COMMISSION OF THE EUROPEAN COMMUNITIES

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COMMISSION STAFF WORKING DOCUMENT

Accompanying the

Proposal for a

COUNCIL DIRECTIVE

amending Council Directive 2003/48/EC on taxation of savings income in the form of interest payments

IMPACT ASSESSMENT

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1. SECTION 1: PROCEDURAL ISSUES AND CONSULTATIONS OF INTERESTED PARTIES

1.1. Organisation and timing

Council Directive 2003/48/EC on the taxation of savings income in the form of interest payments (the '2003 Directive') was adopted on 3 June 2003. Its ultimate aim is to enable savings income in the form of interest payments made in one Member State to beneficial owners who are individuals resident for tax purposes in another Member State to be made subject to effective taxation in their State of residence. The initially foreseen date of application (1 January 2005) was postponed until 1 July 2005. At that date Andorra, Liechtenstein, Monaco, San Marino and Switzerland started to apply equivalent measures to those of the 2003 Directive under Agreements signed between each one of these jurisdictions and the Community; at the same time all the relevant dependent or associated territories of the Netherlands and the UK (ten in all) started to apply the same measures as those of the 2003 Directive, under agreements signed by each of them with each of the Member States at the time.

Under Article 18 of the 2003 Directive the "*Commission shall report to the Council every three years on the operation of this Directive. On the basis of these reports, the Commission shall, where appropriate, propose to the Council any amendments to the Directive that prove necessary in order better to ensure effective taxation of savings income and to remove undesirable distortions of competition*".

Following the first revelations, in February this year, about fraud cases involving Liechtenstein, there was a debate at the Ecofin Council on 4 March 2008, and the Council *"…called on the Commission to accelerate preparation of a report on the implementation of the Directive 2003/48/EC since its entry into force on 1 July 2005… "*. It appears, some wealthy European individuals (over 1,000 in Germany alone), with the support of certain financial institutions, evaded taxes by investing in foundations in Liechtenstein since the early 2000s. The tax probe in Germany unveiled at least 50 foundations of German residents in Liechtenstein with millions of Euros in their accounts. Neither the current provisions of the 2003 Directive nor the equivalent measures included in the savings taxation agreement between the EC and Liechtenstein covered these cases.

On 29 April 2008 a Commission Staff Working Document [SEC(2008)559] entitled "Refining the present coverage of Council Directive 2003/48/EC on taxation of income from savings" was presented. This working document highlighted the main problems identified and possible solutions for refining the scope of the 2003 Directive. At the end of the document, a number of key issues needing clarification were listed. It served as basis for an oral report by the Commission to the Ecofin Council of 14 May 2008. It was further subject to discussions with a group of external experts (see 1.2 below), as well as with representatives of Member States at a more technical level, and was also put on the Commission website to enable comments from other stakeholders and interested parties.

The first formal report under Article 18 of the 2003 Directive was adopted by the Commission on 15 September 2008 [COM(2008)552], following a request included in the Council conclusions of 14 May 2008 to submit it to Council at the latest by 30 September.

The report is accompanied by a Commission Staff Working Document "presenting an economic evaluation of the effects of Council Directive 2003/48/EC on the basis of the available data" [SEC (2008)2420]. This working document provides quantitative approaches

to evaluate the functioning of the 2003 Directive. It analyses the evolution of certain proceeds from investments that are covered by the 2003 Directive or that contain elements falling within its scope. In addition, the analysis looks at the effects of the implementation of the 2003 Directive on some investment patterns. The last section of the document offers a statistical analysis of the impact of the introduction of the 2003 Directive on savings and on bank deposits.

There has not been an inter service steering group, but the inter service consultations on the above three documents have involved five Directorates-General (Internal Market, Legal Service, Economic and Financial affairs, Secretariat General and External Relations). And several Directorates-General have also been actively following the work of the group of external experts as well as the discussions with Member States in Commission technical working groups (see 1.2).

It should also be noted that the European Parliament resolution of 2 September 2008 on a coordinated strategy to improve the fight against fiscal fraud (2008/2033(INI))

"34. Points out that reform of Directive 2003/48/EC must tackle its various loopholes and deficiencies, as they prevent discovery of tax evasion and fiscal fraud operations;

35. Calls on the Commission, in the context of reform of Directive 2003/48/EC, to examine options for reform, including investigating some widening of the scope of the Directive with regard to types of legal entity and sources of financial revenue;"

1.2. Consultation and expertise

Early in 2007 a special *Expert Group on Taxation of Savings*, with tax experts from banking, insurance, investments funds, asset management and related sectors of the European Union, was set up to assist the Commission Services in their review of the functioning of the 2003 Directive. The Expert Group thus consisted of representatives not only from sectors which are directly concerned by the 2003 Directive, but also from sectors which provide other savings products or investment structures and which could conceivably become concerned, if the scope of the 2003 Directive were to be extended.

The Expert Group has met in Brussels four times between March 2007 and May 2008 and its mandate expires at the end of 2008. The objective of the group is to provide the Commission with the viewpoint of the European Union market operators on the application of the 2003 Directive in Member States and, at the same time, facilitate a first scrutiny of the possible impact on markets of any amendments to the Directive which could come up for consideration as a result of the review process. Also representatives of other Directorate Generals attended the meetings of the Expert Group and were informally consulted in the preparation of working documents submitted to the group.

In particular, the experts were asked to examine and comment on the main legal and practical issues of application of the Directive identified in the discussions with Member States as well as on other issues which were brought to the attention of the Commission services (through market operators, EC agreements partners, complaints etc.)

The various trade associations of European market operators were also asked to answer a quantitative questionnaire that was prepared with the cooperation of the European Banking Federation. More detailed information about the work of this Expert Group can be found on

the following webpage, where there is a special section devoted to the "Savings Directive Review", created in the first semester of 2007:

http://ec.europa.eu/taxation_customs/taxation/personal_tax/savings_tax/savings_directive_review/index_en.htm

> On that webpage i.a. the following documents can be found: a document prepared by the Commission Services (early 2007) with 26 questions on policy issues to the experts; the written contributions from the experts and from their trade associations in response to those questions; a summary made by the Commission services of the contributions thus made from the trade associations; summary meeting records; a quantitative questionnaire and a revised version of this questionnaire prepared with the cooperation of the European Banking Federation and taking into account the suggestions of this and other associations; the responses received, from eight trade associations, to this revised questionnaire (see *tables 2.31 and 2.3.2*); a working document by the Commission services of 27 March 2008 for a meeting with experts from Member States (and also discussed in the Expert Group); contributions from a number of the experts in response to that document; and contributions notably from the European Banking Federation (of 3 July 2008), Comité Européen des Assurances (of 28 May 2008 and 3 October 2008) and the European Fund and Asset Management Association (10 September 2008) on additional issues which they consider relevant for the Commission's assessment of the operation of the 2003 Directive and its future possible developments, taking into account the discussions during spring/early summer this year. On the webpage all interested parties have been invited to make contributions to the review process and a special e-mail address has been provided for that purpose. – However, very few contributions or questions were received in that way.

Informal meetings have also been held with interested parties to capture their views and sound out any problems they have encountered. Furthermore, the 2003 Directive has been discussed at a number of seminars and conferences (most recently at the Annual Congress of the International Fiscal Association in Brussels in early September 2008).

Starting already in 2005, Commission staff have also been examining the operation of the 2003 Directive and its interpretation with experts from the tax administrations of Member States in two Commission working groups, *Working Party IV on Direct Taxation*, and the *Working Group "Administrative Cooperation in the field of Direct Taxation"*. The first group has concentrated on the legal and practical issues related to the substantial content of the 2003 Directive. The latter group has helped ensure a monitoring of the correct implementation of the Directive concerning exchange of information and transfer of funds relating to the revenue sharing arrangements between Member States. It has also helped develop the format for information exchange.

The Commission's standards on consultations have thus been met.

1.3. Data availability

In order to properly assess the functioning of the 2003 Directive and to be able to prepare the reports that the Commission has to present to the Council every 3 years pursuant to Article 18, the Commission needs to receive relevant statistics from Member States and market operators. However, the 2003 Directive currently does not contain provisions requiring either the Member States or market operators to provide any statistical data.

Against this background, the Council, on 26 May 2008, adopted conclusions with respect to the list of Statistics that Member States should send to the Commission every year to facilitate its analysis. These conclusions also committed Member States to complete, before 31 May 2008, the tables based on that list for the fiscal years of 2005 and 2006, in view of the first report that the Commission was asked to send to the Council in September 2008. The conclusions of the Council built on a staff working document of the Commission that defines the statistics to be provided on a voluntary basis by Member States and the other jurisdictions participating to the savings taxation measures. These include:

- For countries levying a withholding tax: the tax revenue shared;
- For countries exchanging information: the interest payments and sales proceeds reported ;
- The number of beneficial owners;
- The number of paying agents;
- The part of the total annual tax collected from resident taxpayers on interest payments made by domestic paying agents (optional) and
- The part of the total annual tax collected from resident taxpayers on interest payments made by foreign paying agents (optional).

Despite the efforts made by Member States and market operators to provide the Commission with statistics, the quality and quantity of the statistics received are not sufficient (and sometimes even inconsistent) to make a detailed quantitative analysis of the Directive during its first years of application.

In parallel, in the framework of the Expert Group on Savings, some of the market operators' associations provided the Commission with some start-up costs and recurrent costs for the application of the provisions of the 2003 Directive (See tables 2 and 3 below). However, the information provided does not cover the whole sector, is partial and is not really representative.

Finally, alternative data have been collected from Eurostat on the interest payments received by individuals as well as from the Bank for International Settlements on bilateral cross-border deposits in banks, but both categories include a mix of products or beneficial owners that are not covered by the Directive. Table 8 in the annex summarises the availability and shortcomings of those data.

The examination of the available data in the Commission Staff Working Document (SEC(2008)2420) presenting an economic evaluation of the effects of Council Directive 2003/48/EC does not establish that the application of the Directive led to any change in the geographical composition of interest-bearing savings.

The lack of quantitative data is not "per se" an obstacle to make a proper analysis of the problems identified during the consultation process held with Member States and market operators or to propose adequate solutions. Furthermore, there is a need to anticipate developments based on the input of the stakeholders, which clearly recognise the need for improvements in the system.

2. SECTION 2: PROBLEM DEFINITION

2.1. What is the issue or problem that may require action?

The ultimate aim of the 2003 Directive is to allow each Member State to apply its domestic tax provisions to its resident individuals on interest payments that these individuals receive from paying agents established in other Member States. To achieve this, the 2003 Directive builds on an automatic exchange of information between Member States on such payments. However, during a transitional period, three Member States (Austria, Belgium and Luxembourg) are allowed to apply a withholding tax and share the revenue with the Member State of residence of the individual concerned instead of providing information. The transitional period does not expire at a specific date but is linked to further conditions being fulfilled in relation to certain other jurisdictions. Under the Agreements for the same or equivalent measures to those of the 2003 Directive, mentioned above, the non-EU parties either provide information to the EU Member States or levy a withholding tax with revenue sharing.

Pursuing the aim of the 2003 Directive would require that interest payments obtained by an individual through an intermediate vehicle are given the same treatment as interest payments received directly by the individual. The same applies to those income payments that can be considered equivalent to interest payments because they arise from savings products with similar levels of risk and liquidity as debt claims. If **consistent treatment of other comparable situations** is not achieved**,** not only is the effectiveness of the Directive endangered, but there can be distortions in competition between comparable savings products and structures.

The 2003 Directive has only been in application for three years. The Council, when adopting the unanimous conclusions on 27 November 2000 (see description of option 2 in section 4.1 below), on what should be the coverage of the future Directive, made a deliberate choice of principle to limit the scope to interest payments (or payments of interest originating income from investment funds) made to individuals, and to rely on the cooperation of market operators acting as paying agents either at the moment when the interest is paid out to the beneficial owner or, under specific conditions, when the interest is received by the entity concerned ("paying agent on receipt"). But the wish to provide, as far as possible, simple and clear rules for these market operators led to the measures being drafted in a way which, unintentionally, further limited their actual coverage. In some cases, more attention seems to have been devoted to the formal aspects of transactions than to their economic substance and to the actual way in which the market operates. Conversely, provisions such as the so-called “paying agent on receipt” mechanism [Article 4(2)] seem not to have been fine-tuned so as to provide market operators with the degree of legal clarity needed to achieve the expected results. Article 4(2) currently defines this "paying agent on receipt" only in a residual way, by using a reference to conditions (lack of legal personality and benefits not taxed under the general rules for business taxation) which can be very difficult to assess, notably by the upstream economic operators which are given some obligations on the payments made to the entities concerned in cross-border situations.

The review process has shown that the coverage of the 2003 Directive is not as wide as was intended according to the unanimous Council conclusions of 27 November 2000, and that there are loopholes in the provisions of the Directive. Such loopholes are detrimental to the effectiveness of the 2003 Directive, whether it is applied in the form of automatic information exchange or, transitionally, through the levying of a withholding tax. Furthermore, experience

shows that some aspects of the 2003 Directive should be clarified to facilitate the application of its provisions by paying agents, thus reducing their administrative burden. This is notably the case, as indicated previously, for the special rule of paying agent on receipt in Article 4.2 of the Directive.

There is evidence that, for payments made within the European Union, the 2003 Directive can be circumvented by EU resident individual investors by:

1. making use of intermediate investment vehicles (legal persons or arrangements) which are not covered by the current formal definition of beneficial owner (that refers only to individuals) or which are not currently compelled to act as paying agents, and/or

2. rearranging their portfolio financial/investment in such a way that income remains outside the definition of interest payments under the Directive, whilst benefiting from limitations of risk, flexibility and agreed return on investment that are equivalent to debt claims.

In relation to the second issue, it should be recalled that the original choice to exclude all innovative financial products from the scope of the Directive (ECOFIN Council conclusions of May 1999 and November 2000) was accompanied by an express statement that this choice should be re-examined on the occasion of the first review of the Directive, the aim being to find a definition covering all securities that are equivalent to debt claims so as to ensure the effectiveness of the Directive in a changing environment and to prevent market distortions. It is also worth mentioning that domestic tax systems have evolved over the last few years to assimilate the treatment of income from some types of innovative financial products to interest from debt claims.

Besides the loopholes mentioned above, the consultation with market operators has also revealed that the application of the provisions of the Directive by paying agents may in certain cases be burdensome because of lack of clarity. "This is the case of (i) the definition of 'interest payment' and 'paying agent', (ii) the definition of 'residual entities' (i.e.: *the entities to be considered as paying agents upon receipt of an interest payment*) and (iii) the formulae that may be used in different Member States to determine whether a fund or a particular fund event falls under the Directive", as has been pointed out by the European Banking Federation (EBF), which represents most of the paying agents already involved in the application of the Directive across the EU.

Finally, it has to be mentioned that the Directive at present does not require Member States to provide the Commission with relevant statistics respectively on the information exchange or on the withholding tax aspects of the Directive. This lack of information makes it difficult to properly assess the effectiveness of the Directive.

The following table provides a list of the identified problems and/or loopholes in the current Directive according to their relevance and the need for action:

Table 1: Hierarchy of identified problems
1. Use of intermediary structures not covered by the present scope, notably some legal arrangements (which can't legally speaking be defined as "entities"), and lack of clarity on the paying agent upon receipt rule for the economic operators which are directly or indirectly involved (see option 3 in section 4)
2. Different treatment of investment funds which are not authorised UCITS in accordance with Directive 85/611/EEC ("non-UCITS"), depending simply on the legal form of these non-UCITS (incorporated always excluded from the scope of the 2003 Directive whilst non-incorporated are always included) (see options 2 and 3 in section 4)
3. Use of comparable products to debt claims (certain structured products and certain life insurance contracts) (see option 3 in section 4)
4. Deficiencies in the rules for identification of beneficial owners, notably concerning the determination of their residence for the purpose of the 2003 Directive (see option 3 in section 4)
5. Coping with the use of conduit vehicles established in third countries in a way which is coherent with freedom of capital movements (parallel need of replacing the certificate procedure to avoid the withholding tax with the simplest procedure of voluntary disclosure of information to the tax authorities) (see option 3 in section 4)
6. Lack of statistics from Member States. Too limited use of the Tax Identification Number of beneficial owners which makes the information more difficult to use by the Member State where they are resident (see option 3 in section 4)

2.2. What are the underlying drivers of the problem?

Recent events, such as the tax fraud cases in relation to Liechtenstein foundations, have demonstrated clearly how important it is to establish international cooperation with a view to preventing, in the direct taxation area, fraud and evasion linked to cross-border financial investments. The 2003 Directive, together with the related Agreements, should certainly be considered as an important step in this process, developing further the principles already provided for by Directive 77/799/EEC on mutual assistance between tax authorities in the field of direct taxation. This Directive is designed to allow the flow of information in relation to direct taxation (income tax, company tax and capital gains tax), together with Insurance Premium Tax, between the tax authorities of Member States. The Directive enables Member States to co-ordinate their investigative action against cross-border tax fraud and carry out more procedures on behalf of each other, but at present Member States are allowed to make the exchange of information conditional on some aspects of their internal law (e.g. confidentiality of bank information).

The 2003 Directive builds on the Mutual Assistance Directive but ensures cooperation independently of the existence of specific national conditions. It signifies an important step

forward in that, for the first time, a coordinated effort in the direct tax area has been agreed and simultaneously applied by a wide number of jurisdictions with different interests and traditions. However, it is clear that a further strengthening of the mutual assistance rules is needed to combat tax fraud and evasion.

In the era of globalisation, the relative ease with which customer relationships can be established and maintained via the internet and the advantage of open markets make Member States' tax systems more vulnerable to tax evasion. Even if it is difficult to make an estimation of the bulk of tax evasion involving territories not covered by the 2003 Directive or bilateral agreements on savings taxation, it was very apparent from the beginning that the savings taxation mechanism should be coupled with an extension of the same or equivalent measures to as many important financial centres as possible. This international aspect has been underlined by the Council's conclusions of 14 May 2008 on good governance in the tax area whereby the Commission has been mandated to ensure that relevant agreements with third countries contain clauses committing those countries to the principle of exchange of information.

It is difficult to make a proper assessment of the effects that any extension of the scope of the 2003 Directive could have on capital flight to third countries. As explained before in section 1.3, the examination of the available data does not establish that the application of the Directive led to any change in the geographical composition of interest-bearing savings. Although there appears to have been no major shifts in the composition of savings when viewed at macroeconomic level, both national administrations and operators have argued that improvements are needed either to deal with loopholes or to clarify procedures.

A recent study carried out in 2004 on elasticity of savings in the form of cross-border deposits in banks [1] concludes that:

(1) A 1% increase in the interest tax burden (defined as the interest rate time the tax rate) increases external deposits by about 2.4% (i.e. the capital flight is an additional 2.4%).

(2) The sensitivity of external depositing to the tax seems to be dependent on the level of interest rates. With low interest rates, the tax burden becomes small in percentage of the asset up to a point where depositors may become insensitive.

(3) There is little evidence that international information exchange has a strong impact on bilateral depositing.

It should however be noted that the study applies to international deposits that probably represent a small share of total savings in interest-bearing instruments and which may also be amongst the most mobile instruments. The study also refers to data for 1983-1999, a period prior to the implementation of the Savings Directive. Hence, the relevance of the study for the present context is subject to the Lucas Critique that the sensitivity may have decreased because of the existence of a new regulatory environment created by the adoption of the 2003 Savings Directive.

[1] Huizinga, H. and Nicodème, G. (2004). Are International Deposits Tax-Driven, Journal of Public Economics. 88(6): 1093-1118.

As explained in section 4, the different options have taken into account the international dimension of the 2003 Directive and in particular the need to prevent a possible relocation of savings to non-EU countries as a consequence of the strengthening of the measures inside the EU. Options 3 and 4 include the application of a look-through approach for entities and legal arrangements established in non-EU jurisdictions as long as they do not apply equivalent measures to those to be agreed at EU level in the field of taxation of savings.

2.3. Who is affected, in what ways, and to what extent?

The three main actors concerned with the application of the provisions of the Directive are: market operators, competent authorities of Member States and individuals resident in one Member State that obtain payment interests from paying agents in another Member State.

Market operators in the financial services sector are affected. This goes particularly for those who are obliged to act as paying agents, i.e., who are the last link in the chain of payments to an individual beneficial owner and therefore are obliged to report interest payments or to levy a withholding tax under the 2003 Directive (or the related Agreements). Some categories of market operators can be affected even when they do not act as paying agents. This is at present the case of UCITS that have to ensure that paying agents receive the information on the origin of their income and the composition of their assets which is necessary for correctly applying the provisions to interest payments.

It is difficult to provide exact figures of market operators who at present apply the provisions of the Directive in one way or other. Concerning the trade associations represented in the Expert group, one can note that the European Banking Federation (EBF) represents the interests of over 5,000 European banks, large and small, from 29 national Banking Associations (25 Member States plus 4 non-EU Member States), whilst the European Fund and Asset Management Association (EFAMA), through its 23 national member associations and over 40 corporate members, represents about EUR 15 trillion in assets under management, of which EUR 7.5 trillion is managed by around 46,000 investment funds (according to the figures provided by EFAMA in 2007).

In order to make an assessment of the administrative cost incurred by paying agents for the application of the provisions of the 2003 Directive, the Commission services asked the market operators' Associations represented in the Expert Group to provide information on costs incurred in connection to the implementation of the 2003 Directive. It has nevertheless proved to be difficult for these Associations to get comprehensive figures from their members that can be considered as representative of the situation of all the paying agents established in all Member States. The feedback received by various Associations from their members on estimates of specific start-up costs and annual recurring costs incurred by them was not sufficient to make any statistically firm conclusions and to provide the Commission services with reliable answers. For information, the available figures on the costs incurred by paying agents while applying the provisions of the Directive since 2005 are presented below:

2.3.1. Average start-up costs for the first application of the national measures for implementing the Savings Directive[2]

Table 2: Average start-up costs for the first application of the national measures for implementing the Savings Directive

AVERAGE START-UP COSTS	PER BUSINESS UNIT ACTING AS PAYING AGENT[3]	PER MEMBER STATE	SOURCE	PROFILE OF INDIVIDUAL RESPONDENTS	MEMBER STATES DETAILS
2005	EUR 2m	-	European Banking Federation (EBF), based on responses from 40 paying agents in 6 MS	Large banks, retail and private banking	Reporting MSs: - 2 big old MSs - 3 small old MSs - 1 small new MS
2005	-	Germany - EUR 193m for all credit institutions overhead inclusive; - EUR 123m overhead costs exclusive	IW Consult GmbH, Study[4] "Costs of red tape within the credit services sector", December 2006	Credit institutions	Reporting MS - Germany

Recently[5], the European Policy Forum presented its findings on the start-up costs of twelve paying agents from nine Member States (Belgium, Cyprus, the Czech Republic, Hungary, Ireland, Italy, Austria, Poland, the United Kingdom), plus Guernsey and Switzerland.

It is to be noted that the data obtained by the European Policy Forum differs substantially from the data submitted in response to the Commission services' Quantitative Questionnaire. According to the responses received by the European Policy Forum, the implementation costs appear to be much lower. Ten respondents placed their start-up costs below EUR 500.000, which was the smallest amount provided for in the predefined responses. Two respondents – indicated as being "large banks, renowned for their private wealth management businesses

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2 Based on data provided in response to the Quantitative Questionnaire (see p. 1.2), published on the Savings Directive Review website

3 A bank may have several business units acting as paying agent under the Directive

4 The study was commissioned by the associations of the German banking sector. The method of calculating the costs is based on the standard cost model proposed and adopted by the EU to measure administrative costs imposed by legislation

5 The findings of the "Savings Tax Directive review – looking at the views of paying agents and their compliance costs" were presented on 1 September 2008 at a Special Roundtable during the IFA Brussels Congress. This review has not been submitted officially to the Commission Services.

according to the source" - estimated the implementation costs to be between EUR 2.5m and 10m, that is the third predefined response. It should be noted that these costs could be even lower than EUR 500.000 and EUR 10m, due to the range in the predefined responses permitted.

2.3.2. *Average recurring costs per annum directly linked to the application of the national measures for implementing the Savings Directive* [6]

Table 3: Average recurring costs per annum directly linked to the application of the national measures for implementing the Savings Directive

AVERAGE RECURRING COSTS PER ANNUM	APPROXIMATE PER BUSINESS UNIT ACTING AS PAYING AGENT	SOURCE OF INFORMATION	PROFILE OF INDIVIDUAL RESPONDENTS	MEMBER STATES DETAILS
2005	EUR 100.000	EBF[7], based on responses from 6 paying agents in 2 countries	Large banks, retail and private banking	Reporting: - 1 big old MS - 1 small new MS
2006	EUR 100.000	EBF, based on responses from 36 paying agents in 3 countries	Large banks, retail and private banking	Reporting: - 1 big old MS - 1 small old MS - 1 small new MS
2007	EUR 100.000	EBF, based on responses from 16 paying agents in 3 countries	Large banks, retail and private banking	Reporting: - 1 big old MS - 2 small old MSs

The study of the European Policy Forum included as well a question on the average annual compliance costs arising from the implementation of the Directive. The responses it received also vary from the data obtained by the Commission Services so far. Thus, 11 respondents estimate these costs below EUR 1m, being the smallest amount provided for in the predefined responses permitted and only 1 respondent assesses this amount between EUR 1 – 2.5m. However, it should be noted that these costs could even be lower, due to the range in the permitted predefined responses, especially the high level of the lowest amount (EUR 1m).

6 Based on data provided in response to the Quantitative Questionnaire (see p.1.2), published on the Savings Tax Directive website

7 Set up in 1960, the European Banking Federation represents the interests of over 5000 European banks, large and small, from 29 national Banking Associations, with assets of more than EUR 20 000 billion and over 2,3 million employees.

In response to the Commission Services' Quantitative Questionnaire, The European Association of Public Banks stated that it did not receive sufficient feedback allowing it to make any statistically firm conclusion. The European Fund and Asset Management Association also replied that the data required is not available to it. Furthermore, the International Swaps and Derivatives Association responded that the information required is sensitive, not readily available to its members and would require significant effort on the part of the industry to answer. The Society of Trust and Estate Practitioners drew attention to potential problems with incomplete data for discretionary trusts, which could lead to misleading conclusions.

On the basis of the above, it is currently not possible to provide any additional data on the start-up and compliance costs resulting from the application of national measures for implementing the 2003 Directive. This fact makes it difficult to estimate the costs that would be incurred by current paying agents, and by possible new paying agents, in the case of any possible amendment to the Directive to extend its scope.

Member States are affected given that the aim of the 2003 Directive is to enable them to levy the taxes that rightfully should accrue to them and thus to safeguard their revenue and the financing of their budgets. They are also affected through the bilateral Agreements they have concluded with the ten dependent and associated territories in relation to the same measures.

The following tables, extracted from the Commission Staff Working Document SEC(2008) 2420, present the available figures on the interest payments and sales proceeds reported by Member States using information exchange and the tax revenue shared by Member States applying a withholding tax during the second half of 2005 and 2006:

Table 4: Interest payments and sales proceeds reported by countries using information exchange

EU Member States	**2nd half 2005**	**2006**
Cyprus	n.a.	n.a.
Czech Republic	n.a.	17.81
Denmark	n.a.	1.16
Estonia	n.a.	4.40
Finland	n.a.	7.19
France	568.14	1512.54
Germany	660.73	1,392.06
Greece	6.85	23.11
Hungary	n.a.	n.a.
Ireland	258.87	770.72
Italy	n.a.	n.a.
Latvia	0.18	0.65
Lithuania	n.a.	0.09
Malta	1.02	2.10
Netherlands	n.a.	795.69
Poland	0.07	0.61
Portugal	n.a.	0.56
Spain	n.a.	n.a.
Sweden	n.a.	n.a.
Slovenia	n.a.	1.35
Slovakia	1.87	4.76
United Kingdom	9,132.49	n.a.
Total reported	**10,630.22**	**4,534.48**
		in million Euro

n.a. (not available)

If the very conservative assumption is made that the United Kingdom collected a similar amount for the fiscal year from 5 April 2006 to 30 June 2007 to what it collected for the period between 1 July 2005 and 4April 2006, the total amount for 2006/2007 would be 15,492.40 million Euros. It is important to highlight that the total amounts do not include some potentially important countries such as Spain or Italy for which data have still to be made officially available.

Table 5: Tax revenue shared by countries with withholding tax regimes

EU Member States	**2nd half 2005**	**2006**
Austria	9.48	44.32
Belgium	7.51	25.92
Luxembourg	35.90	124.59
Total	**52.89**	**194.83**
		in million Euro

The figure of 194.83 million in the second table corresponds to 75% of the withholding tax collected by the countries applying the withholding tax system. 25% of the total amount collected is kept by the Member State levying the withholding tax. Therefore, the total tax withheld in 2006 by the three Member States that apply a withholding tax during the transitional period is about 194.83 m x 4/3, i.e. about 260 m. Since the withholding tax in 2006 was 15%, the total withholding tax represents a total interest payment of about 260 x 100 / 15 = 1,773 m EUR or about 1.8 Billion EUR.

Finally, **individual taxpayers (beneficial owners)** are affected, although mostly in an indirect way as far as the 'honest taxpayers' are concerned, as the measures only aim at ensuring that they fulfil their obligations under their domestic tax rules relating to savings income These honest taxpayers have an actual interest in a correct functioning of the Directive, which can limit tax evasion and create the conditions for a balanced distribution of the tax burden.

However, there are certain rules which more directly affect individual taxpayers when it comes to the procedures for avoiding the levying of withholding taxes: the 2003 Directive provides for two possibilities in this respect, the so called voluntary disclosure and the possibility of providing a certificate issued the Member State of residence. Two of the Member States transitionally levying withholding tax have only provided for the latter procedure in their implementing legislation. This means that a beneficial owner wanting to avoid the withholding tax cannot simply authorise the paying agent to report the income but is obliged to get a specific certificate from the tax administration of his/her Member State of residence and provide that certificate to the paying agent. If the beneficial owner has difficulties in obtaining this certificate, the withholding tax is levied and can only be credited or refunded to him/her by the Member State where he/she is actually resident for tax purposes. With this certificate procedure, there can be situations where an individual who isn't actually resident for tax purposes in the EU could bear the withholding tax. It follows that this procedure is not compatible with even limited measures aimed at preventing a misuse of intermediate structures located outside the EU.

According to Member States, the number of beneficial owners resident in another Member State for whom their paying agents reported interest income in 2007 was 2,051,127. This

figure could include the same beneficial owner counted a number of times for different interest payments, in the absence of a more extensive use of the Tax Identification Number to identify the beneficial owner – See below the *options 2*, *3* and *4*.

2.4. How would the problem evolve, all things being equal? (N.B. Scenario(s) should take into account actions already taken or planned by the EU, Member States and other actors).

Any delay in finding an agreement between Member States (and, to the extent necessary, with non-EU territories and countries), on solutions for ensuring fairer and more consistent coverage of the savings taxation measures, could result in increased market distortions between comparable products and vehicles.

In this context, it is also worth mentioning that domestic tax systems have evolved over the last few years to assimilate the treatment of income from some types of innovative financial products to interest from debt claims.

For the three Member States entitled to the transitional regime (as well as for those non-EU territories and countries applying a withholding tax under the savings Agreements) the time constraint is of particular importance since the risk of distortion between comparable products will increase as the rate of the withholding tax, which was set at 15% for interest payments made until end June 2008, and which increased to 20% from that date on, will increase to 35% on interest payments made on or after 1 July 2011.

2.5. Does the EU have the right to act – Treaty base, 'necessity test' (subsidiarity) and fundamental rights limitation?

The evaluation of the 2003 Directive under the "'necessity test" and "fundamental rights' limitation" remains valid for the proposed amendments. In similar terms, the principle of proportionality is also very relevant for the evaluation of the Directive in view of any possible amendments to its provisions. In compliance with this principle, any possible action to amend the Directive and to extend its scope has to be limited to what is necessary to achieve the objectives set in Section 3.

The 2003 Directive is based on Article 94 of the EC Treaty and covers **cross-border** savings income and ensures a **common approach** for the reporting and, transitionally, for the levying of withholding tax, on such income. Such a common approach is particularly important since the measures rely on the paying agents (i.e. on market operators) for their application, and this would not be ensured through action at Member State level, which would also be less transparent.

The performance of Member States' tax systems could be significantly improved by more effective co-operation between Member States, and this could in turn help to keep economic activity and 'mobile' assets in the European Union, while avoiding the risk of further increasing the tax burden on less mobile bases such as labour.

The Community is a signatory to the Agreements with the five European non-EU countries on equivalent measures to those of the 2003 Directive. Furthermore, all Member States have concluded bilateral Agreements with the ten dependent and associated territories providing for the same measures as those of this Directive.

It should also be mentioned that pursuant to Council Conclusions of 23 October 2006, the Commission has been asked to conduct exploratory talks with other important financial centres (Hong Kong, Singapore and Macao) with an aim to further extend the geographical scope of the savings taxation measures.

Consideration has been given to aligning the forthcoming proposal to strengthen the general framework of administrative cooperation in the area of direct taxation provided for by Directive 77/799/EEC (as amended) on the positions taken in relation to the amendments to the 2003 Savings Directive. – See 4.1, *option 3* and *option 4*.

3. SECTION 3: OBJECTIVES

3.1. What are the general policy objectives?

The proposal aims at strengthening an already existing mechanism aimed at ensuring the possibility of domestic taxation of cross-border savings income in the Member State where the beneficial owner is resident in accordance with the domestic tax rules of that Member State.

3.2. What are the more specific/operational objectives?

The more specific objective of the proposal is to close loopholes in the existing legislation thus ensuring a level playing field by providing for consistent treatment of comparable situations in line with the principles of the Internal Market and of fair competition between comparable financial products and structures.

At the same time, the proposal provides the paying agents with tools to perform their tasks in a less burdensome manner; it thus seeks to reduce the scope (or need) for subjective judgements, thereby enhancing legal certainty, something which the market operators have been pressing for.

3.3. Are these objectives consistent with other EU policies and, if applicable, horizontal objectives, such as the Lisbon and Sustainable Development strategies or respect for fundamental rights?

The proposed amendments are coherent with the renewed Lisbon Strategy and address the need to preserve the competitiveness of the EU financial operators in the global market. Particular attention has been devoted to limiting any additional administrative burden on EU market operators and, where possible, to reduce the burden already put by the 2003 Directive on some of them.

4. SECTION 4: POLICY OPTIONS

4.1. What are the possible options for meeting the objectives and tackling the problem? Description of the different options

When assessing the various options, it should be kept in mind that the 2003 Directive essentially relies on paying agents for the execution of its provisions. Therefore, due account has to be taken of the Lisbon Strategy and the better regulation initiative, which involves, for example, reducing administrative burdens on and unnecessary costs for businesses. Member States should therefore be prepared to explore solutions whereby any additional

administrative burden for making the provisions of the Directive more effective would be placed as far as possible on the tax administrations, which would benefit from an increase in tax revenue, or on market operators that are currently less involved, rather than on those market operators (such as banks and asset managers) that already make an important contribution to the functioning of the Directive. Therefore, and taking into account possible additional costs for some of the operators and/or competent authorities of Member States, the principle of proportionality has to be particularly considered when assessing the different options.

Another constraint is the relatively limited territorial coverage of the 2003 Directive as well as of the Agreements providing for the same or equivalent measures.

The Commission continues to pursue the objective of promoting the application, by important non-EU financial centres, of measures equivalent to those applied by Member States and third parties participating in the savings taxation mechanism. However, as long as the geographical coverage of the savings taxation measures remains limited, it is also useful to consider, while having due regard to the free movement of capital laid down in the EC Treaty, whether measures should be taken aimed at tackling the attempts of EU resident individuals to circumvent the 2003 Directive by channelling interest payments, made in the EU, through "shell" entities or arrangements located outside the territory of the EU and of the jurisdictions cooperating with the EU.

The consultations with business and national administrations have mainly focused on the analysis of three essential elements of the Directive which have a decisive influence on its effectiveness, irrespective of the system under which the Directive is applied: (i) the definition of the beneficial owner; (ii) the definition of the paying agent and its obligations; and (iii) the definition of 'savings income'., and in particular that of an 'interest payment'.

A balanced solution thus needs to take into account all the three essential elements referred to above, namely "beneficial owner", "paying agent" and "savings income in the form of interest payments", as well as the administrative burden on paying agents and on Member States, the need to safeguard Member States' tax revenue and the competitiveness of the EU financial sector.

It should be recalled that the original choice to exclude all innovative financial products from the scope of the Directive (ECOFIN Council conclusions of May 1999 and November 2000) was accompanied by an express statement that this issue should be re-examined on the occasion of the first review of the Directive, the aim being to find a definition covering all securities that are equivalent to debt claims so as to ensure the effectiveness of the Directive in a changing environment and to prevent market distortions.

In addition to the above considerations there is the need for statistics in order to assess the functioning of the Directive.

Basically four main options have been considered, *option 1* being that of no action. Unlike *option 2,* which consists of closing unintentional loopholes and better coverage of savings products in line with the unanimous Council conclusions of 27 November 2000, *options 3 and 4* would mean a clear extension of the scope of the 2003 Directive. Under *options 3 and 4* there are in reality a number of choices. The possibility of including a limited number of legal persons could be discussed in connection with *option 3* (e.g transparent entities and entities

established in third jurisdictions that are not subject to taxation). For *option 4*, various combinations of 'savings products' could be considered.

Option 1 – No action

This option means that **no** amendments would be introduced into the 2003 Directive. The scope would remain more limited than was intended according to the Council conclusions of 27 November 2000. Nor would the unintentional loopholes be closed, and there would be no reduction in the current administrative burden.

Innovative financial products [including **structured securities]** were excluded from the scope of the 2003 Directive, and they would remain so.

Furthermore, in spite of certain evidence of market distortions, due to inconsistent treatment of similar savings products (for instance incorporated and non-incorporated non-UCITS), no action would be taken.

It would be worth mentioning that the European Banking Federation (EBF), which represents most of the paying agents involved in the application of the Directive across the EU, noted in its comments of 3 July 2008 that its members "share the opinion that the Directive remains unclear as for (i) the definition of 'interest payment' and 'paying agent', (ii) the definition of 'residual entities' and (iii) the formulae that may be used in different member states to determine whether a fund or a particular fund event falls under the Directive". The EBF also emphasised the importance of a level playing field covering the transactions which fall under the scope of the Directive.

Option 1 would also not ensure that the problem of lack of statistics from Member States is solved. Statistics would continue to be provided on an almost voluntary basis as provided by the Council conclusions of 26 May 2008.

Option 1	**Action**
No action	Maintaining the status quo, i.e. "Do nothing"

Option 2 – Amendments to ensure a better implementation of the unanimous agreement reached by the Council on 27 November 2000 about what should be the substantial content and aim of the Directive

The Directive builds on the consensus reached at the Santa Maria da Feira European Council of 19 and 20 June 2000 and the subsequent Ecofin Council meetings of 26 and 27 November, 13 December 2001 and 21 January 2003.

The 27 November 2000 Council meeting conclusions outlined the key principles of the Directive as adopted in 2003. According to these conclusions the following types of income should be exclusively considered within the scope for the purposes of the Directive:

a) Paid or account-registered interest relating to debt claim of every kind, whether or not secured by mortgage or whether or not carrying a right to participate in the debtor's profits, and in particular income from Government securities and income

from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures. Penalty charges for late payments are not considered as interest;

b) Accrued interest relating to products referred in a);

c) Capitalised interest relating to capitalisation products;

d) Income distributed by distribution coordinated UCI invested exclusively in rate products;

e) Income distributed by mixed distribution coordinated UCI;

f) Income relating to investments in coordinated capitalisation UCI more than 40% of the assets of which are invested in rate products, this threshold being lowered at the end of the transitional period to a level to be decided at a later date;

g) Interest paid directly to or credited to an account held by entities such as uncoordinated UCI ("non-UCITS"), partnerships, trusts and comparable undertakings.

The main text of the above mentioned 2000 Council conclusions explicitly indicates that the definition of paying agent must also cover "interest payments relating to the direct management of a portfolio or indirect management of a portfolio, whether by investment funds or similar investment structures (partnerships, trusts, investment clubs, etc.)". According to the following more detailed description made by the conclusion, this objective should be ensured through the application to some "entities" without legal personality and not subject to taxation of the special rule of paying agent on receipt. However, neither the Council conclusions nor the 2003 Directive seem to reflect an accurate consideration of the legal nature of trusts and of some partnerships, which are not entities but legal arrangements and cannot therefore be covered by the special rule of Article 4.2 of the 2003 Directive if the legal text only refers to entities and not also to legal arrangements.

A similar inconsistency arose for investment funds established in the EU. The lack of an explicit reference to non-UCITS with legal personality (like *SICAVs*) gives the result that interest income channelled through them is kept out from the scope whilst non-incorporated non-UCITS with the same composition of assets are always covered by the 2003 Directive, either as paying agents on receipt, or by having their income taken into consideration as income from authorised UCITS.

Option 2 basically means using the 27 November 2000 Council conclusions on what should have been the content of the then future Directive as a benchmark, seeking to close **unintentional** loopholes and extending the scope only to include savings products which are equivalent to debt-claim products and which it was the intention to cover according to the main principles stated in the unanimous Council conclusions. This would mean amending the 2003 Directive to cover all the EU collective investment vehicles (both UCITS and non-UCITS) irrespective of their legal form, so avoiding the current inconsistent treatment of non-UCITS (incorporated vs. non-incorporated).

Furthermore, option 2 consists of extending the rule of paying agent upon receipt of Article 4.2 of the Directive to the case of interest payments made not only to entities but also to arrangements (such as trusts) as it was in principle the Council's intention in 2000.

The amending proposal is also the occasion to take into account some suggestions from market operators like EBF (notably the "home country rule" for treating investment funds or a clearer exclusion of those banks which passively receive a payment on behalf of their customers from the paying agent obligations).

On the other hand, in the same way as for *option 1*, innovative financial instruments would not be included, nor would any insurance products, regardless of whether they cover virtually no risk and are of such a character that they could be assimilated to debt claims, or to UCITS and non-UCITS.

In its comments of 1 October 2007 (relating to a Commission working document) and 10 September 2008, the European Fund and Asset Management Association, EFAMA, stated that "if the scope of the Directive is to be extended to cover non-UCITS, it must be ensured that similar competing products targeted to retail investors, in particular structured bonds and unit-linked insurance products are included as well". It pointed to the Ecofin Council conclusions of 8 May 2007, inviting the Commission to review the consistency of EU legislation regarding the different types of retail investment products, so as to ensure a level playing field, and it went on to say that the Commission should have this in mind also when regulating tax issues.

The number of new actors that would be concerned by option 2 is difficult to estimate. In principle, the proposed amendments would only affect incorporated non-UCITS and trusts or similar arrangements established in a Member State.

Option 2	**Action**
Amendments to ensure better coverage according to the Council conclusions of 27.11.2000	Extension to all collective investments vehicles Extension of paying agent on receipt rule to arrangements (trusts)
Limiting the administrative burden for paying agents in the respect of the same conclusions	"Home country rule" and solution to the "passive receipt" issue

Option 3 – The same amendments as those under option 2, in combination with amendments to close loopholes and extend the coverage to certain other products which can be assimilated to debt claims or to interest-bearing instruments, notably certain insurance products with virtually no risk protection

Option 3 would mainly involve the solutions below. The opinion of market operators and of the competent authorities of Member States has been considered before presenting this option. The annex to this document provides a table with the positions of market operators and Member States in relation to the proposed amendments as discussed during the consultation period described in 1.2. As mentioned above (2.5) consideration has been given to aligning the forthcoming proposal to strengthen the general framework of administrative cooperation in the area of direct taxation under Directive 77/799/EEC (as amended) on the positions taken in relation to the amendments to the 2003 Savings Directive:

– extending the scope of the 2003 Directive to

  – include securities which are equivalent to debt claims from the point of view of the investor, because virtually all of the capital invested is protected at the end of the duration of the contract, and because the return on capital is defined at the issuing date although the product is not formally composed of debt claims;

  – include those life insurance contracts providing for very low biometric risk coverage and investing the capital in debt-claims, units/shares in investments funds or equivalent securities.

  Extending the scope to other savings products that are perceived by investors as comparable to debt-claims because of their low risk and their capital protection was discussed with market associations in order to avoid administrative burdens on paying agents. A reference to the "substance over form" principle for identifying these products was first suggested by the Commission as a more flexible approach to developments in the financial markets. However, economic operators objected to an open reference in the Directive to this principle arguing that it is not very feasible in practice. Other alternatives, such as lists of products to be included under the scope of the Directive and to be subject to review under a comitology procedure, were also dismissed because any procedure to update the list would be time consuming and not effective. Therefore, leaving aside the above solutions, option 3 would involve extending the scope to specific products that meet certain objective criteria, easy to be checked by paying agents that have not participated in the creation of the product.

– clarifying the situations where the 'paying agent on receipt' mechanism applies (cf. the quote from EBF above): besides trusts as described in option 2, this rule would also extend to transparent entities provided with legal personality.

  These transparent entities include foundations without charitable purposes. An example of the situations that would be covered is offered by Liechtenstein foundations. These legal persons are in principle covered by the agreement on savings signed with Liechtenstein as paying agents at the moment when they make an interest payment for the benefit of an individual resident in the EU. However, in practice, payments made by these foundations can very rarely be qualified as interest payments. The most effective way to ensure that interest income obtained through them by an individual is fully caught is obliging the foundation to act as a "paying agent on receipt".

  In order to facilitate the tasks of economic operators, a positive list with the entities and arrangements to be considered as paying agents on receipt would be included in the annexes to the Directive as suggested by market operators' associations represented in the Expert Group on Savings.

– introducing a 'look-through approach' in relation to selected jurisdictions outside the EU in order to ensure that the savings taxation measures cannot be avoided or circumvented by channelling payments through entities and legal arrangements in those jurisdictions which are not effectively taxed there.

  The 'look-through approach' consists of asking paying agents established in an EU Member State who are subject to the application of anti-money laundering

obligations, to use the information already available to them within this framework, insofar as it relates to the actual beneficial owner(s) of a payment made to specific kinds of legal persons or arrangements established in selected jurisdictions outside the EU, where appropriate and effective taxation of interest income paid to these kinds of legal persons or arrangements is not ensured. An indiscriminate extension of this approach, to all entities and legal arrangements in the EU, even if it refers to information already available to the paying agent, does not seem to an appropriate and proportionate solution as market operators' associations have pointed out. A selective approach concerning only payments to some non-EU legal structures could be easier to implement as it could be automatically applied through IT resources and would not raise the risk of duplicating paying agent responsibilities on the same interest payment within the EU. The paying agent would not need any cooperation of the selected jurisdictions outside the EU, as it would use the results of the Customer Due Diligence which it is already obliged to perform under the Third Anti-Money Laundering Directive (also applied in Liechtenstein as part of the EEA).

As in the case of paying agents on receipt, a positive list with categories of entities and arrangements, resident in non-EU jurisdictions which do not ensure their appropriate and effective taxation, would be included in the Annexes to reduce the uncertainties and limit the administrative burden.

Updating of the lists established for applying this option (paying agents on receipt and untaxed entities/ arrangements in third jurisdictions) would require regular amendments of the directive or, as a more practical alternative and as proposed under this option, the use of a committee with limited delegated powers.

Option 3 would include some further minor changes to facilitate the operation of the Directive for beneficial owners (elimination of the certificate procedure to avoid the transitional withholding tax in 3 Member States) and to obtain a more accurate and updated establishment of their residence as well as of their tax identification number (if any) on the basis of the information already available to the paying agent. In order to solve the problem of lack of information, MS would be required to submit to the Commission certain statistics on a yearly basis.

In addition to the new actors under option 2, the proposed amendments under this option would involve some life insurance providers. However, taking into account the specifically targeted life insurance contracts and the fact that the paying agent in the Directive is the last payer in the chain of payments (so it could be a bank already involved in the operation of the Directive rather than the life insurance company), the number of new actors concerned as paying agents should be rather limited.

Option 3	Action
Amendments to ensure extension of the current scope, to close loopholes and include some further savings products	Extension to all collective investments, securities equivalent to debt claims and life insurance products with low biometric risk Extension of the paying agent on receipt rule to arrangements (trusts) and certain transparent entities with legal personality (such as foundations) Look through approach for payments to certain structures established in certain third jurisdictions Other amendments: making more use of the available information for establishing the residence of the beneficial owner and eliminating the certificate procedure

Option 4 – Amendments to enlarge the scope of the Directive to include all legal persons and further savings products such as, notably dividend payments, any financial capital gains and/or insurance products.

At the Ecofin Council in March 2008, a number of Member States expressed their wish to extend the scope of the Savings Directive beyond the Council conclusions of 27 November 2000 and to include payments to legal persons and all other types of investment income (dividends, capital gains, "out payments" from genuine life insurance contracts and pension schemes etc.).

There are certain constraints to be considered as far as an extension of the scope to all savings products is concerned.

As mentioned, there are, transitionally, two different mechanisms in place under the Directive, automatic information exchange and the levying of a withholding tax. Withholding tax is not a suitable mechanism unless the net income to be taxed is known. While this is usually the case for interest income in the hands of individuals, it is but rarely so for some other forms of income, e.g., capital gains. Also, the rules on capital gains taxation vary considerably between Member States, as well as between different types of capital gains. Against this background, the levying of a withholding tax on the full sales proceeds would be disproportionate. Thus information exchange would appear, prima facie, to be the only mechanism which would be suitable for such savings products.

Under *option 4* the question therefore arises whether it would be appropriate to include all of the above savings products or only some (or one) of them within the scope of the savings taxation measures; one dimension of the question is to what extent the 2003 Directive is the appropriate instrument or a strengthening of the cooperation within the framework of Directive 77/799/EEC on mutual assistance would be a more appropriate instrument in order to prevent the unlawful non-reporting of these types of income by taxpayers in their state of residence.

Enlarging the scope to include dividends, especially if this includes dividends to corporate beneficial owners, as suggested by at least one Member State, could lead to multiple reporting

and to multiple layers of withholding tax. In particular, where there is an obvious risk of multiple layers of withholding tax, the general framework for administrative cooperation (Directive 77/799/EEC as amended), which builds solely on information exchange, would seem more appropriate.

Option 4	Action
Achieving the widest possible coverage of payments of savings income without any selectivity	Extension of the scope to payments to all legal persons and to all types of investment income (dividends, capital gains, "out payments" from genuine life insurance contracts and pension schemes, etc)

4.2. Which options have been discarded at an early stage and why?

For political reasons, the option of repealing the 2003 Directive has never been on the table. It took around ten years of discussions and negotiations to get the measures into place. They have only been in operation for three years. And this is the first review process, with another one due in three years' time. Furthermore, the Community and its Member States have entered into international Agreements on the same, or equivalent, measures. Currently, 42 jurisdictions are thus covered by the savings measures, and exploratory talks on such measures are ongoing with yet other jurisdictions, and negotiations are about to be launched with Norway.

In addition, it should be mentioned that the economic evaluation carried out (see SEC (2008)2420) shows a small shift in deposits of non-bank depositors from countries within the scope of the 2003 Directive towards third countries but it is impossible to link it directly to the implementation of the Directive as this development gradually took place in the years before the 2003 Directive came into force.

5. SECTION 5: ANALYSIS OF IMPACTS

5.1. Impacts of the different options

Option 1 – No action

Impacts from the point of view of:

a) **Market operators (paying agents)**: Even if in principle the no action option would avoid any new administrative costs for paying agents, the absence of clarity in the application of some of the current provisions of the Directive is also a problem for paying agents such as the lack of an explicit reference to a home country rule in the case of payments obtained through UCITS or the application of the special rule of paying agent on receipt of Article 4.2 of the Directive.

Furthermore, some of the existing loopholes in the Directive provide beneficial owners with incentives to invest in some products or through certain structures that have nothing to do with their financial return. By this, investors undermine fair

competition in the industry at EU level and with third countries which leads market distortions. As explained above the EBF has highlighted these problems to the Commission in the context of the Expert Group on savings taxation. (See description of option 1 in section 5.1)

b) **Competent authorities (Member States):** Current loopholes in the Directive result in budgetary losses that exceed any necessary administrative costs that could be involved by amending the Directive. Member States have underlined that according to their experience the lack of compliance by their taxpayers when it comes to cross-border savings income leads to a loss of tax revenue which may be substantial.

c) **Individuals (beneficial owners):** Indirectly, the continued existence of some loopholes in the Directive would have a negative impact in terms of fiscal pressure on diligent taxpayers and on taxpayers whose main income is subject to closer controls (i.e., labour income).

Option 2 – Amendments to ensure a better implementation of the unanimous agreement reached by the Council on 27 November 2000 about what should be the substantial content and aim of the Directive

Impacts from the point of view of:

a) **Market operators (paying agents)**: The introduction of the amendments would not involve onerous administrative costs for paying agents already covered by the 2003 Directive. Paying agent obligations would be imposed on some further market operators who would then incur administrative costs. However, their number would be relatively limited. The extension of the provisions of the Directive to incorporated non-UCITS would have a positive impact on competition in the investments funds industry, but would leave a competitive advantage to other products not covered under the Directive.

b) **Competent authorities (Member States):** The introduction of the proposed amendments would not be exceptionally onerous for the competent authorities. Any necessary costs should normally be outweighed by the positive impact on the budget because the coverage would be more complete.

c) **Individuals (beneficial owners):** Indirectly, reduction in the negative impact on diligent taxpayers and on taxpayers whose main income is subject to closer controls by increasing tax revenues from products and arrangements to be covered under the Directive (more horizontal equity). In accordance with the principle of horizontal equity, taxpayers who have the same level of similar income should pay the same amount of taxes**.**

Option 3 – The same amendments as those under option 2, in combination with amendments to close loopholes and extend the coverage to certain other products which can be assimilated to debt claims or to interest-bearing instruments, notably certain insurance products with virtually no risk protection

Impacts from the point of view of:

a) **Market operators (paying agents)**: Current paying agents would have to incur administrative costs to adapt their systems to the new scope of the Directive

(structured products and look-through approach). Paying agent on receipt obligations would be given to transparent entities with legal personality. Furthermore, since new products would fall within the scope (such as life insurance contracts without significant biometric risk coverage) new paying agents would have to introduce rules to apply, or to make possible the application of, the provisions of the Directive.

b) **Competent authorities (Member States):** Similarly to option 2, the introduction of the proposed amendments would involve administrative costs, but, again, these should normally be compensated through a more effective collection of tax revenue due.

The amendments regarding payments to legal entities and arrangements established outside the EU would better align the requirements of identification of beneficial owners under the 2003 Directive with those foreseen for anti money laundering purposes. Through this, third countries that act as shelters for EU residents would also be caught under the Directive.

The amendments regarding abolition of one of the two procedures to allow non-payment of withholding tax, namely exemption on the basis of a certificate submitted by the beneficial owner, would result in an additional burden for the tax administration of the State of the paying agent by the compulsory application of the voluntary disclosure and automatic information exchange procedure. However it would be more than balanced by the reduced burden on the State of residence of the beneficial owner as well as on the beneficial owner himself.

c) **Individuals (beneficial owners):** Indirectly, as the result of closing the identified loopholes, positive effect on horizontal equity between capital income and other type of income less movable and therefore, subject to closer supervision by the tax authorities.

Positive effect on the beneficial owners concerned of the elimination of the certificate procedure.

This option should ensure a fairer treatment between comparable products of the "interest family", thus reducing existing and potential distortions, and should improve the breadth of information available to MS administrations, thus improving their possibilities to collect tax. Costs for operators and administrations should be reduced where clarifications are being made to procedures.

Option 4 – Amendments to enlarge the scope of the Directive to include all legal persons and further savings products such as, notably dividend payments, any financial capital gains and/or insurance products

Impacts from the point of view of:

a) **Market operators (paying agents)**: This option would clearly involve more administrative costs for paying agents at the level of IT resources. The same interest payment could be reported many times. Some market operators in exchange of information countries expressed nevertheless sympathy for solutions which would not oblige them to make any selection of the information to be treated.

b) **Competent authorities (Member States):** The introduction of the proposed amendments could be excessively onerous for the competent authorities because of possible redundant information received at different stages on savings income. Furthermore, Member States that do not already have in place a system to collect information on payments of income that can be classified as dividends, capital gains and/or insurance products, will have more costs for the application of the new rules.

c) **Individuals (beneficial owners):** Indirectly, more enhanced positive effect than in option 3 on horizontal equity, if Member States are able to correctly treat the mass of information received.

As explained in the description of the option, the main pitfall is the possibility for redundancies of information and multiple layers of withholding taxes (which would almost certainly impose the abandonment of the transitional provisions at least on the new categories of income and payees covered) and the potentially disproportionate administrative burden this could impose.

Other effects

As in option 2 and 3, the amendments would have an impact on the agreements signed with non-EU jurisdictions for the application of the same or equivalent measures. (See "other considerations" below). Unlike in options 2 and 3, where the scope and functioning of the Directive is not substantially modified, in the case of option 4 any negotiation with third jurisdictions for a review of the Agreements, notably those agreements based on the levying of a withholding tax, would be significantly difficult and delicate.

5.2. Table 6: Impact table

Options	**Affected parties**	**Effect** Direct: D Indirect: I	**Impacts** Positive: + Strongly positive: ++ Negative: - Strongly negative: -- Neutral/marginal: ≈	**Impact Timing** One-off Short-term Medium-term Long-term On-going	**Impact Nature** Dynamic Static	**Impact Likelihood** Certain High Medium Low
No action	Market operators	D	- (Market distortions)	On-going	dynamic	high
			≈ (No additional costs)	on-going		
			- (Lack of clarity)	One-off	static	
	Competent Authorities	D	- (Budgetary loss)	on-going	dynamic	high
			≈ (no additional costs)			
			- (poor statistics)			
	Individuals	I	- Less horizontal equity			Medium
Amendments to ensure better coverage according to the Council conclusions of 27 November 2000	Market operators	D	+ (Less distortions)	Short-term	dynamic	certain
			- (higher costs)	On-going		high
			+ (More clarity)	One-off	static	
	Competent Authorities	D	+ (Budgetary protection)	on-going	dynamic	high
			- (Higher costs)			
			+ (better statistics)			
	Individuals	I	+ horizontal equity	Medium term		Medium

Amendments to ensure extension of the current scope, to close loopholes and include some further savings products, mainly in the hands of individuals	Market operators	D	++ (Less distortions)	Short-term	dynamic	certain
			- (higher costs)	On-going	dynamic	high
			+ (More clarity)	One-off	static	
	Competent Authorities	D	+ (Budgetary protection)	On-going	dynamic	high
			- (Higher costs)			
			+ Better statistics			
	Individuals	I	++ horizontal equity	Medium term		Medium
Amendments to enlarge the scope to legal persons and to a wide range of savings products	Market operators	D	+ (Less distortions)	Short-term	dynamic	certain
			- - (Higher costs)	On-going		high
			+ (More clarity)	One-off	static	
	Competent Authorities	D	++ (Budgetary protection)	on-going	dynamic	low
			- Redundancies	Short-term	dynamic	Medium
			- (Higher costs)	on-going	dynamic	high
			+ Better statistics			
	Individuals	D	- Multiple withholdings	on-going	dynamic	high
		I	++ horizontal equity	Medium term		Medium

5.3. Preferred option

In view of the above analysis, and as shown in the summary table, the third option, i.e. to amend the Directive to refine **the current scope, to close loopholes and include some further savings products, mainly in the hands of individuals and to clarify and simplify certain rules**, appears as the best option at present. The first option (i.e. no action) should be rejected for not closing the current loopholes in the Directive that have a negative impact on public revenues and on competition in the financial markets. Furthermore, as explained above,

the EBF considers that the Directive needs to be modified to clarify certain aspects and to remove the rule of paying agent on receipt unless it also applies to the agreements signed with Third Countries.

In comparison with option 2, the costs to be incurred by current paying agents and new paying agents should be outweighed by less distortion between products of similar characteristics and by a positive impact on the budget of Member States. Furthermore, trusts would be treated in the same terms as foundations and transparent entities that serve as special purpose vehicles for investments by individuals.

Option 4 would be more comprehensive than option 3 but its application would involve more costs and could also lead to redundancies of information and to double withholding (unless radical changes in the functioning of the Directive are accepted by the Member States admitted to the transitional regime). Furthermore, option 4 does not seem to respect the principle of proportionality since the additional burden and costs on both the competent authorities and the paying agents could go beyond what can be considered to be justified to achieve the objectives of the Directive. This has to be carefully considered in the present difficult situation of international financial markets On the other hand, the advantages that could be derived from option 3 would still justify the effort for all the actors concerned and therefore respect the principle of proportionality.

5.4. Other (general) considerations

The same or equivalent measures have also been applied since 1 July 2005 in 10 dependent and associated territories and in 5 European non-EU countries. Any amendment to the Directive would not be directly applicable to the 15 non-EU jurisdictions. Therefore, any amendments to the scope of the Directive, mainly those concerning the definition of interest payment, the beneficial owner and/or the paying agent on receipt rule, would make necessary a review of the agreements with the 10 dependent and associated jurisdictions that apply the same measures.

As far as the 5 non-EU countries that apply equivalent measures are concerned, the Council would have the last word on whether the agreements signed before 1 July 2005 with the 5 countries would still provide for equivalent measures to the amended Directive. However, it is the view of the Commission that some of the proposed amendments under option 2 and 3 (notably those related to making more effective the paying agent on receipt mechanism, which is currently not included in these agreements) and definitely all the proposed amendments under option 4, as long as the scope and the functioning of the Directive is substantially changed, could require a parallel change in the agreements signed with the 5 non-EU jurisdictions. The kind of changes in the agreements which would be linked to an extension to the agreements of option 4 would be particularly ambitious to achieve, even in the present political environment

In this respect it is important to highlight that in the opinion of the EBF, EU economic operators find themselves at a significant competitive disadvantage to economic operators in these 5 Third Countries because of the absence in the agreements of the "paying agent on receipt" rules. According to the EBF, this represents a serious failure to ensure a level playing field. Therefore, the EBF is strongly opposed to any extension of Article 4.2 without agreeing equivalent measures with the Third Countries concerned and also calls for the abolition of such a rule if the absence of equivalence persists.

As long as the 5 non-EU jurisdictions do not provide for the paying agent on receipt rule (and for un updating of that rule as far as the 10 dependent and associated territories are concerned), Options 3 and 4 propose to apply the look-through approach to some of the entities and legal arrangements established in these jurisdictions (such as trusts, Anstalten and Stiftungen)

6. SECTION 6: MONITORING AND EVALUATION

6.1. What are the core indicators of progress towards meeting the objectives

Less tax evasion and less distortion in the financial markets can be considered as the main objectives of the amendments to the Directive. When it comes to measuring progress it is difficult to set core indicators since we may not expect in the short-term quantification or even a quality assessment of these indicators. This task will rely on the quality and availability of statistics to be provided by Member States and market organisations in the future.

If it is difficult to have an indicator of tax evasion, increased tax revenues or increased tax bases corresponding to debt claim products and assimilated could be a good approximation to evaluate the reduction in tax evasion in Member States. However, it has to be considered that other variables such as interest rates and evolution of the real estate market may have an influence on this indicator. In broad terms the total amount of interest payments exchanged can be also a good indicator of the performance of the Directive in this area.

In relation to distortions in the financial markets, a good indicator may be possible changes, from before to after the application of the new amendments, in investors' decisions in respect of products covered by the Directive and those outside the scope.

Other indicators are administrative costs for both paying agents and competent authorities and quality of the information exchanged.

An improvement in the available statistics from Member States administrations will facilitate any evaluation.

The mandate of the Expert Group on Taxation of Savings should be extended beyond 31 December 2008 in order to set up a sort of permanent forum to discuss on the Directive and its impacts on market operators after the introduction of possible amendments to the Directive. If its mandate is actually extended, this group will be asked to provide data allowing examination of potential future substitution effects between comparable products.

6.2. What is the broad outline for possible monitoring and evaluation arrangements?

As foreseen in the Directive, the Commission has to report to the Council every three years on the operation of the Directive. The report is the basis for any proposal to amend the Directive. As it has been the case for the first report in 2008, the Commission will start discussions with all the parties involved on the application of the Directive, after the amendments will be introduced, to follow up the impact of the amendments.

7. HOW HAS THE OPINION OF THE IA BOARD BEEN TAKEN INTO ACCOUNT?

On 8 October 2008 the Impact Assessment Board (IAB) discussed the draft of the Impact Assessment (IA) report with the services of the author DG. Further to this meeting, the IAB adopted its opinion on the draft version of the IA on 10 October 2008.

The recommendations of the IAB (as explained below) were considered by the author DG, which led the author DG to introduce a number of changes to the original draft before sending a second version to the IAB:

1. Better description of the baseline scenario and of the main loopholes in the Directive. Clear overview of how different actors are affected.

Section 2 "problem definition" has been changed to provide a better definition of the current situation of the Directive and the main loopholes as discussed during the consultation process with Member States and market operators. A hierarchy of the identified problems has been included at the end of the section to facilitate the understanding by the reader as to the different problems and their relevance. Section 2.2 has been improved to provide more details on the external dimension of the Directive, on the link with the dialogue with important financial centres outside the EU and the consideration given to the risk of possible capital flights. The different options in section 4 have been modified to provide a better description of the impacts of the four options on the three main actors in the application of the provisions of the Directive: paying agents, tax authorities and individual taxpayers. The changes to the draft IA also include some definitions of technical terms, such as "look through approach" and "paying agent on receipt", to make the report more comprehensible.

2. Clear set of options in section 4

The description of the four options, with solutions to the identified problems, has been moved from section 5 to section 4. The differences between option 2 and option 3 have been clarified by explaining in more detail the content of the Council conclusions of 27 November 2000 used as benchmark.

3. Significant limitation of the availability of data

A new sub section 1.3 on "data availability" has been introduced to better reflect the information that has been received and considered in the analysis as well as to reflect the lack of sufficient information for a quantitative analysis and the impact of this lack. See also table 8 in the annex.

4. Overview of the input received from stakeholders

A more detailed explanation has been given of the view of market operators and how these views have been taken into account in the different options. Table 7 with the opinions of Member States and market operators to the suggestions under the preferred option (option 3) has been modified accordingly.

Other recommendations in the Impact Assessment Quality Check list that was received previously to the IAB meeting have also been taken into account (notably in sections 5.3 and 6.1)

On 17 October 2008, the IAB adopted its opinion on the second draft version of the IA report. The recommendations of the IAB have been considered as follows in this final third version:

1. In relation to the recommendation to strengthen the link between the statement "data does not establish that the application of the Directive led to any change in the geographical composition of interest-bearing" and the need for immediate action, mention has been made of the views of national administrations and operators that improvements are in any case needed (Recommendation 1);

2. Table 1 with the hierarchy of identified problems has been supplemented with cross-references to the different options in section 4. These links will allow a better understanding of the relationship between identified problems and proposed solutions (Recommendation 1);

3. The recommendation of the IAB to indicate the extent to which the input received from stakeholders has been taken into account does not need further development in the view of the author DG. In fact, the descriptions of option 1 and 2 in section 4 provide the view of some of the operators (namely EBF and EFAMA) on the proposed solutions and table 7 in the annex describes the position of tax administrations and operators on the solutions provided in option 3 (the preferred option).The advantages and disadvantages of option 4 from the viewpoint of tax administrations and operators are also summarised in section 4 (Recommendation 2).

4. Option 3 in section 4 has been improved by describing the possible options (and the preferred one) for updating the "positive lists"; (Recommendation 2)

5. In relation to the consequences of the insufficient availability of data, it has been clarified at the end of section 1.3 that there is a need to anticipate developments based on the input of the stakeholders. The lack of quantitative data should not be a deterrent to act. In section 6.2 it has been clarified that the expert group s on savings taxation will be asked to provide data which are useful to examine the potential future substitution effects between comparable products (Recommendation 3).

6. Concerning the need to further elaborate on budget consequences for MS and operators, even if this is impossible to quantify, a new paragraph has been introduced at the end of the description of option 3 in section 4; (Recommendation 3)

7. Section 6.3 has become the new section 7. (See point D "procedure and presentation")

Annex

Table 7: Positions of Member States and Market operators on amendments proposed in option 3

Proposal	Favourable	Non favourable	Comments
Extending the scope of the 2003 Directive to include securities equivalent to debt claims (with substantial capital protection)	Large majority of MS Most economic operators	1 MS The industry of the innovative financial products (reluctance)	– No special comment from the MS against – Economic operators' view is that the extension has to be made with total clarity on which financial products will be brought within the scope. It can be acceptable only if the need of paying agents for simple tracking of the securities concerned is taken into account. The industry specialized in the creation of innovative financial products would have to be charged with this tracking of the securities concerned to the benefit of downstream paying agents, this would be possible only for newly issued securities

Proposal	Favourable	Non favourable	Comments
Extending the scope of the 2003 Directive to include those life insurance contracts providing for very low biometric risk coverage and investing in debt claims and equivalents funds and securities	A majority of MS Most economic operators	Some MS Insurance operators	– Some MS reserved their position about the best legal instrument (Savings Directive or mutual assistance Directive) – Many insurance operators would prefer cooperation under a single instrument for all insurance products, but the Savings Directive doesn't seem the appropriate instrument for this purpose and another solution could take time to be found and to be possibly agreed with non-EU countries, leaving room for distortions in competition – Tax treatment of these products is not consistent in all MS. Different views on whether the exclusion of these products at present leads to distortions – Practical difficulties to set criteria for low biometric risk coverage

Proposal	Favourable	Non favourable	Comments
Clarifying the situations where the paying agent on receipt mechanism applies (Article 4.2)	Large majority of MS (a few MS reserved their positions) Most operators, however the EBF prefers to abolish the mechanism if it is not extended to third countries	1 MS	– Doubts on the application to discretionary trusts – Most economic operators ask for a positive list of entities and arrangements concerned if the measure is to be retained and/or extended
Introducing a look-through approach in relation to selected jurisdictions	Large majority of Member States	2 MS Most economic operators	– Some" favourable" MS would even like to apply the look-through approach to all legal persons, entities and arrangements, and even resident in any EU MS – Economic operators fear that this could erode competitive position of EU paying agents. In any case, in favour of a positive list and application limited to entities and legal arrangements established in third countries

Table 8: data availability and shortcomings

Provider	Description	Shortcomings
Bank for International Settlement (BIS)	– Quarterly data on bilateral cross-border deposits by banks and non-banks for 40 reporting countries. Non-bank depositors include individuals, public institutions and businesses (non-bank financial institutions such as mutual funds, hedge funds and insurance companies). – A country breakdown with regard to the country of residence of the beneficial owner is available. – From the Q1 2000 to Q4 2007. – Geographical scope includes third countries that are known to attract savings such as Switzerland, Cayman Islands, Bermudas, etc. Singapore and Macao and partially Japan did not provide any data	– Not all EU-Member States are included. – No split between deposits from individuals (covered by the Directive) and from companies (not covered). – Dataset mainly covers one instrument (deposits) whose share in the total savings might be small.

Provider	Description	Shortcomings
EUROSTAT	– National accounts data on aggregated interest income split by source country is available. – 1995 to 2006 for EU-27 with some gaps	– Only for Member States. Available Data stems from the national authorities. – Definition of interest payments according to the national accounts is not identical to the definition of interest payments in the Savings Directive. – Covers both interest from foreign (covered by Directive) and domestic (not covered) sources.
Member States and territories where Directive is applied	– Bilateral data on information exchange and tax withhold (when applicable). – Number of beneficial owners, residual entities, paying agents, and number of records exchanged between countries – Available for the second half of 2005 and for 2006.	– Data quality is partly unsatisfying as many data are still missing and awaited from Member States. – Cannot be used to evaluate the impact of the Directive on investment and tax evasion since it provides only the data that are actually exchanged.