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Key Individual Concept and the risk of Central Management and Control in the UK

5 October 2011



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Private and confidential

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The Directors
Alderney Gambling Control Commission
St Anne's House, QEII Street
Alderney
GY9 3TB

Dear Sirs

Tax implications of the Key Individual Concept and risk of Central Management and Control in the UK

In accordance with your instruction, we enclose our report which outlines the tax implications of the Key Individual Concept and the risk of Central Management and Control being based in the UK.

Our report has been prepared for Alderney Gambling Control Commission ("AGCC") and, any decisions taken in relation to the work performed remain the responsibility of the Directors. The Important notice opposite should be read in conjunction with this letter.

Our report is for the benefit and information of AGCC only and should not be copied, referred to or disclosed, in whole or in part, without our prior written consent. The scope of work for this report has been agreed by the addressees and to the fullest extent permitted by law we will not accept responsibility or liability to any other party (including the addressees' legal and other professional advisers) in respect of our work or the report.

Important notice

Our report is designed to meet the agreed requirements of AGCC determined by their needs at the time. Our report should not therefore be regarded as suitable to be used or relied on by any party wishing to acquire rights against us other than the AGCC for any purpose or in any context. Should any party other than AGCC choose to rely on the report it does so at its own risk. We will accordingly accept no responsibility or liability in respect of it to persons other than the addressees of the report.

Our advice in this document is based upon the facts and assumptions as set out in this report. If any of the facts or assumptions are not entirely complete or correct then it is imperative that we are informed as any such inaccuracy or incompleteness could have a material effect on our conclusions.

No inference should be drawn from the use of the words 'will', 'should', etc, as they relate to the relative strengths of a particular position outlined in each document. Each of the positions described in the document entails certain risks.

Yours faithfully

KPMG Channel Islands Limited

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Key Individual Concept / Central Management and Control

■ Overview

- The Key Individual Concept (“KIC”) applied by Alderney Gambling Control Commission (“AGCC”) is used to identify someone associated with an eGambling licensee who acts in a managerial position or performs functions identified by the licensee or AGCC as key. Crucially, this is not restricted to individuals employed directly by the company but can also apply to people who operate under a Service Level Agreement (“SLA”) with an entity connected to the licensee providing advice to the Board of the licensee.
- The identification of key individuals can conflict with HMRC’s policy of Central Management and Control (“CMC”) and cause suspicion with HMRC to the effective tax location of the business.
- If HMRC successfully argue that the CMC of a company is in the UK then that company will become taxable under UK tax law.

■ Aim

- This report aims to explain how the KIC can affect the tax residency of eGaming companies with the risk of them becoming taxable in the UK; and
- offer measures in order to mitigate the risk of key individuals causing the CMC of eGaming companies to be deemed to be in the UK.

Key Individual Concept / Central Management and Control

■ Key Individual Concept

- An individual who has been identified either by a licensee or AGCC as occupying a key position in relation to an eGaming company will need to apply for AGCC approval.
- A key individual recognised by AGCC is a person who is or will be:
 - someone who occupies or acts in a managerial position;
 - someone who carries out managerial functions; or
 - someone in a position to control or exercise significant influence over the operations, of an eGambling licensee or a foreign gambling associate certificate holder .

■ Central Management and Control

- Generally, a company's residence for tax purposes is determined by the location of its central management and control. Central management and control as defined by HMRC is taken to be in the country where the highest level of decision making in the company occurs, not where the day to day management is. Therefore, an Alderney incorporated eGaming company may be UK resident if:
 - important strategic decisions are made in the UK;
 - decisions regarding new acquisitions, financing or expansion plans are made at Board meetings in the UK;
 - chief operations of the company are controlled, managed and directed in the UK.

Key Individual Concept / Central Management and Control

■ Important Differences

- AGCC look to identify key individuals that influence the organisation within the group even if this individual is not directly employed by the company.
- HMRC seek to identify how and where key decisions of the legal entity are made and by whom. These decisions are usually made by the board of directors, or a group acting in that capacity, however, it is sometimes the case where specific directors hold more influence than others, and it is the decisions that they make that could determine the CMC of the company if they are made in the UK.
- It is possible that a person identified as a key individual within a group of companies for AGCC's purpose is not necessarily a director, quasi-director or 'shadow' director of the entity that holds the eGaming licence.
- HMRC seek to identify the decision making process of the company and also the manner in which the company acts on any advice it has obtained. AGCC, on the other hand, will also identify any key individuals outside of the legal entity that provide advice to the company. Therefore, it is important to communicate with HMRC that some key individuals may provide advice in the UK but the decision to act on the advice rests with the board.

Risks

- Some of the potential risks associated with the KIC are outlined below:
 - HMRC are aware of the KIC and can require information from a UK person under existing UK law and also Alderney persons under the UK/Guernsey Tax Information Exchange Agreement (“TIEA”). HMRC can only acquire information under the agreement by proving there is a sufficient body of evidence to warrant the information being exchanged.
 - If HMRC used this information to identify key individuals who are UK resident and subsequently successfully argue that the CMC is based in the UK, the company will become taxable in the UK.
 - An eGaming company considered to have UK tax residence would be subject to a potential corporation tax rate of 26% as opposed to a corporation tax rate of 0% in Alderney.
 - If an eGaming company registered in Alderney has influential personnel active in the UK, the maintenance of non-UK corporate residence will require careful management.
 - A key individual, as recognised by AGCC, who undertakes the role of a director, as recognised by HMRC, and exercises this role in the UK may cause HMRC to determine that the CMC is in the UK.
 - HMRC may not make the distinction between key individuals that are directly employed by the Alderney based company and a UK based ‘key individual’ not employed but under a service level agreement (“SLA”).

Ensuring non-UK tax residence

- There are a few steps that can be taken to strengthen a company's position against a residence challenge. These are as follows:
 - Directors should take all decisions affecting the key policy matters of the companies' business during board meetings outside of the UK.
 - Decisions affecting the companies' CMC should not be delegated to committees of the directors where the majority are located in the UK or who meet in the UK.
 - Transactions should be entered into following approval at board meetings.
 - Contracts should preferably be signed outside of the UK.
 - The boards of directors should be able to demonstrate that they are exercising full control over the companies. They must therefore ensure that no UK resident individuals or entities, either collectively or individually, can be seen as making key decisions on the direction of the companies.
 - The board should receive and review reports on the operations of the company, the state of its finances and its performance.
 - To the extent that there are UK based "key individuals", as recognised by AGCC, they should avoid holding a directorship position in the Alderney company.
 - It is acceptable for a Director to take advice from a UK based source but it is essential that the Director then has the choice on whether to act on this advice and the decision to act is made in Alderney

Conclusion

- The KIC used by AGCC may assist HMRC to identify individuals that are UK resident. If HMRC can demonstrate that these key individuals in the UK can override or usurp decisions affecting the direction of the company, it can shift the CMC of the company to the UK. The the company may then become taxable in the UK at a higher rate of corporation tax than Alderney.
- In order to strengthen eGaming companies' Alderney residence with HMRC, they should demonstrate that the CMC is in Alderney by preventing any key individuals, as recognised by the AGCC, that work in the UK from being on the board.
- eGaming companies should ensure all major decisions are decided upon at board meetings based outside the UK and should be wary of the influence of any UK based individuals or shareholders.
- Although these measure will help strengthen the companies stance, HMRC will take into account the overall affairs of a company in order to establish the location of its CMC.
- The rules surrounding CMC can be complicated, and the advice provided is of a general nature and is not intended to address the circumstances of a particular entity as HMRC will review each company on a case by case basis. If you would like us to review the position of a specific licensee company or you require further help or advice, please do not hesitate to contact us.

Thank you

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