relief. Companies which do not qualify for ***group relief*** may qualify for consortium relief. Where a company is owned by a consortium company, group relief can be surrendered from the consortium to companies in the same group as the consortium members and from such group companies to the consortium company (*sections 402–413, Income and Corporation Taxes Act 1988*) (ICTA) subject to various anti-avoidance provisions.

Double taxation treaty. Also known as a double taxation agreement. An agreement between two countries under which the taxation authorities of each grant tax concessions or reliefs to prevent taxpayers being liable for tax on the same amount under both systems and to lower the withholding tax payable in one country on dividends, interest and royalties paid to a person in the other country. These treaties are incorporated into UK domestic laws by statutory instruments made under section 788 of ICTA.

Group relief. Trading losses or other amounts eligible for relief from corporation tax incurred by a company (the surrendering company) may be surrendered to another company within its group (the claimant company) for the claimant company to set off against its own profits for corporation tax purposes. The companies are within the same group where one is the 75% subsidiary of the other or both are 75% subsidiaries of a third company and certain other conditions are met. The group relationship may be established by reference to non-UK resident companies.

Thin capitalisation. In the UK (and in many other jurisdictions throughout the world) the tax regime differentiates between dividends and interest. Dividends are not tax deductible in computing the taxable income of a company whereas interest is. This potentially influences the decision as to whether a subsidiary should be provided with equity capital or debt (and the relative proportions of debt and equity). Within multinational groups, in particular, there may be a limited commercial distinction between financing a company with debt or equity. If it is intended to reduce the tax liability of that company the tendency is for the company to be financed almost entirely with debt. A company that has a very low equity capital as compared to the amount of debt it owes is described as thinly capitalised.

Many tax regimes have rules to ensure that companies have a fair proportion of equity capital so that taxable profits cannot be minimised in this way. These may apply where the company has an inadequate debt:equity ratio or interest coverage.

Transfer pricing. Prices at which associated entities transfer goods, services and carry out other transactions (such as loans) between each other, for example, between group companies. In the absence of preventative legislation, connected companies would be able to manipulate transfer prices to create tax advantages by, for example, setting them at a level which would enable them to move profits to a lower tax jurisdiction. Anti-avoidance legislation in many jurisdictions permits the tax authorities to adjust the amount of income earned or expense accrued on transactions between affiliates, including intra-group debt and related interest, where it appears that the transaction was not at arm's length.

Related information

Links from www.practicallaw.com and the web

These links can be found from this article which is at www.practicallaw.com/A45781

Topic

Corporation tax www.practicallaw.com/T826

Practice notes

Banking: tax	www.practicallaw.com/A14685
International business: tax	www.practicallaw.com/A14715
Asset purchases: tax	www.practicallaw.com/A14654
Group reorganisations: tax	www.practicallaw.com/A14671
Tax clearances and related legislation	www.practicallaw.com/A14612

Previous article

Non-discrimination:
UK tax rules under pressure (2003) www.practicallaw.com/A28108

Weblinks

Inland Revenue www.inlandrevenue.gov.uk
The Inland Revenue's 13 draft guidance notes are available at www.inlandrevenue.gov.uk/international/transfer-pricing.htm.

For subscription enquiries to PLC web materials please call +44 207 202 1200

countries with low effective corporate tax rates, such as Ireland, the Netherlands and Switzerland.

Although low tax rates may indeed heighten the risk of enquiry, it seems probable that the Inland Revenue will continue to target any substantial cross border transactions, because it knows from experience that transfer pricing misstatement arises primarily from taxpayers' neglect, rather than deliberate manipulation, so it is as likely to occur in a transaction with, say, the US as with Australia (which has the same 30% corporate tax rate as the UK).

Jonathan Kandel is a tax lawyer in the international tax group of Clifford Chance LLP specialising in UK and international transfer pricing. Gareth Green is the director of transfer pricing boutique, Transfer Pricing Solutions Ltd (www.tp-solutions.co.uk).

PRACTICAL LAW COMPANY

- Banking Lawyer
- Financial Services Lawyer

Make a career doing what you enjoy in the law

Do you want to be at the cutting edge of law and practice but cannot see yourself spending the rest of your career in a law firm or legal department?

Practical Law Company is establishing a Banking and Financial Services Service and is looking for a banking lawyer and a financial services lawyer to work with the existing team to establish the service. This is an exciting opportunity to be involved in the service from its inception and to move to an organisation that realises know-how is the front line of its business.

You will have at least five years' PQE in the banking or financial services area or will be a professional support lawyer working in this area. You will be integrally involved in establishing the scope of the service and will write practice notes and standard documents and analyse and comment on the legal and regulatory developments in the banking and financial services sectors, gauging market and practitioners' reactions and approaching the policy makers directly. In this dynamic role you will also be reporting developments directly on a dedicated electronic update service.

You will be confident, articulate and enthusiastic and enjoy communicating the law and practice to a demanding audience. You will be proficient in using the internet and feel comfortable working on screen. You will be joining an existing team of lawyers and technology specialists, where the atmosphere is informal but hardworking. You will have a lot of responsibility but will have the opportunity to make things happen and shape the future of legal professional support.

If you are interested, please send your CV to Kelly Jones at *kelly.jones@practicallaw.com* or to Practical Law Company, 19 Hatfields, London SE1 8DJ