

Autumn Budget 2021

Notification by large businesses of uncertain tax treatments

November 2021

Finance Bill 2021-22, published on 4 November 2021, includes proposed legislation for the new notification of uncertain tax treatment (UTT) regime.

The UTT regime will require large businesses to notify HMRC of 'uncertain amounts' in respect of corporation tax, VAT or income tax (including PAYE), subject to a threshold test and specific exemptions. A treatment is defined as being 'uncertain' if it falls within one (or more) of the two specified conditions (or 'triggers').

The proposed legislation included in Finance Bill 2021-22 makes a significant change to the definition of 'uncertain amount' as compared to the draft legislation published earlier this year. One of the proposed triggers - which would have been satisfied whenever there was a 'substantial possibility' that a court or tribunal would find the treatment to be incorrect - has now been removed.

The removal of this third condition or trigger will be welcomed by businesses, as this had been a key area of concern during the consultation on the draft rules. However, the Government has indicated that it remains committed to further consideration of a future third trigger, so it is possible that a modified version of this trigger will be introduced at a later stage.

The notification requirement will apply to tax treatments included in 'relevant returns' required to be filed on or after 1 April 2022. This means that notification is potentially relevant to transactions and uncertain treatments arising now. Businesses should begin preparing at the earliest opportunity for the implementation of the regime - this may include considering the potential application of the UTT regime to past, ongoing and proposed transactions, and putting in place the necessary processes to comply with the rules.

Unless stated otherwise, the summary set out in this alert is based on clauses included in Finance Bill 2021-22 as published on 4 November 2021 and on draft guidance which was issued by HMRC on 19 August 2021 and subsequently withdrawn on 27 October 2021. The proposed UTT legislation contained in Finance Bill 2021-22 remains subject to change and will not become final until Royal Assent is received, the timing of which is not yet known. It is anticipated that HMRC will issue revised guidance on the UTT rules in due course, which may provide further clarification on the application of the rules.

This alert is intended only as an overview of the UTT rules and should not be used as the basis for determining whether the UTT rules apply to a specific transaction or treatment.

Which taxes are in scope?

The taxes in scope are corporation tax, VAT and income tax (including amounts collected via PAYE). For these purposes corporation tax includes any amount chargeable as if it were corporation tax or treated as corporation tax, except that the bank levy, the bank surcharge and controlled foreign company (CFC) charges are specifically excluded.

Which entities are within the scope of the UTT regime?

The UTT regime applies to companies and partnerships (including LLPs) which meet the definition of 'large business' – which is modelled on the Senior Accounting Officer (SAO) regime, and Publication of Tax Strategies (PoTS) regime. Broadly, businesses will fall within the scope of the regime if they have a 'UK turnover' above £200 million and/or UK balance sheet total over £2 billion. For groups, the turnover and balance sheet amounts for all companies and/or partnerships within the charge to corporation tax need to be aggregated.

Some entities that satisfy turnover and balance sheet criteria are not intended to be in scope, such as collective investment schemes.

Which tax treatments are potentially notifiable?

A tax treatment in relation to corporation tax, VAT or income tax (including PAYE) which satisfies one or both of two specified conditions (or 'triggers') will be an 'uncertain amount' and will be potentially notifiable, subject to the application of a threshold condition and specific exemptions.

The first condition/trigger (Trigger 1) applies where a provision has been recognised in the accounts of the company (or members of the partnership) in respect of the treatment.

The second condition/trigger (Trigger 2) is applicable where the treatment relies on an interpretation that is contrary to HMRC's known interpretation of the law. HMRC's position is 'known' if it is apparent from published HMRC documents or from 'dealings' with HMRC. 'Dealings' in this context means direct interaction between the taxpayer and HMRC – but is not limited to discussions regarding the specific transaction or treatment concerned.

Businesses will need to consider putting in place processes to ensure that any treatments included in a relevant tax return which are not consistent with HMRC's known position are identified. With respect to published HMRC documents, draft guidance issued in August 2021 (but formally withdrawn on 27 October 2021) provided a number of examples of documents which do, or do not, indicate HMRC's 'known' position on a matter; however, these examples are not exhaustive. In the absence of an exhaustive list of documents (or types of document) that establish HMRC's 'known' position, businesses may find it difficult to apply this Trigger with certainty.

There may be uncertainty as to how to apply this test in cases where HMRC publications, such as its manuals, are not fully up-to-date. HMRC has indicated that it is undertaking an exercise to update its

manuals. The interaction between case law developments and HMRC's known position may also cause further complexities in the application of this condition/trigger.

A third trigger, which was originally included within draft legislation published on 20 July 2021, would have applied where there was 'a substantial possibility that a tribunal or court would find the taxpayer's position to be incorrect'. This trigger is not included in the Finance Bill 2021-22.

How does the threshold operate?

Notification of an uncertain amount will only be required where the 'tax advantage' arising from a treatment exceeds a £5m threshold. Where the financial year in respect of which notification may be required is more or less than 12 months, then the £5m threshold will be adjusted proportionately. The threshold applies separately for each of the three taxes.

In order to determine whether a treatment exceeds the threshold, it is necessary to quantify the tax advantage arising from the uncertainty. The proposed legislation provides detailed rules for this quantification, based on (broadly) comparing the actual treatment to the tax outcome under an alternative scenario. The alternative scenario to be used depends on which of the two triggers is applicable. Where an uncertain amount meets both notification criteria, the question of whether the threshold is exceeded will be determined based on the criteria that produces the largest tax advantage.

It is unclear from the proposed legislation whether a net or gross basis should be used when considering what constitutes the uncertain amount for VAT. If netting is not to be used for these purposes, this would seem to be at odds with the way in which the VAT regime works ordinarily.

Generally, the threshold applies separately for each uncertain amount, but treatments which are 'substantially' the same are required to be aggregated for these purposes. For corporation tax and PAYE, the good news is that these aggregation provisions are limited in scope – generally they apply to treatments in the same return (or same type of return) for the same financial year, and there is no requirement to aggregate treatments across the group.

From a VAT perspective, aggregation would be required within a VAT group, and across 'related' transactions for the same financial year (whether within a VAT group or as part of a single VAT registration).

For PAYE, aggregation of treatments which are substantially the same is required across different returns for the same financial year. It should also be noted that where the return is a PAYE return, national insurance contributions are to be treated as income tax for the purposes of determining the aggregate value of the tax advantage.

Are there any exemptions from notification where the threshold is exceeded?

The rules provide a number of specific exceptions which, where applicable, mean that an 'uncertain amount' will not need to be notified.

A 'general exemption' will apply where it is reasonable to conclude that all, or substantially all, of the information which would otherwise be required to be notified has already been made available to HMRC.

Any information disclosed under the Disclosure of Tax Avoidance Schemes (DOTAS) rules, the DASVOIT VAT rules or the mandatory disclosure of cross-border arrangements (DAC 6) rules is treated as having been made available to HMRC.

Situations where the general exemption could apply in practice include where a business has already informed its Client Contact Manager (CCM) of the uncertainty concerned in the course of ongoing discussions, or where it has obtained clearance from HMRC regarding a specific treatment which has been adopted in a return. It is to be hoped that HMRC's new guidance on the UTT regime, when published, will provide clarity on the steps that businesses will need to take to ensure that this exemption applies.

For those businesses without CCMs, HMRC has stated that it would make a process available to ensure that these taxpayers are not disadvantaged in terms of their ability to avail themselves of the general exemption. However limited information is currently available about how this process will work, for instance, timeframes, input required etc.

Businesses may wish to carefully consider whether records of previous exchanges which have taken place with HMRC on a matter contain sufficient information for the general exemption to apply. They should also be aware of the potential application of the general exemption when engaging with HMRC regarding current and proposed transactions.

In addition to the general exemption, an exemption is included which will apply, for corporation tax only, to intragroup transactions where the net tax advantage arising to the group from the treatment is below the £5m threshold. It is notable that the group exemption does not apply to VAT groups.

It had been hoped that the legislation would include a specific exemption for transfer-pricing treatments, in recognition of the fact that transfer pricing is inherently subjective, with 'uncertainties' in many cases reflecting the judgments about the application of the arm's length principle, rather being a matter of legal interpretation. However, the proposed legislation included in the Finance Bill 2021-22 does not provide any such exemption. If one of the Triggers is satisfied in respect of a transfer pricing treatment, the treatment will be potentially notifiable, subject to the threshold and the potential application of one of the other exemptions (group exemption or general exemption).

When do the rules apply and when should businesses make a notification?

The notification process applies separately for each of the three taxes within scope and is aligned to the return filing process for that tax. The regime will first apply to uncertain tax treatments in relevant returns that are required to be made on or after 1 April 2022.

In a corporation tax context, this means that any corporation tax returns which are due to be filed on or after 1 April 2022 will fall within the regime. To the extent that these returns contain tax treatments which are notifiable, the deadline for notifying these will generally be the corporation tax return filing deadline. Where the relevant return is not an annual return (e.g. PAYE or VAT), the notification must be given on or before the date on which the last relevant return for the financial year in question is required to be made.

From a VAT perspective, to identify the period relevant for notification, a business will need to consider both its financial year and the VAT return stagger. The first standard VAT return period where notification could be required is the VAT return period ending 28 February 2022 (monthly or quarterly) which would be

due on 7 April 2022. However, notification will only be required if this is the last prescribed VAT accounting period falling wholly within the financial year. So, a business with quarterly VAT returns ending 28 February 2022 would also need to have a financial year ending between the end of February 2022 and 30 May 2022 to require notification by 7 April 2022.

For PAYE the same principle applies: notification must be made on or before the date on which the last relevant return for the financial year in question is required. The withdrawn draft guidance included examples of notifications of an amount included in a PAYE return for a financial year.

The notification would be for a 'financial year' so the first notification after commencement of the regime could be regarded as 'retrospective' in the sense that it may apply to transactions and treatments which are arising now. It is notable also that, despite comments made during the consultation process, the proposed legislation does not provide for 'grandfathering' of historic uncertain treatments – i.e., transactions or treatments which were first entered into in prior periods but which will be reflected in relevant returns falling with the UTT regime.

It will be interesting to see whether HMRC introduces a light touch approach in the first year with regard to discussing uncertain tax treatments and any potential penalties.

How do businesses notify?

The withdrawn draft guidance indicated that notifications would need to be carried out via a digital form which will be accessible from within the business's Government Gateway account. It set out a detailed list of the information which would need to be supplied via this form, including a quantification of the uncertainty, a description of the transaction/issue and details of the nature of the uncertainty. HMRC indicated that the notification form would be available to access from April 2022 to notify HMRC of any uncertainties relating to relevant returns due after 1 April 2022. For those businesses that need to make their first notification as early as April 2022, this would provide very limited opportunity to address any teething problems that may arise. It will be interesting to see whether updated guidance provides further details.

The formal notification is an obligation of the entity concerned, rather than that of a named individual. For VAT notification purposes, the representative member of a VAT group should notify and for non-VAT groups, each VAT registration would have an obligation to notify. For other taxes, each entity is responsible for its own notification. For partnerships, this is the nominated partner.

Penalties

The penalty for failure to make a notification in respect of any of the relevant taxes will be £5k initially, £25k for a second failure and £50k for a third failure within a three-year period.

A person is not liable to a penalty for a failure to notify an uncertain amount if they satisfy HMRC that they have a 'reasonable excuse' for the failure, and they put right the failure without unreasonable delay after the excuse has ended. There is no statutory definition of reasonable excuse, which is a matter to be considered in the light of all the circumstances of the particular case. What is reasonable will differ from person to person depending upon their circumstances and abilities. However, there are some excuses that are not normally accepted as reasonable including shortage of funds and reliance on another person.

It will be interesting to see how HMRC will seek to apply penalties in practice with regard to proportionality.

How we can help

If you would like to discuss how to prepare for the UTT regime, please get in touch with one of the contacts listed below, or with your usual EY contact.

For example, we would be happy to discuss how we can support you in identifying and appraising historic, current and proposed positions; scoping and implementing new processes to comply with the rules; determining HMRC's 'known position' in respect of a matter; or in quantifying potentially notifiable tax positions.

If your business has specific areas of concern in relation to the UTT regime, we would be happy to discuss these further.

Further information

If you have any questions or would like to understand more about the UTT regime and the benefits it may bring to you, please get in touch with one of the following EY contacts:

Ian Dennis	International tax	011 8928 1278
Tim West	International tax	011 3298 2330
Tarunya Kumar	Transfer pricing	020 7951 0142
Richard Milnes	Financial Services	020 7951 7750
David Reaney	Indirect tax	028 9044 1704
Sarah Delaney	Indirect tax	011 8928 1303
Steve Wade	Employment taxes	020 7951 6185
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