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UK Tax Update

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Set out below is a snapshot of recent UK tax developments:

HMRC BRIEFING

HM Revenue & Customs ("HMRC") has recently released a briefing aimed at providing an overview of the complexities of taxing multinational companies. In this briefing, HMRC stressed the importance of international cooperation and noted that multinationals have the opportunity to structure their business to take advantage of beneficial tax rules in different countries. In such instances, provided that this results in profits being taxed in line with where genuine economic activity is carried on, this will not amount to tax avoidance. The briefing also emphasises the importance of all tax payers (businesses and individuals) paying their fair share of tax as intended by Parliament.

In the course of setting out how multinational businesses are taxed, HMRC acknowledged that broadly companies are required to pay corporation tax in the country where they carry on the economic activity that generates their profits, not where their customers are located. As such, in contrast to the typical UK VAT position, which usually looks to the location of the customer, tax rules need to establish how much of a business's overall activities should be treated as 'belonging' in a particular country. This area is likely to be the subject of on-going scrutiny by HMRC, particularly given the recent high profile news stories surrounding the likes of ASDA and Starbucks.

GROUP RELIEF AND NON-DISCRIMINATION

On 17 October 2012, the UK Court of Appeal dismissed HMRC's appeal in HMRC v FCE Bank PLC ("FCE"). This case is noteworthy as it had seen HMRC appeal against a decision from the Upper Tribunal that the UK's pre-2000 group relief rules breached the non-discrimination article in the UK-US Income Tax Treaty (1975).

The rules had provided that, in connection with group relief claims, where both the claimant and the surrendering company were 75% subsidiaries of a third company, that third company had to be resident in the UK. In this case, FCE's parent entity was US resident.

Upon HMRC refusing FCE's claim for group relief, FCE argued that such denial, being based on the presence of their non-UK resident parent, was in breach of the non-discrimination article of the 1975 UK-US double taxation treaty. Whilst HMRC contended that the parent company was not subject to UK corporation tax, the Court of Appeal stated that the parent company's liability to UK corporation tax was immaterial for the purposes of the group relief provisions at issue and HMRC's appeal was dismissed.

Although the group relief rules were changed from 1 April 2000 to allow claims and surrenders between UK-resident members of a group even where the group relationship is traced through a

non-resident parent company, the FCE case may still be helpful to companies in non-EU parented groups which are seeking relief in the UK for losses incurred by EU-resident members of their group. It is likely that this case will also impact consortium relief claims. Whilst previously there has been a requirement for, broadly, an EEA "link" company to be present, following both the FCE case and the case of Felixstowe Dock and Railway Company & Others v HMRC, there appears to be a strong argument that such a requirement should fall foul of the non-discrimination provisions contained in the relevant UK double tax treaty.

TAXATION OF INTEREST

In response to a consultation on possible changes to income tax rules on interest, HMRC has announced that they will drop their proposals for: (i) removing the withholding tax exemption from certain intra-group Eurobonds; (ii) extending the requirement to withhold tax to "short" interest; and (iii) requiring withholding tax on funding bonds to be paid in cash. This is welcome news.

However, HMRC has confirmed that the Finance Bill 2013 will look, amongst other changes, to cater for the introduction of an equivalent for income tax of the disguised interest rules in Chapter 2A Part 6 CTA 2009.

FATCA UPDATE

Following the signing of an intergovernmental agreement between the US and UK on September 14 2012, the UK has become the first jurisdiction to actually enter into a bilateral information exchange agreement with the US to implement the US foreign account tax compliance provisions ("FATCA").

Although this intergovernmental agreement is generally viewed as being a positive step in lessening the burden of FATCA compliance, it is likely that there will still be various hurdles for financial institutions to overcome.

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If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

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