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Dear James,

BVCA response to consultation on International Tax Enforcement: disclosable arrangements

The British Private Equity and Venture Capital Association ("BVCA") is the industry body for the private equity and venture capital industry in the UK. With a membership of over 750 firms, the BVCA represents the vast majority of all UK-based private equity and venture capital firms, as well as their investors and professional advisers. Over the past five years (2014-2018), BVCA members have invested over £38bn into nearly 2,800 companies based in the UK. Our members currently back around 4,330 companies, employing close to 1.6 million people on a full-time equivalent basis ("FTEs") across the world. Of these, around 843,000 FTEs are employed in the UK. Of the UK companies invested in during 2018, around 87% were SMEs.

We have supported targeted action to ensure that strategies for unacceptable tax avoidance and evasion are effectively countered and recognise the need to effectively implement legislation to achieve this. However, we are concerned that if proposals on disclosable arrangements are not implemented appropriately, this could lead to an unnecessary level of disclosures that will not only undermine what the rules were designed to do, but also increase the administrative burden on the industry.

Introduction

The BVCA have reviewed the proposed regulations (the "Regulations") and the comments and guidance in the HMRC consultation document (the "Consultation") published on 22nd July 2019 with a view to the implementation of the provisions contained in Council Directive (EU) 2018/822 published on 25th May 2018 ("DAC6").

We welcome the opportunity to comment on the aforementioned Regulations and Consultation and set out our comments below. We begin by identifying key areas of concern and then respond more specifically to the questions posed in the Consultation. We are, of course, available to discuss the issues raised in person should you wish.

We should be clear that we do not make any specific comment on whether arrangements referred to in a generic way such as "acquisition" or "fund establishment" are reportable under DAC6 or not. Such conclusion will involve an analysis of each individual instance and we anticipate that, in many cases, reporting will not be required.

Preference for legislation as opposed to guidance

We do have some concern that taxpayers will be required to place considerable reliance on guidance indicated by the content of the Consultation in order to obtain clarity unavailable in the Regulations or, indeed, in DAC6 itself. The investment fund industry is already required to deal with a plethora

of statutory provisions which require reliance on guidance and, since this is a trend we would prefer to see reversed, we would like to raise the point in this context.

We would therefore suggest that references to DAC6 are transposed directly into the Regulations, with clarifications included as required to ensure the Regulations are drafted to reflect HMRC's policy intent on a standalone basis. Where this is not possible by virtue of DAC6 itself, we would welcome any other means by which HMRC can provide greater security to taxpayers needing to rely on guidance.

Multiple reporting

A key concern for the investment fund industry is the significant scope for multiple reporting of essentially the same transaction and the related scope for inconsistency in such reporting throughout the EU.

A typical cross border fund transaction or fund establishment will involve a number of potential intermediaries. Each party to the transaction will have legal and accounting advisers and potentially other specialists and a number of entities (including certain entities within the fund structure in question) may also, technically, be regarded as additional "intermediaries" under the terms of DAC6. Given the breadth of the potential hallmarks and the corresponding breadth of the definition of "intermediary" under DAC6, the scope for multiple reporting of the same information is significant. Additionally, it is entirely possible that different jurisdictions could differ in their interpretation of the DAC6 hallmarks and in the detail of information required to be reported so that the content of reports could well differ throughout the EU.

We recognise that a certain degree of "crossover" may be unavoidable to ensure that the purpose of DAC6 is met, even if this results in the same subject matter being reported on more than one occasion. Equally, we recognise that HMRC has endeavoured to address this issue at Paragraph 6 of the Consultation. However, we do not consider the current proposals to be adequate and would make the following specific comments and recommendations.

- The requirement to have a scheme reference number from another intermediary is unduly onerous and impracticable as a matter of timing. For example, there is flexibility in DAC6 on the timing of reports so that it may be that the most appropriate intermediary to make the report does not, under their domestic law, need to make it until a later point in time. Even where timing coincides (e.g. two UK intermediaries) the scheme reference number obtained by one is unlikely to be available to the other before the second intermediary's reporting deadline. This would mean that a reference number would be unavailable and an additional report would be required.

- The Consultation reference to ensuring that all information is captured in any report made by another intermediary effectively means that intermediaries are required to review the reports of others. This is significantly burdensome and adds unnecessary costs to compliance.

- It is very possible that one intermediary may not even be given access to the report of another, leaving them with no choice but to file an additional report in the UK under the provisions given in the Consultation.

- It is unclear who has the ultimate responsibility to file the report. Our members often employ multiple advisers to work on a single transaction, and in some cases all the advisers have included clauses stating that they will file the disclosure on the members behalf. This is both impractical and unnecessary and may lead to multiple submissions of similar but not

identical data. Our members would have to check multiple submissions to ensure all facts are captured correctly, which is frustratingly duplicative, unnecessarily time-consuming and costly, in particular for smaller firms with limited resources. We recommend that the guidance makes clear that a lead adviser can be appointed to lead on the disclosure and circulate the disclosure number to the other advisers involved in the transaction.

- The combination of the need for a scheme reference number and the need to effectively review other report(s) when considered in the context of the proposed penalty regime (see discussion below) means that intermediaries are likely to have to report to adopting an approach of submitting reports unnecessarily, adding to complexity and cost for the intermediaries and their clients and an overload of information for HMRC.

- DAC6 itself offers some flexibility in this area, requiring only "proof" in accordance with national law that a report has been filed in another Member State or by another intermediary. We would, accordingly, suggest that HMRC adopts a different approach here and requires only that intermediaries obtain written confirmation that another intermediary has or intends to file a report in the UK or in another Member State relating to the same subject matter and that either the reporting intermediary will provide the scheme reference number to it when it is received or will notify the scheme reference number to all parties that require it.

Concept of "made available"

We have some concerns over the explanatory wording in Paragraphs 4.2, 4.3 and 4.4 of the Consultation regarding when a reportable cross border arrangement is "made available" for implementation. We consider these paragraphs to be unnecessarily broad and lacking in clarity. This concept is also not adequately addressed in contexts outside those of "promoted" schemes, i.e. the multiparty, negotiated, commercial transactions that our members are typically involved in.

In the context of investment funds, the type of "promoted" scheme marketed to a taxpayer does not represent the type of arrangement most likely to be impacted by DAC6. Instead, potentially reportable arrangements will typically be cross border arrangements involving the initial fund establishment itself or subsequent acquisitions or exits. In addition, the day to day running of a fund itself might also technically raise issues in the form of e.g. cross border payments to or from investors or fund management entities. Is it the intention that following establishment of a structure every movement within such structure will need to be reported?

The wording of "making available for implementation" is the same in both the existing Disclosure of Tax Avoidance Schemes ("DOTAS") legislation and the Regulations. However, the interpretation suggested in the Consultation differs from that in the DOTAS guidance. Under DOTAS, for a scheme to be made available, it requires that the scheme is fully designed and is capable of being implemented. This is materially different to Paragraph 4.4 of the Consultation which states "the full details do not need to be finalised, as long as the essence of the arrangement is identifiable."

Relatively simple or internal arrangements which may (on a conservative view) trigger the hallmarks (e.g. interest free loans, or payments to investors), are such that the "essence of the arrangement" will invariably be identifiable very early. We consider it unlikely to be the intention of HMRC that the moment these are considered (e.g. by a fund house internally) they would need to be reported but clarity on when "made available" arises in such context would be welcome. In our view, this should be when legal documentation is finalised.

More complicated arrangements which involve discussions between e.g. a UK fund house and their advisers may, given the language in Paragraphs 4.2-4.4 of the Consultation, give rise to the need for

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a report at a very early stage. Early discussions of potential structuring options could need to be disclosed in a report identifying the relevant fund and the cross-border arrangement. This would potentially need to be made ahead of any action being taken by a fund to proceed with an arrangement so that a report naming a fund might be made despite such fund actively declining to engage in the arrangement. Funds might be legitimately concerned about being associated with arrangements they have no intention of implementing. Whilst we do appreciate the benefit of drawing potentially aggressive tax arrangements to the attention of tax authorities at an early stage, there appears little benefit in identifying the relevant taxpayer to which the idea is simply presented to them (unless they decide to engage the intermediary in respect of implementing the arrangement).

Certain specific arrangements in relation to funds would benefit from equally specific examples (despite our observations above, we recognise this would likely be required in guidance). For example, a new fund structure might involve a cross border arrangement and it would be helpful to receive confirmation of whether this might become reportable at the point of establishment or when investors make their initial investments into the fund. Equally, in relation to an acquisition transaction, would this be "made available" when structure papers are circulated or when the agreements are ready to be signed? As stated, these arrangements are not promoted but rather the result of mutual negotiated commercial decision making and such situations are not currently addressed in the Consultation, which focuses on promoted arrangements.

Given the foregoing, we would recommend the following points, which should preferably be included in the Regulations.

- The concept of making available should be aligned with the DOTAS guidance.
- There should be more clarity on what "making available" means in the context of non-promoted arrangements (noting the above observations on in-house considerations and fund specific situations) again involving consistency with the DOTAS guidance and with an emphasis on ease of operation and an absence of need to disclose at a very early stage.
- The "relevant taxpayer" should not need to be identified in disclosures unless they enter into an agreement with the intermediary to provide advice in respect of the arrangement.

Confidentiality hallmark

We have some observations surrounding the drafting of the guidance at Paragraph 8 of the Consultation and the confidentiality hallmark at A(1). We consider this to be too broad and that any guidance on this point should make it completely clear that the objective purpose of the confidentiality must be related to the tax advantage in question. We are particularly concerned at the language in Paragraph 8.6 which makes it clear that standard confidentiality language will automatically fall within this hallmark.

Again, this is linked to our observations regarding the emphasis on promoted schemes. There may be many valid commercial reasons why investment funds might wish to keep certain commercial arrangements confidential and it is perfectly consistent with the aims of DAC6 for HMRC to implement this hallmark by way of a clear link between the confidentiality and the relevant tax advantage. We recommend that this is made clear in the Regulations.

Penalty regime

We note that DAC6 gives discretion to Member States in the area of penalties and we consider the proposed penalty regime set out in the Regulations to be disproportionately punitive and not

effectively targeted. Our understanding is that the HMRC proposals are the highest of any EU jurisdiction and, given the inherent ambiguity within DAC6 as to whether a report is required, we consider the strict "failure to comply" proposals are simply unfair on taxpayers and result in a significantly increased compliance burden. Inevitably, businesses will adopt overly conservative approaches to the reporting process (with potential and related volume of unnecessary reports being made to HMRC). While we recognise that a penalty regime must act as a suitable deterrent, the current proposals are excessive and are not properly directed at those who carelessly or deliberately flout the rules.

We would make the following specific observations and comments:

- There should be a clear exemption or "reasonable excuse" from penalties for those able to demonstrate that they had in place reasonable procedures to address reporting compliance under the Regulations.

- Penalties should not be based on strict "day counting" with reference to the number of unreported transactions. These could lead to penalties being excessive if a reasonable "judgment call" is held to be wrong, especially if, technically, multiple but very similar transactions are affected. Instead, the regime should target behaviour which intentionally or carelessly circumvents the rules.

- The provisions relating to the obtaining of legal advice should be amended. A person should be able to rely on advice provided by an intermediary involved in the arrangement. There is no reason to suppose that legal professionals are subject to lower standards of care as result of their involvement and there are ample professional safeguards in relation to e.g. conflict of interest to ensure that such professionals remain impartial. In addition, it is unreasonable to expect those receiving legal advice to be responsible for determining whether conclusions in relation to such advice are "unreasonable" or not. The reference to this should be deleted.

We would suggest that the penalty regime be softened such that it would not apply where intermediaries had reasonable procedures in place to determine whether reporting was required in a manner similar to that used for the recent prevention of facilitation of tax evasion rules.

Compliance issues

We do consider some of the compliance obligations in the Regulations to be unduly burdensome. For example, taxpayers would appear to be expected to include overseas reference numbers if a transaction or arrangement has been reported under DAC6 in another jurisdictions, even if the same transaction or arrangement would not have been reportable under the UK regime. This is utterly impractical in terms of actually obtaining such reference numbers and would not appear to add anything which might benefit HMRC or be consistent with the policy intent of DAC6. We would urge HMRC to reconsider this point.

In addition, we consider the annual reporting requirement for taxpayers to be onerous and unnecessary. It should be sufficient for HMRC to be made aware of an arrangement on a single occasion and cannot see the benefit of submitting the same material on multiple occasions. Again, we would ask that HMRC review this point.

Administrative and cost burden

We recognise that DAC6 must be effectively implemented and that this will, inevitably, result in a compliance cost and administrative burden for businesses. However, it should be ensured that the burdens remain proportionate and that UK law does not prompt over-disclosure in instances where there is no benefit to HMRC or the authorities in other Member States of receiving the report. Certain issues pertinent to this general point are set out above. In addition, for arrangements which are subject to material uncertainty regarding whether they are reportable, intermediaries involved in the investment fund industry may need to decide whether they disclose to mitigate the risk of penalties but accept the possibility that this could breach their legal obligations under data protection laws or other confidentiality agreements, in instances where the disclosure is ultimately deemed to not be required. We wonder if HMRC has given any thought to this issue, which will not be unique to the fund industry.

Jurisdictional scope of tax advantage

We consider that the proposed extra-territoriality of the UK Regulations applying to non-EU tax advantages is disproportionate and could have an adverse impact on the competitiveness of the UK as a place to do business, with non-EU businesses being brought within the scope of the Regulations by virtue of doing business with a UK entity.

From the introductory text of DAC6 we understand that its purpose is to protect the national tax bases of Members States from erosion. This point is elaborated upon stating that it is "critical that Members States' tax authorities obtain comprehensive and relevant information about potentially aggressive tax arrangements". Bearing in mind the nature of DAC6, this purpose envisages a "tax advantage" (which falls within one of the hallmarks) should only be considered if it relates to a "tax advantage" arising in an EU Member State. We would urge HMRC to review its position on this.

If you would like to discuss any aspect of our submission, please do not hesitate to contact Chris Elphick at celphick@bvca.co.uk.

Yours faithfully,

Mark Baldwin
Chairman of the BVCA Tax Committee

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Consultation question responses

1. **Do you have any suggestions about how HMRC can provide more clarity about when an arrangement will concern multiple jurisdictions?**

Please see our wider comments on jurisdictional scope generally and multiple reporting issues.

2. **Are there any persons or arrangements who might be caught by this approach to defining "intermediary" who you think should not be caught?**

Territorial scope of intermediaries reporting obligations

The definition of "intermediaries" given by Article 3(21) of DAC6 would appear to catch a UK resident entity where it is only providing services relevant to the cross-border arrangements from an overseas permanent establishment (PE). Imposing a reporting obligation to HMRC on a UK entity which isn't involved in the transaction at an entity level in the UK appears disproportionate and administratively burdensome. Where the PE is located in another Member State, the PE would be caught irrespective of this requirement, but the report would be required to be made in the UK to prevent multiple reports under the hierarchy of reporting intermediaries under Article 8ab. (3) of the DAC. We would therefore recommend that the Regulations clarify that if the services relevant to the cross-border arrangements are only provided from an overseas PE and the UK "parent" isn't involved in the transaction at an entity level in the UK, then there should be no UK reporting obligation.

Legal professional privilege

We are not certain that the HMRC position on legal professional privilege is technically correct, but defer to comments made by the Law Society and similar bodies in this area, which will be better placed to raise any concerns on this.

3. **Does this definition of intermediary risk not catching certain types of intermediary who should be caught?**

No – we do not consider this to be a risk.

4. **Can you identify any particular practical challenges with regard to HMRC's approach to identifying intermediaries, and what information they have in their knowledge, possession or control?**

One challenge which we do see is that, in large advisory organisations, there are likely to be very strict procedures surrounding client confidentiality and it may be that certain teams within the same organisation do not have ready access to the same information, despite all such information being held by the organisation as a whole. We think it would be beneficial for it to be clear that information should be within the knowledge, possession and control of the individuals involved in the relevant arrangement. This should not necessarily be by reference to the entirety of the organisation concerned.

5. **Do you have any other comments about the definition of intermediary and who will be caught under the proposed rules?**

Territorial scope of the UK regulations

The definition of intermediary in the UK Regulations refers back to the meaning given by Article 3(21) DAC6. The policy intent of HMRC in the Consultation (see Paragraph 3.14) appears to be to

limit the definition of intermediary to those that have a connection with the UK but the definition is not refined in the Regulations beyond that in Article 3(21) of DAC6, which makes reference to intermediaries with a connection to any Member State. Assuming the policy intent is to limit the definition of "intermediary" within the Regulations to just UK intermediaries, we should be grateful if this could be clarified.

Treatment of in-house tax teams

In the absence of a third-party intermediary advising on a reportable cross-border arrangement, advice may have been provided by in-house experts (including the in-house tax team) on the reportable cross-border arrangement. In many fund structures, the employing entity of the in-house experts will not always be the "relevant taxpayer". In this case, would the in-house tax team be classified as an intermediary, or would the reporting obligation fall on the relevant taxpayer? This is currently unclear and we would welcome a flexible approach (for example by way of a choice as to which entity makes the disclosure).

Treatment of general partners in fund structures

We should appreciate confirmation that general partners in fund structures will not generally be treated an intermediaries under these rules. General partners are typically advised by fund managers and advisers in relation to running their funds and, although they are empowered to implement such advice or not, it would appear disproportionate for them to be regarded as additional intermediaries given the nature of their role. The investment managers/advisers will, of course, be intermediaries in the relevant transactions if the nature of the fund's involvement meets the intermediaries threshold.

6. **For the purposes of the ongoing requirement on relevant taxpayers, do you agree that a relevant taxpayer should be regarding as participating in the arrangement in any year where there is a tax effect or where it could reasonably be expected that there would be a tax effect in a subsequent year?**

Please see our comments above on the annual reporting requirement.

We would also urge HMRC to clarify the treatment of historic structures and whether they would be grandfathered. For example, a business may have an existing funding structure (i.e. which was in place prior to the introduction of DAC6) under which cross-border interest continues to be paid. In this example for instance, would the ongoing payment of interest trigger any disclosure obligations? Additional disclosure would be inconsistent with the DOTAS in situations where new hallmarks have been introduced.

Definition of "made available"

Please see our wider comments on this.

7. **Do you agree that the amount of evidence required for intermediaries and taxpayers to satisfy themselves and HMRC that all the necessary information has been reported is appropriate?**

Please see our wider comments in relation to multiple reporting.

8. **Do you think that the approach to defining main benefit test and tax advantage is proportionate?**

We welcome the clarification that the main benefit of an arrangement will "not be to obtain a tax advantage, if the tax consequences of the arrangement are entirely in line with the policy intent of the legislation upon which the arrangement relies". It should be clear that this determination is be based solely on the UK policy intent so that there is no burden in relation to the policy intent of other Member States.

9. **Do you have any comments on the approach set out for hallmarks under Category A?**

Please see above comments regarding confidentiality.

10. **Do you have any comments on the approach set out for hallmarks under Category B?**

It does not appear to us that the example of FDI in relation to B(3) is a circular arrangement since it does not make clear that the source and destination of the funds is the same person or entity as should be required. In addition, it should be confirmed that the intention is for B(1) and B(3) is to apply only to wholly artificial arrangements since this hallmark is otherwise unduly wide.

11. **Are there any points in the definition of associated enterprise which you think require clarification or explanation in guidance?**

We consider this to be clear.

12. **Do you think the above approach will prevent unnecessary reporting of benign activities, while avoiding loopholes that could enable intermediaries and/or relevant taxpayers to avoid their reporting obligations? If you foresee problems with the approach please provide details of possible solutions.**

Please see our wider comments on the issues with multiple reporting and reporting of potentially benign activities.

13. **Do you think that this approach will also work for dealing with Collective Investment Schemes? Alternatively, what other approached do you think would be better?**

It would be helpful if there was some acknowledgement that widely held Collective Investment Schemes are not expected to be engaged in reportable arrangements in their core operations of receiving investments from investors, buying and selling assets and returning money to their investors.

14. **Do you think particular guidance is needed in respect of hallmark C(3)?**

This would appear to be sufficient.

15. **Do you agree that this hallmark should refer to the amount treated as payable for tax purposes? What do you think are the advantages and disadvantages of this approach, and of any suggested approach?**

We have nothing specific to add on this point.

16. **Do you have any general comments about the approach to hallmarks under category C?**

The information in the consultation document is helpful in providing clarity in some areas

17. **Do you have any comments on the approach set out for hallmarks under Category D?**

We have no comments on this.

18. Where an arrangement relates to companies which are resident for tax purposes in jurisdictions where corporate tax applies at the group level, should hallmark E(3) similarly apply at the level of the sub-group located in that jurisdiction or at the company level? What would be the particular advantages or disadvantages of applying the rules at the group level?

We have no comments on this.

19. Do you have any comments about the approach to hallmarks under Category E?

We have no comments on this.

20. Do you have any suggestions for how the penalty regime could be improved?

Please see our wider comments in relation to penalties.

21. Do you have any particular comments about the commencement rules, and HMRC's approach to dealing with backdated reporting requirements?

We welcome the clarification that penalties will not be due where there is a lack of clarity around the obligations or interpretation of the UK Regulations, prior to the publication of the consultation document. However, we would reiterate the point made above regarding the application of the Regulations to non-EU tax advantages as outlined above. As stated, we hope that this will be clarified in accordance with HMRC policy in the final version of the Regulations. However, in the event that this remains unchanged and the Regulations are not altered, it is important that reporting requirements in this area apply only from the date the final legislation is published.

Please see also our wider comments on "making available" in the context of commercial transactions.

22. Are there any particular areas of DAC 6 that you would like HMRC to provide guidance on, which are not covered elsewhere in this consultation?

Impact of Brexit

It is understood that the UK Regulations will come into force irrespective of whether the UK leaves the European on 31 October 2019 or at a later date, further clarity would be welcome on how information will be exchanged in these instances and whether the UK will have access to the Schema.

LLP members

We note that the Consultation makes it clear (see Paragraph 3.10) that employees will not be treated as intermediaries on an individual basis. However, this is not the case in relation to LLP members, who are not employees, but who are self-employed. We would welcome confirmation that LLP members (or other partners in a partnership business) will likewise not be treated as intermediaries required to report in their own capacity but that any obligations will fall only on the LLP (or other partnership) itself.