Pension Fund Sub Committee
23rd February 2010

Report from the Director of Finance and Corporate Resources

For Action

Wards Affected:
ALL

Report Title: European Withholding Tax

1 Summary

1.1 This report details work commissioned to reclaim additional European withholding tax from various states.

2 Recommendations

2.1 Members are asked to note the report.

3.0 Detail

3.1 Most European countries levy a tax – known as a withholding tax – on dividends paid by companies within their jurisdiction. However, to encourage investors to invest in their home countries, local investors have often been able to either receive their dividends gross of withholding tax or been able to reclaim any tax suffered. However, overseas investors have been to irrecoverable withholding taxes.

3.2 EEC law (and European Free Trade Area (EFTA) rules) state that European investors should be treated equally – there should be no distortion of capital movements arising from local discrimination.

3.3 In 2004, judgements were handed down in two important test cases around European tax law. Fokus bank is a Norwegian bank which has paid dividends to Norwegian shareholders in respect of shares previously held by non-resident shareholders in the UK and Germany. Under Norwegian domestic tax law (now repealed) dividends paid to non-resident shareholders in Norwegian resident companies were subject to a 15% rate of dividend withholding tax. In addition, Norway ran a full imputation system imputing the 28% Norwegian corporation tax to Norwegian resident shareholders, but not to non resident shareholders. This case was heard by the EFTA court. The facts of the Fokus case were very similar to those in the European Court of Justice case of Manninen v Finland, where Finland was similarly running a full imputation system, but only imputing domestic corporation tax paid by the Finnish resident companies to Finnish resident individual shareholders.

3.4 The courts ruled that the arrangements followed by the Finnish (ECJ) and Norwegian (EFTA) authorities were contrary to law. However, other issues now arise, in particular, the impact on other European states that have / have had similar arrangements, and how far back claims for repayment of tax can go.

Actions taken by Brent

3.5 The accountancy firm, KPMG, has been prominent in publicising its tax recovery services to local authorities. KPMG identifies which countries have adopted tax systems that are contrary to European / EFTA law, which are now accepting claims to recover tax, and which might in future. They have identified fourteen countries that appear to be in breach of perceived European law (including France, Germany, Netherlands (now repaying), Italy and Spain). KPMG liaises with custodians to gather information about tax suffered, and present claims to local tax authorities. They also institute local legal action where individual countries are seeking to resist repayment – this is likely to be required in France. KPMG currently have around 30 local authority clients.

3.6 Although the custodian (Bank of New York Mellon) reclaims tax in normal circumstances, they are not able to provide a retrospective service where the European Court of Justice is involved. Brent has therefore signed up to use the services of KPMG – the issue became urgent because there was a danger of losing potential recoveries if claims were not registered by 31st December. The fees payable are £29,500 (at present the council is committed to 3 countries, but this is may grow) and a share of costs if legal action is required.

3.7 It is anticipated that the claims may amount to around £600,000. The amount that may be recovered depends on legal action, the extent of any retrospection and records of holdings and tax withheld. For example, Finland may be required to go back to 1994, but Norway is maintaining that any retrospection should not go beyond three years. Value for money will also be an issue – members will be aware that overseas equity exposure did not rise above 25% of the Brent Fund until 2003, so that claims may not be worth pursuing apart from in major markets (possibly France, Germany, Netherlands and Italy).

3.8 Resolution will take some time, but the initial claims have been submitted for Germany, France and Netherlands. KPMG is optimistic that substantial recoveries can be made.

4.0 Financial Implications

4.1 These are outlined within the report.

5.0 Staffing Implications

5.1 There are no staffing implications apart from authorising claims and liaising with custodians and KPMG.

6.0 Legal Implications

6.1 There are no legal implications.

7.0 Diversity Implications

7.1 The proposals in this report have been subject to screening and officers believe that there are no diversity implications.

8.0 Background Information

Articles in the Tax Adviser in January 2005 (Manninen case) and March 2005 (Fokus case)

Contact Officer

Martin Spriggs – Head of Exchequer and Investment
Duncan McLeod – Director of Finance and Corporate Resources