



CFC Finco state aid investigation webinar

Proactively mobilise to protect your position in advance of the European Commission's decision

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12 April 2018



With you today



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Background to the investigation

- In October 2017, the European Commission (“EC”) announced an investigation into whether the 75% and 100% UK CFC Group Financing Exemptions (“Finco Exemptions”) breach EU state aid rules within the meaning of Article 107(1) Treaty on the Functioning of the European Union (“TFEU”).
- The UK CFC rules are essentially an anti-avoidance measure aimed at ensuring the UK corporate tax base is not inappropriately reduced by transactions undertaken by non-UK subsidiaries of UK corporate taxpayers.
- The EC has indicated a preliminary view that the Finco Exemptions amount to illegal state aid, as they confer a selective advantage on multinationals funding overseas group companies (vs. third parties and UK group companies).



What is 'state aid'?

Art.107(1) TFEU” provides:

“Save as otherwise provided in the Treaties, **any aid** granted by a **Member State** or **through State resources** in **any form** whatsoever which **distorts or threatens to distort competition** by **favouring certain undertakings** or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.”

Key conditions:

- aid (any benefit or advantage in any form whatsoever);
- granted by Member States or public resources (imputable to the Member State);
- favours certain economic operators or products (selectivity);
- which actually/potentially distorts competition; and
- affects trade between Member States.

Selectivity

- For state aid to exist, there must be “selectivity”. This has consistently been held by EU jurisprudence to require three elements – a reference system from which there is a derogation, differentiation between comparable economic operators, and a lack of justification for the differentiation.
- Derogation – what is the correct reference system, and has there been a derogation?
- Differentiation – are related party and unrelated party loans comparable?
- Justification – what are the underlying principles on which the CFC regime is based?



Anticipated decision



- The EC is expected to release its decision **between August and November 2018** (and possibly earlier).
- The EC is expected to find that the Finco Exemptions amount to illegal state aid in line with its preliminary views.

The impact of a negative decision

A negative decision by the EC means that the UK Government (“the UK”) will be required to take steps to recover the ‘illegal’ aid from recipients of the aid.

In principle means affected taxpayers will be required to repay the illegally granted benefit associated with the Finco structure (from as far back as the introduction of the new CFC rules in 2013), plus compound interest. These amounts could be substantial.

Taxpayers need to consider in advance of that decision whether:

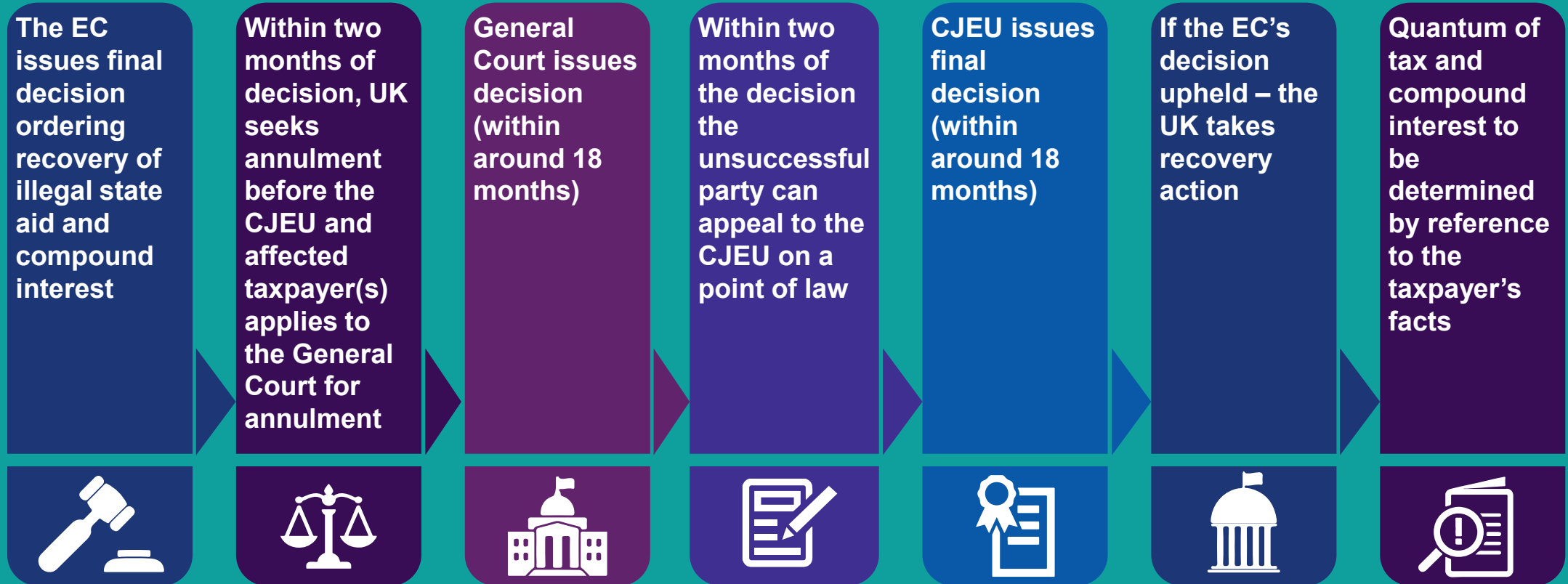
- (i) they would wish to support the UK if it challenges the EC’s decision before the General Court;
- (ii) they are entitled to and wish to lodge there own challenge against the EC’s decision before the General Court; and
- (iii) the potential action the UK may be forced to take, and whether it can be shaped and/or challenged and/or mitigated.



Recovering state aid



Challenging EC's decision



**The General Court has the power to suspend the recovery order pending the final resolution of the challenge.*

Annulment proceedings – the General Court

Late 2018 the EC issues final decision ordering recovery of illegal state aid and compound interest



Within two months of decision affected taxpayer applies to the General Court for annulment the decision

Affected tax payer will have two months from official notification of the decision to issue annulment proceedings before the General Court.

- A Beneficiary will have to demonstrate that they are likely to be subject to a recovery order or that they are regarded as directly affected by the EC's decision to be able to bring such an action.
- A Beneficiary will have two months and 24 days from the date of the decision to bring an action.
- Any challenge requires lodging a petition with a fully reasoned case, including legal arguments and supporting evidence.
- A lot of work in a short timescale.

Appeal – Court of Justice of the European Union

General Court Judgment



Within 2 months of the decision, the unsuccessful party can appeal to the CJEU on a point of law

- Any final decision of the General Court may be appealed to the CJEU on points of law (including lack of competence of the General Court, breach of procedure, or an incorrect application of EU law).
- Appeals may be brought by any party who was unsuccessful in their submissions to the General Court.

UK implementation of the EC decision

- The UK will be required to determine how to recover aid in accordance with the time limit of four months from notification of the final decision unless non-recovery is ordered.
- The relevant conditions for the permanent or interim relief from recovery of illegal state aid under EU law are rarely met.
- The UK may need to enact new domestic legislation to facilitate the recovery of the aid from UK taxpayers. Any such legislation would need to adhere to EU law principles.



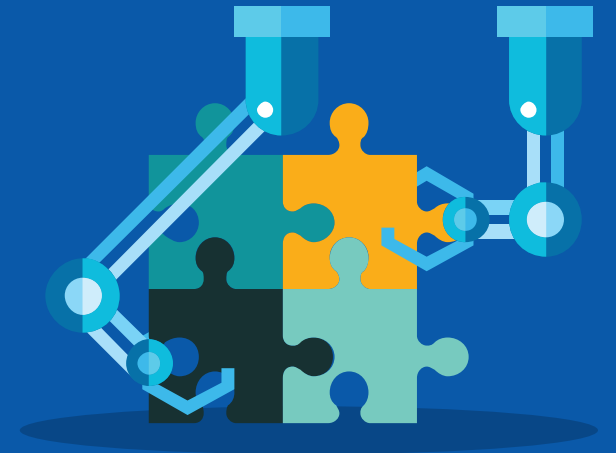
Challenging the UK

- Once the taxpayer has received a recovery order from HMRC, it will need to consider whether it can challenge the recovery order before the UK courts.
- Grounds for challenge may include legitimate expectations and/or a '*Cadbury Schweppes*' argument and/or quantum.
- Timescales for challenge are tight and therefore prior thinking and preparation is essential.



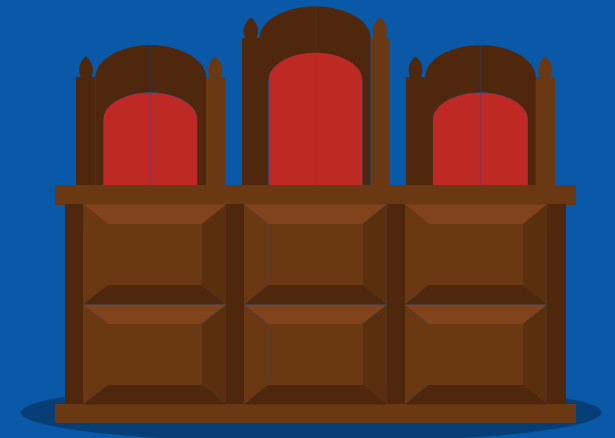
Appealing a recovery order on quantum

- It may be possible to resist recovery of aid on quantitative grounds by issuing proceedings before the UK courts on the basis that if the Finco Exemptions had not existed, the additional CFC tax payable by the taxpayer would have been lower than the amount assessed by HMRC.
- The strength of this argument will depend on the facts for each taxpayer and the quality of supporting evidence.

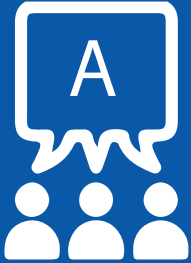


Judicial review – legitimate expectation

- It is possible to challenge the recovery of the aid on public law grounds of legitimate expectation before the UK courts.
- A legitimate expectation is said to arise “as a result of a promise, representation, practice or policy made, adopted or announced by or on behalf of government or a public authority.”
- The argument is that the UK created a legitimate expectation that the Finco Exemptions were compatible with EU state aid law.
- The strength of this argument will be specific to individual taxpayers and will depend on the extent of evidence that the UK made specific statements that it considered the Finco Exemptions to be compatible with EU state aid principles (either as part of the CFC consultation process or in separate communications to the taxpayer).
- Judicial Review must be brought as soon as possible and no later than three months after the grounds to make the claim first arose.
- The likely remedy will be damages.



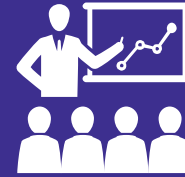
KPMG offering



**Education regarding
timelines and key
milestones**



**Modelling of the
financial impact of the
likely outcomes**



**Strategic planning
regarding options for
challenge and possible
arguments**



**Organising and/or
supporting a challenge
of the EC decision
before the General
Court and the CJEU**



**Assessing possible
arguments for resisting
any recovery action by
the UK**



**Assisting with the
mitigation of any
consequences should
all avenues of challenge
fail**



**Bringing a claim
against the UK for
damages suffered**



**General tax,
restructuring and legal
support**



Questions?





Thank you



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