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Taxud-E2 – [REDACTED]

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SUMMARY RECORD OF THE MEETING OF THE WORKING PARTY IV ON DIRECT TAXATION

*Review of the operation of the Council Directive 2003/48/EC on
taxation of income from savings*

Held in Brussels on 1 April 2008

B-1049 Brussels / Belgium. Room: MO59 [REDACTED] / [REDACTED]

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1. INTRODUCTION

The meeting of the Commission Working Party IV on Direct Taxation was attended by the appointed experts representing the Member States and was chaired by [REDACTED] [REDACTED] [REDACTED] [REDACTED] [REDACTED] [REDACTED] at the Directorate General Taxation and Customs Union of the Commission. The Chair welcomed the participants and presented agenda of the meeting.

The first part of the meeting was devoted to follow-up work by EU Clearing and Settlement Fiscal Compliance Experts' Group (hereinafter 'FISCO') on clearing and settlement whereas the second part dealt with the discussions on the review of the Savings Directive and exchange of letters between the Commission and Swiss Confederation on the application of the savings agreement.

2. FOLLOW-UP TO WORK ON CLEARING AND SETTLEMENT

The Commission services presented the findings and proposals by FISCO Group on the removal of fiscal compliance barriers to the post-trading of EU cross-border securities transactions. In particular, it addressed the proposals as provided for in the 2nd report of FISCO Group on the removal of Giovannini Barriers 11 and 12 on withholding and transaction tax procedure. On the basis of the findings and proposals by FISCO Group, the Commission services intend to adopt Commission recommendation on withholding and transaction tax procedure at the beginning of 2009.

FISCO Group has concluded that regimes requiring transaction tax to be collected by domestic settlement service providers may prevent foreign custodians from accepting securities subject to such transaction tax. In that regard it was suggested to ensure a level playing field for settlement service providers. With regard to simplification of withholding tax procedure FISCO Group inter alia recommends:

- Harmonisation of EU tax relief procedures
- Abolishing the requirement of paper-form certification and allowing intermediaries to make use of modern technology to pass information in electronic format
- Establishing of one-stop-shop in order to centralise refund procedures to one tax authority
- Establishing one-time limit for a refund application.

The Commission services briefly addressed global dimension of tax relief procedures noting that joint EU-OECD Working Group "Improving Procedures for Tax Relief for Cross-border Investors" has been recently established.

As the Commission proposals will serve as the basis for a Council recommendation, DE and ES suggested examining proposals in a joint meeting of FISCO Group and tax experts. Moreover EL suggested discussing any tax issues at the meeting of Council Working Party on Tax Questions – Direct Taxation. In response the Commission services confirmed openness for further consultations with all stakeholders. However, discussions at the Council Working Party could be held following the adoption of Commission recommendation.

Before concluding the discussion on the clearing and settlement, the Chair invited experts to submit written comments on the proposals made in the 2nd FISCO report by 30 of April at the

latest. The Commission services will keep MS informed on the follow-up work, including work of joint EU-OECD Working Group.

3. DISCUSSION ON THE REVIEW OF THE SAVINGS DIRECTIVE

The Chair shortly introduced with the background documents summarising opinions expressed during 2007 in the Commission Experts Working Group on Taxation of Savings (hereinafter 'EUSD Expert Group') and comments from the MS on the questions concerning the review of the operation of the Directive. ■ gave a brief overview on Commission services' working document "Review of the operation of the Council Directive 2003/48/EC on taxation of income from savings" (hereinafter 'working document'). The experts were invited to submit written comments on the working document as well as any clarifications on the Commission services' draft summary document on the comments received from the MS.

3.1. DISCUSSION ON THE ROOM DOCUMENT

During the meeting room document on the review of the Directive (hereinafter 'room document') was briefly introduced by DE. It recalled the discussion at the ECOFIN held on 5 March 2008 on the need to improve the effectiveness of the Directive. In that respect the room document suggests the following:

- Extending the scope of the Directive to all types of investment income, especially life insurance products, derivatives and structured products
- Inclusion of the legal vehicles that can be used for avoiding the Directive such as offshore companies, trusts, specialised investment funds and foundations
- Extending the geographical scope to the third countries by negotiating measures having equivalent effect to the Directive.

With regard to the 3rd point of the room document BE recalled the discussion in ECOFIN held on 5 March 2008 concerning the difficulty of extending measures having equivalent effect to the Directive to the 3rd country financial centres as long as their domestic tax systems are not changed. It noted that suggestions under the 1st point of the room document concerning the extension of the scope of the Directive to life insurance products, non-UCITS and structured financial products are the most realistic ones provided that unanimity is reached by the MS. Nevertheless, it questioned the reference in the 1st paragraph that risk capital is not subject to effective taxation noting that discrepancies derive from the lack of harmonisation of the MS' tax systems rather than lack of effective taxation as such. In that regard the Chair clarified that the Directive aims at effective taxation according to domestic tax laws of the MS. With regard to question on follow-up work she responded that the Commission staff working document will be presented at the Council Working Party on Tax Questions – Direct Taxation held on 5 May 2008. Proposal of the amendments to the Directive is due to be presented on the 3rd or 4th quarter of 2008.

DK, ES, FR, IT and NL expressed general support for DE suggestions. In that regard FR urged the Commission services to speed up the work on the review of the Directive in order to present a proposal as soon as possible. It underlined the necessity to extend the scope of the Directive to other legal vehicles such as trusts and foundations used to avoid obligations under the Directive as well as to cover life insurance products, derivatives and non-UCITS. ES insisted on establishing a level playing field for financial market operators indicating that exclusion of certain financial products may lead to financial instruments market distortions.

NL added that extension of the scope of the Directive to all legal entities could be the most radical and the simplest solution at the same time.

IT underlined the importance of applying the Directive uniformly by all MS. Both IT and DK observed that extension of the scope of the Directive shall give rise to broader exchange of information by all MS rather than imposition of withholding tax.

UK noted that any amendments of the Directive shall be effective and simple as possible. In that regard it would favour clearer solutions than the principle “substance over form” such as broadening the definition of savings/investment income. It underlined the advantage of having a clear cut savings income definition over rather unclear notion of investment income. Further, the scope of the Directive could be extended to certain legal entities used as savings vehicles in order to tackle tax evasion. Finally, it noted that extension of the scope of the Directive to all kinds of insurance products rather than insurance products giving rise to interest income would make the reporting by paying agents less burdensome.

On chapter 6 of the working document LU disagreed with the Commission services’ analysis that withholding tax system is not equivalent to exchange of information system. It observed that OECD standards cannot be automatically applied within the Community. With regard to follow-up work it suggested continuation of work in the framework of the review of the Mutual Assistance Directive. Finally, it highlighted the importance of prior cost and benefit analysis allowing the measuring the effectiveness of the two systems in operation (exchange of information against withholding tax) before any proposals to amend the Directive are made.

AT confirmed its openness for further discussions on the extension of the scope of the Directive to legal entities. It added that exchange of information and withholding tax systems can be applied in parallel.

With regard to the review process of the Directive PL suggested proceeding in two phases: in the short term to work on improving effectiveness of the Directive within the present scope and in the long term to work on extending the scope of the Directive.

3.2. DISCUSSION ON THE WORKING DOCUMENT

3.2.1. Beneficial ownership

On chapter 2.1., the Commission services' working document suggests extending the scope of the Directive to payments which are made to entities and legal arrangements whose beneficial owner is an EU resident individual as identified under the Third Anti Money Laundering Directive. With regard to question raised by DE on the application of the concept of beneficial ownership to all types of entities including specialised collective investment funds in countries imposing withholding tax the Commission services noted that choice has to be made on the application of the Directive on upstream economic operator at the moment the interest payment is made or on downstream economic operator at the time of distribution of assets. Application of the Directive at the moment of distribution of assets has its merits since it is relevant moment for imposition of taxes in the most MS.

3.2.2. Definition of paying agent

On chapter 4.1, dealing with the extension of the "paying agents on receipt" provision to all transparent entities with the exception of UCITS, BE expressed concerns that establishing and updating of "positive list" of entities under the Comitology procedure would be too burdensome. In response, the Commission services referred to complaints by market operators that current application of "paying agents on receipt" provision is too burdensome on upstream economic operators.

UK observed that "paying agent on receipt" provision currently is of limited application and questioned the usefulness of having a "positive list" of entities concerned by Article 4(2). Nevertheless, such suggestion could be explored further as an alternative to look-through approach. Insofar as an official list is concerned IE would support establishing of a "positive list" under the Directive rather than under the Comitology procedure.

On chapter 4.2., the Commission services' draw attention to the fact that the position of discretionary trusts is similar to LH foundations as in both cases distributed assets have no link with the interest payment. It suggested imposing an obligation on trustee or manager of the foundations to exchange information or to withhold tax at the moment of the first distribution of assets. With regard to bare trusts UK disagreed with the analysis of the Commission services, observing that bare trusts are covered by the Directive not because of the look-through approach but due to the fact that settlor maintains control over a trust. UK raised the question whether the Directive could be applied to foundations by imposing an obligation on upstream economic operator as in case of bare trusts. It noted that difference between bare trusts and foundations lies in legal personality. In response the Commission services drew a link to chapter 2.1 of the working document dealing with application of look-through approach to entities established outside the EU noting that such a solution not necessarily is appropriate in the intra-community situation. There is a practical difficulty of imposing withholding tax at the moment interest payment is made since the beneficial owner is unknown. Application of the Directive at the moment of distribution of assets is feasible both for exchange of information and withholding tax systems.

DE underlined the necessity to cover under the Directive both entities which are recognised for tax purposes and entities which are not recognised for tax purposes. In case of entities not recognised for tax purposes, Directive would be applied at the moment the payment is made and in case of entities recognised for tax purposes, the Directive would be applied at the moment of distribution of assets.

On chapter 4.3., the Commission services' working document suggests an introduction of anti-abuse provision dealing with prevention of deliberate routing of interest payments through non-EU branches. On the Commission services' question concerning the MS' experience UK referred to the judgment delivered by UK tax commissioners requiring banks with head offices in UK to obtain any information which is in their power and possession. Banks are required to provide information which is in their power and possession outside UK jurisdiction, including branches and, eventually subsidiaries. In addition, voluntary disclosure scheme has been launched on reporting of income from offshore accounts without being subject to additional penalties. With regard to question on the compatibility of such measures with the banking secrecy provisions in the 3rd countries UK was not aware of any obstacles. The Chair noted that suggestions concerning prevention of routing interest payments through non-EU branch are of particular interest with regard to SG since banks with their headquarters in EU are usually established in the form of SG branch.

3.2.3. Definition of interest payment (Article 6)

On chapter 5.1, (also 3rd point of the exchange of letters between the Commission and Swiss Confederation), dealing with the application of the principle "substance over form" to structured financial products ES and DE questioned the feasibility of producing a comprehensive list of structured financial products concerned. Preferably, objective criteria need to be defined in order to keep in line with the developments of financial markets. In that regard the Commission services raised the point that producing of a "positive list" of structured financial products would result in greater legal certainty required by market operators.

With regard to chapter 5.2 dealing with the extension of the scope of the Directive to life insurance products the Commission services indicated the difficulty of maintaining a dual system of exchange of information and withholding tax system. In regard to point 1 of the room document DE suggested different approach for products which cannot be classified as insurance as such. In particular, life insurance policies with minimal cover and individual asset management by credit institutions should be treated in transparent manner. As the result, exchange of information or withholding tax would apply as soon as the income accrues to the insurance company provided that the income can be attributed to individual.

With regard to chapter 5.3, DK supported the Commission services' suggestion to work out a definition of collective investment vehicle on the basis provided by the 2002 OECD Model Agreement. The Commission services added that the extension of the definition to any kinds of collective investment funds for the purposes of the Directive eventually would facilitate a broader interpretation of the notion of "collective investment vehicle" as provided for in the EU savings agreements with the 3rd countries.

On chapter 5.5, ES supported the Commission services' suggestion that slight amendments to Art 8 of the Directive would be useful in order to clarify application of "home country rule" for collective investment vehicles. In regard to the list of service providers the Commission services clarified that number of MS provides for a list of reliable data providers for the convenience of paying agents. Establishment of reliable data providers under the Comitology procedure or adoption of more informal measure could facilitate uniform application of the provision.

3.2.4. Appropriate forms of cooperation for other products not covered by Article 6 of the Directive

With regard to chapter 6 the Commission services reminded that any suggestion to amend the Directive shall follow the structure of the Directive. As a paying agent is the last link in the chain of economic operators, only the companies making direct dividend payments could be considered as paying agents for the purposes of the Directive. With regard to DE suggestion to extend the scope of the Directive to all kind of investment income UK was reserved noting that requiring the companies to introduce reporting systems could be too burdensome.

Regarding IT question on the imposition of withholding tax on dividends at the level of paying agent, the Commission services were not aware of similar difficulties as in case of clearing and settlement service providers since the withholding tax under the Directive is applied at the last link of chain of intermediaries. The Commission services added that according to Article 16 of the Directive there is no interference between the withholding tax

under the Directive and withholding tax under the source country tax laws. Due to eventual economic double taxation of dividends in some MS it would be difficult to maintain a system of withholding tax for dividend payments. Therefore a system based on exchange of information would be more appropriate for dividend payments.

3.2.5. Improvements to the information reporting and exceptions to the withholding tax procedure (Articles 8 and 13)

With regard to chapter 8 dealing with exceptions to the withholding tax procedure BE was reserved to making voluntary disclosure procedure compulsory. It recalled the statement by the Minister of Finance that BE will apply exchange of information system as from 1 July 2011. The Commission services referred to the example of LU which has introduced both tax certificate and voluntary disclosure procedure. Further, it drew attention to the fact that problems associated with the certificate procedure have broader implications than suggested by BE, indicating the difficulty of obtaining tax refund in case tax residence does not coincide with permanent address of individual. Finally, it noted that the 3rd countries mostly use voluntary disclosure procedure since it is less burdensome for tax administrations.

Before concluding the discussions on the review of the Directive, the Chair thanked DE delegation for its room document and briefly reflected on the comments made by MS. She informed on the follow-up work on the Commission services' staff working document due to be presented at the Council Working Party on Tax Questions – Direct Taxation held on 5 May 2008. Finally, she asked the experts to submit comments on the working document by 24 April 2008 at the latest, as well as informed on the Commission services' intention to invite EUSD Expert Group for further comments.

3.3. EXCHANGE OF LETTERS BETWEEN THE COMMISSION AND SWISS CONFEDERATION

The Commission services briefly addressed three issues that were dealt in the exchange of letters between the Commission and CH - accession of BG and RO to the EU, exclusion of real estate funds from the scope of the savings agreement and exclusion of interest payments made to non-domiciled persons from the scope of the agreement. With regard to application of the savings agreement to non-domiciled persons CH raised the issue of level playing field as well as requested MS having non-domiciled systems to declare that revenue accrued is subject to withholding tax. In that regard UK and IE noted that as a matter of principle the Directive and the savings agreement shall equally apply to ordinary residents and non-domiciled persons. At the same time, they found it reasonable to request a special statement on liability to tax. The Commission services will contact MT on this issue as well.

4. FINAL REMARKS

Before concluding the meeting, the Chair thanked the experts for their contribution and informed on the follow-up work. If necessary, the following meeting of the Working Party IV on Direct Taxation will be held on 25 June 2008 and the meeting of EUSD Expert Group will be held on 29 May 2008. Finally, ■■■ asked the experts to make their best efforts in order to ensure that comments by the MS on the working document and DE room document are received by the Commission services by 24 April 2008 at the latest.