

WIRRAL COUNCIL

PENSIONS COMMITTEE

22 JUNE 2015

SUBJECT:	UPDATE ON TAX MANAGEMENT ARRANGEMENTS
WARD/S AFFECTED:	NONE
REPORT OF:	STRATEGIC DIRECTOR TRANSFORMATION & RESOURCES
KEY DECISION?	NO

1.0 EXECUTIVE SUMMARY

- 1.1 The purpose of this report is to provide members with an update on the progress made by the Fund in:
- Recovering Withholding Tax (WHT) from UK and European tax authorities.
 - Reclaiming tax on Manufactured Overseas Dividends (MOD).
 - And to report on a Property VAT Audit conducted by KPMG during the Financial Year ended 2014/15.

2.0 BACKGROUND AND KEY ISSUES

- 2.1 In order to assist in the recovery of European Withholding tax KPMG has been engaged as tax advisor as, in various tax jurisdictions, physical presence of the tax agent is necessary to initiate the claims.
- 2.2 In respect of the MOD claim, Pinsent Mason is leading the test case in the First Tier Tribunal, with KPMG as lead advisors, on behalf of a group of claimants under a Group Funding arrangement. Merseyside Pension Fund is a part of that group.

KPMG was appointed in 2009 and updates on progress were brought to this Committee in September 2009, March 2011 and March 2013.

2.3 European Withholding Tax

MPF has filed European Withholding Tax claims in the following six tax jurisdictions:

- Spain
- Netherlands
- Norway
- Italy
- Germany
- France

European Tax Claims By Merseyside Pension Fund
(WHT)

Country	Claim Value Local Currency (€)	Claim Value Base Currency (£)	Amount Received Base Currency (£)	
Spain	€ 579,107	484,731	520,803	Note 1
Netherlands	€ 256,513	225,762	225,762	Note 2
Norway	€ 69,875	54,613	54,613	Note 3
Italy	€ 593,201	421,415	0	Note 4
Germany	€ 812,707	577,415	0	Note 5
France	€ 530,061	376,599	0	Note 6
	€ 2,841,464.33	£2,140,535	£801,178	

As at Financial Year End 2014/15 a cumulative total of £801,178 has been recovered from the Spanish, Dutch and Norwegian tax authorities since 2009 and total of £1,339,357 remains unsettled.

Note 1 (Spain): All the Withholding Tax claims have been paid in full by the Spanish Tax Authority. Total value of the claim was €579,107 plus €45,963 of interest.

Note 2 (Netherlands): The Dutch claim has been settled in full.

Note 3 (Norway): The Norwegian tax claim amount has been received in full.

Note 4 (Italy): Claims have been filed by KPMG Italy and all the supporting documents have been submitted by MPF. Currently we are awaiting response from Italian Tax Authority. Total value of the claim is €593,201.

Note 5 (Germany): Claims have been filed with the local tax offices but there has been no progress as yet by the German Tax Authority. The Fund has recently filed a top up claim for 2012-14 with the value of approx. €181,000. Total value of German WHT claim is €812,707.

Note 6 (France): Total value of French WHT claim is €530,061. Although the French Supreme Court has decided that French WHT rules contravene EU law, the relevant courts must verify that other European pension funds were comparable to a French Not for Profit organization. Various submissions have been made to satisfy this requirement which are still under consideration by the French Tax Authority.

2.4 Manufactured Overseas Dividends (MOD) Claims:

Total value of MPF's MOD claim is £5,974,394.

This claim has arisen out of discriminatory treatment of stock lending income by HMRC whereby no tax was charged when a UK security was borrowed by a UK borrower from a UK lender. HMRC, however, imposed a 15% withholding tax when an overseas security was lent to a UK borrower by a UK lender. This discriminatory treatment of stock lending income has been abolished with effect from 31 January 2014.

The MOD claim has reached litigation stage and a First Tier Tribunal hearing is anticipated later this year. As with all litigation, the outcome has a degree of uncertainty.

2.5 Internal Tax Claims:

The Fund's internally managed portfolios are monitored by the accountancy team to identify potential tax claims. Since July 2011 the internal team has been successful in recovering £518,440 of withholding tax from HMRC.

The Fund has implemented the practice of appraising prospective investments from a tax implications point of view at the due diligence stage, where tax impact is assessed on UK and overseas investments, to ensure double taxation treaties relief is available and utilised and returns are not eroded by unforeseen tax implications.

2.6 Value Added Tax (VAT) Audit:

VAT is a significant element in Fund's direct property portfolio. During Financial Year ended 2014/15 KPMG were engaged to provide:

- A review of property VAT accounting policies and practices.
- An evaluation of VAT optimisation on the Property portfolio.

The outcome of the VAT audit was favourable, with no findings, which provides assurance around the current VAT accounting policies and practices.

3.0 RELEVANT RISKS

- 3.1 There is a potential risk that Withholding tax claims filed in Italy, Germany and France may be unsuccessful but given the success in other European territories it is prudent that those claims are pursued.
- 3.2 The MOD claim has reached the early stage of litigation. It is expected that findings of First Tier Tribunal, if unfavourable to HMRC, would be challenged in Upper Tribunal and higher courts which may increase the legal costs and risks of claim failure. The Fund is part of a group of claimants under a Group Funding Arrangement (GFA) which shares litigation costs and is under no

obligation to proceed further with litigation. The Fund is kept informed of the costs incurred and can withdraw from the arrangement at any time.

- 3.2 The Fund is a tax exempt organization which puts it in a different position from other non-exempt institutional investors. However, this exemption is not applied as a default during tax deduction at source stage on various investments and exemption has to be claimed via R63N submissions in the UK and under Double Taxation Treaty provisions in overseas tax jurisdictions. It is therefore important that investments are monitored and appropriate submissions are made in timely manner.
- 3.3 The Fund is working with its advisors, global custodian, overseas sub custodians and other institutional investors in tax matters to ensure that it responds to ever changing domestic and foreign tax rules and regulations in a timely manner to avoid the risk of non-compliance.

4.0 OTHER OPTIONS CONSIDERED

- 4.1 The Fund could have decided not to pursue its overseas tax claims and opt out of the Group action against HMRC over its MOD claims but, given the significant amounts involved and substantial tax recoveries made, it has strengthened Fund's view that the claims should be pursued.

5.0 CONSULTATION

- 5.1 There has been no consultation undertaken or proposed for this report. There are no implications for partner organisations arising out of this report.

6.0 OUTSTANDING PREVIOUSLY APPROVED ACTIONS

- 6.1 There are no outstanding previously approved actions.

7.0 IMPLICATIONS FOR VOLUNTARY, COMMUNITY AND FAITH GROUPS

- 7.1 There are no implications arising directly from this report.

8.0 RESOURCE IMPLICATIONS: FINANCIAL; IT; STAFFING; AND ASSETS

- 8.1 Costs to date are £239,000 and are offset by the recoveries of £801,178 from European claims. An additional £518,440 has been recovered by the internal team. Outstanding withholding tax claims amount to £1,339,357 and MOD claims to £5,974,394. KPMG's fee for the MOD claims includes a contingency fee element. Therefore, should the MOD claim fail, there will not be any further fees due to KPMG.

9.0 LEGAL IMPLICATIONS

- 9.1 There are no implications arising directly from this report.

10.0 EQUALITIES IMPLICATIONS

10.1 Has the potential impact of your proposal(s) been reviewed with regard to equality?

(b) No because there is no relevance to equality.

11.0 CARBON REDUCTION AND ENVIRONMENTAL IMPLICATIONS

11.1 There are no carbon usage implications, nor any other relevant environmental issues arising from this report.

12.0 PLANNING AND COMMUNITY SAFETY IMPLICATIONS

12.1 There are no planning or community safety implications arising from this report.

13.0 RECOMMENDATION/S

13.1 It is recommended that members note the report and agree to officers continuing with the recovery of tax under the existing arrangements.

14.0 REASON/S FOR RECOMMENDATION/S

14.1 The Fund has the potential to recover further substantial amounts of tax from the UK and European tax authorities.

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APPENDICES

BACKGROUND PAPERS/REFERENCE MATERIAL

SUBJECT HISTORY

BRIEFING NOTES HISTORY

Briefing Note	Date

SUBJECT HISTORY (last 3 years)

Council Meeting	Date
Pension Committee	March 2013