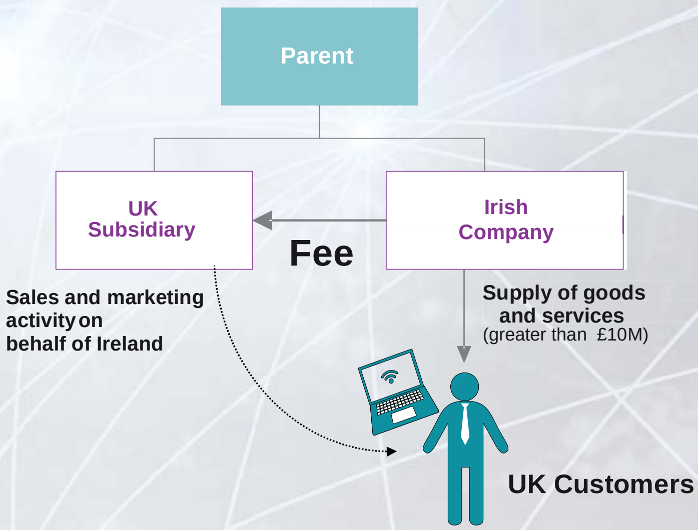
What is Diverted Profits Tax (DPT)?

The UK government published and is set to put into legislation a new tax entitled the 'Diverted Profits Tax'. DPT is aimed at multinationals entering into arrangements to divert profits from the UK either by arranging their affairs so as to avoid having a UK permanent establishment (PE), or by making payments which lack economic substance (or end up in a low tax company that lacks the economic substance).

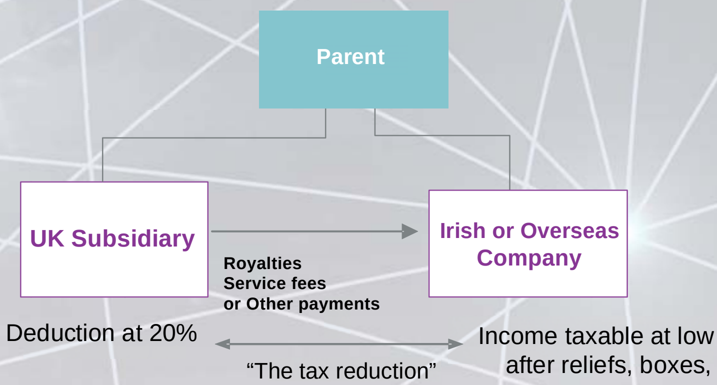
The draft DPT legislation is very complex and likely requires advice by specialists who have considered whether common transfer pricing arrangements, used by multinationals in Ireland, are likely to be caught when DPT comes into force this April. The legislation does not grandfather pre-existing arrangements from being subject to DPT.

Two pillars of DPT targeting business arrangements in UK

Avoided Permanent Establishment



Payments Lacking Economic Substance



The scope of DPT legislation is very wide...

Does your business...?

Many commercial transfer pricing arrangements that could be caught by DPT	
Sales of goods or services cross-border which are supported by on the ground UK teams but without a taxable UK branch presence	Sales of goods or services into the UK through a UK branch or subsidiary where the Irish seller, in turn, is making payments to a low-tax jurisdiction, e.g. purchase of goods with embedded royalties
Undertake cross-border leasing, financing, insurance, royalty licensing arrangements or property transactions	Payments for management, procurement, R&D or other services

When must I comply with DPT?

The new law is expected to apply from 1 April 2015, applying a punitive rate of 25 percent to the diverted profits (greater than UK corporation tax rate of 20 percent). DPT cannot be ignored by Irish business operating in the UK as the law places the onus is on the company to notify HMRC within three months of accounting year-end if the company might be subject to DPT. For financial year ends after 1 April 2015, KPMG expects that first notices from HMRC could require DPT payments this coming autumn.

HMRC maintains that DPT is consistent with principles and international efforts led by the OECD on tackling Base Erosion and Profit Shifting (BEPS) by multinational companies.

Key concerns for Irish business	
No treaty relief	***Prepay a presumed tax***
Because DPT is a new tax, Irish companies will be unable to avail of double tax relief under the tax treaty between Ireland and the UK.	Cash flow is negatively impacted because DPT must be paid within 30 days of a notice by HMRC, followed by a 12 month review to decide if DPT was correct.
Inconsistency with BEPS initiatives	***No comfort from UK APAs***
Risk of critical differences between the DPT rules when compared to OECD recommendations on addressing the BEPS concerns regarding the avoidance of PEs or lack of economic substance.	DPT may still apply even when a UK entity has pre-agreed with HMRC through an Advanced Pricing Agreement (APA) on the transfer pricing outcome of a cross-border transaction into the UK.

Interaction with transfer pricing

DPT has a secondary aim to remove information bias that is perceived to favour taxpayers, in order to allow HMRC a full and timely examination of higher-risk transfer pricing transactions into the UK. DPT provides strong financial incentives for full disclosure and early engagement with HMRC on those higher-risk transfer pricing structures.

How KPMG can help

Business in Ireland need to know now if either of the two DPT pillars might apply to them. Final DPT legislation is only due on 18th March, making it prudent to evaluate your DPT position today on the draft legislation.

Our tailored offerings to address the broad DPT and transfer pricing impact include:

- Evaluate your DPT position in the light of draft legislation, current guidance, ongoing discussions with HMRC as well as our prior DPT evaluations for global companies
- Prepare documentary evidence for DPT analysis (i.e. not relying on the traditional transfer pricing analysis)
- Refresh your transfer pricing structure to carefully examine economic substance
- Model tax and cash flow implications of falling into DPT
- Consider a protective notification to protect against the DPT penalty for not filing
- Restructure your UK business model
- Engage with HMRC for a transfer pricing APA to also cover your DPT position

Come talk to our UK DPT and Irish Transfer Pricing experts today.

Mathew Scott

Partner, UK Corporate Tax
t: +44 (0) 7939 048604
e: mathew.scott@kpmg.ie

Warren Novis

Director, Transfer Pricing
t: +353 1 700 4154
e: warren.novis@kpmg.ie

kpmg.ie

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