

INCEPTION IMPACT ASSESSMENT

Inception Impact Assessments aim to inform citizens and stakeholders about the Commission's plans in order to allow them to provide feedback on the intended initiative and to participate effectively in future consultation activities. Citizens and stakeholders are in particular invited to provide views on the Commission's understanding of the problem and possible solutions and to make available any relevant information that they may have, including on possible impacts of the different options.

TITLE OF THE INITIATIVE	New EU system for the avoidance of double taxation and prevention of tax abuse in the field of withholding taxes
LEAD DG (RESPONSIBLE UNIT)	DG TAXUD.D.2. Coordinated with DG FISMA units B1 and B4
LIKELY TYPE OF INITIATIVE	Council Directive
INDICATIVE PLANNING	By Q4 2022
ADDITIONAL INFORMATION	Action Plan for fair and simple taxation supporting the recovery strategy A Capital Markets Union for people and businesses-new action plan

The Inception Impact Assessment is provided for information purposes only. It does not prejudice the final decision of the Commission on whether this initiative will be pursued or on its final content. All elements of the initiative described by the Inception impact assessment, including its timing, are subject to change.

A. Context, Problem definition and Subsidiarity Check

Context

The [political guidelines for the current Commission's mandate](#) call for fair taxation and fight against tax fraud, as key foundations of an economy that works for people. They also state the importance of removing all barriers to the completion of the Capital Markets Union (CMU) and supporting businesses and citizens' investments alike across Europe. In this context, fostering cross-border investment, tackling tax fraud and simplifying taxation feature high among the Commission's priorities. The European Commission has already undertaken certain actions to address tax barriers to cross-border investment and the risk of tax abuse within the European Union. [In 2009, the European Commission adopted a recommendation](#) that outlined how EU Member States could simplify procedures for claiming cross-border withholding tax relief and which contained measures to eliminate the tax barriers that financial institutions faced in their securities investment activities, while at the same time protecting tax revenues against abuse. [In 2017, the European Commission published a Code of Conduct](#) which put forward new guidelines on withholding tax to help Member States reduce costs and simplify procedures for cross-border investors in the EU. The implementation of the Code of Conduct was voluntary for Member States with the Code outlining a range of practical ways for Member States to introduce quick, simplified and standardised withholding tax relief procedures that reduce the challenges faced by smaller investors when doing business cross-border.

Despite these actions by the European Commission, tax barriers to cross-border investment and the risk of tax abuse persist within the European Union. One of these remaining barriers is the problem of inefficient withholding tax relief procedures. According to the most recent publicly available data from 2016 costs related to withholding tax refund procedures, foregone tax relief and opportunity costs are estimated to a value of EUR 8.4 billion annually.¹ The [Action Plan for fair and simple taxation supporting the recovery strategy](#)² proposes to introduce a common, standardised EU-wide system for withholding tax relief at source coupled with a new exchange of information and cooperation mechanism between administrations. Alleviating the tax-associated burden in cross-border investment is also one of the actions put forward in the [Capital Markets Union for people and businesses-new action plan](#)³.

¹ See COM(2017) 147 final and SWD(2016) 146 final. See also for the methodology the underlying study from 2009: https://ec.europa.eu/info/sites/default/files/booklet-fisco-09022010_en.pdf

² COM(2020) 312 final

³ COM(2020) 590 final

Problem the initiative aims to tackle

The problem this initiative aims to tackle is the particularly burdensome withholding tax relief procedures for cross-border investors in the securities market. The stakeholders within scope of this initiative are primarily cross-border portfolio investors⁴. When an EU resident makes an investment in securities in another Member State, the payments received in return (dividends or interest) are normally subject to a withholding tax in the country of the investment (source country), at a rate which is often higher than the reduced rate on the basis of an applicable bilateral Double Taxation Convention (DTC). Where this applies, in order to eliminate the double taxation, the non-resident investor is then required to submit ex-post a refund claim of the excess tax withheld by the source country. The current procedures can be abused as shown recently by an investigation carried out by a consortium of investigative journalists that reported the existence of an alleged large-scale tax fraud known as “Cum/Ex” scheme and subsequent “Cum/Cum” Scheme in some EU Member States⁵.

In addition, such withholding tax relief mechanisms for cross-border payments have proved to be lengthy, resource-intensive and costly for both investors and tax administrations due to the lack of digitalized procedures and the existence of complex and divergent forms across Member States. In some cases, these high costs drive non-resident taxpayers to forego their right to apply for the tax treaty benefits that they are entitled to, thereby leading to double taxation and as a consequence to less attractive net returns than for domestic investments. The existence of inefficient, burdensome and costly procedures for the recovery of excess tax paid in a cross-border context discourages cross-border investment in the Union.

From the point of view of the Capital Markets Union, inefficient withholding tax relief procedures are one of the main barriers that deter people to invest across borders and hence to free movement of capital and capital market integration. In particular, burdensome procedures for withholding tax have long been identified as a barrier to achieving a single European securities market because they disrupt financial processes and increase the cost of cross-border trading, undermining investment within the EU⁶. They have been identified as particularly burdensome for individual and small investors.

In the aftermath of the Covid-19 crisis, the goal of streamlining the withholding tax relief procedures will be even more important for the economic recovery, as there is a strong need for investment (private as well as public) throughout the EU.

Basis for EU intervention (legal basis and subsidiarity check)

The legal basis for this initiative is Article 115 of the Treaty on the Functioning of the European Union (TFEU) which stipulates that EU action in the field of direct taxation is well-grounded where the functioning of the internal market would be hampered by the persistence of uncoordinated national legislation.

The initiative has a cross-border dimension as it concerns the procedures for relieving from withholding tax of dividend and/or interest payments on investments made in the source country by a non-resident investor. As it is the co-existence of different procedures and forms to be used in different Member States which makes existing withholding tax relief procedures inefficient, it is clear that the problem cannot be solved at an individual Member State's level. Also, in order to ensure that out-of-state investors from all other Member States are treated equally, bilateral DTC cannot solve the issue. Acting at EU level would offer an efficient holistic solution to a common problem relevant for all Member States in a cross-border context, as it would allow for the introduction of single, streamlined and simplified withholding tax relief procedures for non-resident investors. Avoiding duplication and inconsistencies among national practices is essential when it comes to streamlining administrative procedures across the EU. An EU initiative could be expected to significantly lower costs related to withholding tax relief procedures for cross-border investors, ensure a well-functioning internal market, and to prevent tax abuse.

B. Objectives and Policy options

The general objectives of the initiative are to ensure the proper functioning of the Capital Markets Union, to facilitate cross-border investment and to prevent tax abuse. This initiative has the specific objectives of making withholding tax relief procedures for non-resident investors more efficient and of increasing the ability of tax

⁴ Portfolio investment is defined as cross border transactions and positions involving debt or equity securities, other than those included in direct investment or reserve assets.

⁵ More information about “cum-ex scandal” can be found at the website of the European Securities and Markets Authority (ESMA) and in its report: https://www.esma.europa.eu/sites/default/files/library/esma70-155-10272_final_report_on_cum_ex_and_other_multiple_withholding_tax_reclaim_schemes.pdf

⁶ Final report of the High Level Forum on the Capital Markets Union - A new vision for Europe's capital markets (https://ec.europa.eu/info/sites/default/files/business_economy_euro/growth_and_investment/documents/200610-cmu-high-level-forum-final-report_en.pdf)

administrations, to identify and target investors that abuse rights granted under DTC's. The baseline scenario used as a benchmark will consider that the current legislative rules and national administrative practices on withholding tax relief procedures remain unchanged. The Commission will consider policy options, including legislation, to achieve the before-mentioned objectives while adhering to the principle of proportionality. A range of policy options (or a combination of them, if it is deemed appropriate) might include the following:

Option 1: Improving withholding tax refund procedures to make them more efficient: This option entails the implementation of several measures, the objective of which is to simplify and streamline withholding tax refund procedures by making them quicker and more transparent.. These measures are not limited by but could include: the establishment of common EU standardised forms and procedures for withholding tax refund claims irrespective of the Member States concerned and the obligation to digitalise current paper based relief processes.

Option 2: Establishment of a fully-fledged common EU relief at source system: This option entails the implementation of a standardized EU-wide system for withholding tax relief at source whereby the correct withholding tax rate, as provided in the DTC is applied at the time of payment by the issuer of the security, to the non-resident investor thereby not incurring double taxation.

Option 3: Enhancing the existing administrative cooperation framework to verify entitlement to double tax convention benefits: This option envisages a reporting and subsequent mandatory exchange of beneficial owner-related information on an automated basis, to reassure both the residence and source country that the correct level of taxation has been applied to the non-resident investor.

C. Preliminary Assessment of Expected Impacts

Likely economic impacts

The initiative will mainly affect cross-border portfolio investors⁷, tax administrations and intermediaries. The main impact of this intervention will be to improve the allocation of investment within the European Union and on the Member States' tax revenues by making the EU capital market more efficient and the economy more productive. EU competitiveness should be enhanced by a better functioning of the Single Market, which would become more attractive for investors and will boost investment volumes in the EU. Higher investment would underpin the higher growth of companies and of the economy in general. This will translate into higher tax revenues on a larger tax base. In the case of the introduction of stronger cooperation rules between tax authorities and reporting obligations to tax administrations, the latter will have more tools to verify that non-resident investors pay their fair share and that withholding tax relief claims are not subject to abuse.

Likely social impacts

Fair(er) taxation is expected to have a positive social impact. A well-functioning tax system carries the potential of playing a stronger distributive role, whereby higher public revenues would translate into more and better public services for the benefit of all citizens.

Likely environmental impacts

The initiative is expected to have a small positive environmental impact, as a result of the reduction in paper-based processes that would come with the digitalisation of withholding tax relief procedures. Furthermore, additional revenues generated from increased investment within the EU market will increase the resources available, amongst others, to environmental protection.

Likely impacts on fundamental rights

The protection of fundamental rights and especially data protection must be ensured. In particular, regarding the extension of the administrative cooperation framework, the set of data elements to be reported and transmitted to tax administrations will be defined in a way to capture only the minimum data necessary, for example to detect underreporting, non-reporting or tax abuse in line with the General Data Protection Regulation obligations.

Likely impacts on simplification and/or administrative burden

More efficient procedures will result in benefits in the form of reduced costs, not only for the Member States' tax administrations, but also for different actors such as intermediaries and investors. The impact assessment will endeavour to quantify how much an EU harmonised framework on withholding tax relief procedures may reduce regulatory costs (administrative burden/compliance costs) for both tax administrations and private stakeholders for each of the options assessed. The analysis will also assess the dynamic effect a new EU-wide standardised withholding tax system may have on increasing cross-border investment in the EU while simultaneously assessing the costs associated with increased reporting obligations and exchange of information.

⁷ Portfolio investment is defined as cross border transactions and positions involving debt or equity securities, other than those included in direct investment or reserve assets.

D. Evidence Base, Data collection and Better Regulation Instruments

Impact assessment

An impact assessment is being prepared to support the preparation of this initiative and to inform the Commission's decision. The work on data collection and the economic analysis has already started and will be included in the impact assessment.

Evidence base and data collection

An ongoing study is being performed by the Commission's Joint Research Centre (JRC), to estimate the potential impacts and to assess the dynamic effect that any new EU-wide standardised withholding tax relief system may have in increasing cross-border investment within the EU. Extensive work on possible improvements to withholding tax relief procedures has been carried out over the last years, which will feed into the work:

- At EU level: Two reports by FISCO expert group ([Fact-finding study on fiscal compliance procedures \(FISCO team\) First report 2006](#) and [Solutions to fiscal compliance barriers related to post-trading within the EU \(FISCO group\)](#)), [Code of Conduct on withholding taxes and its subsequent monitoring](#), [final report of the High Level Forum on the Capital Markets Union](#).
- At international level: In 2013, the OECD released the ['Treaty Relief and Compliance Enhancement' \(TRACE\) implementation package](#), which provides for authorised intermediaries to claim reduced rates on withholding taxes pursuant to tax treaties on behalf of their customers (portfolio investors) on a "pooled" basis. Significant work and comprehensive reports on a relief at source system were carried out under the TRACE negotiations, such as: [Report of the informal consultative group on procedures for tax relief for cross-border investors on possible improvements to procedures for tax relief for cross-border investors \(12 January 2009\)](#) and [Report by the pilot group on improving procedures for tax relief for cross-border investors. Public discussion draft: 8 Feb 2010 to 31 August 2010](#).

The European Securities and Markets Authority (ESMA) was requested to produce a report to address the underlying drivers and the potential ways forward to tackle fraudulent schemes: [ESMA report On Cum/Ex, Cum/Cum and withholding tax reclaim schemes Sept 2020](#). Additional sources at both national and international level will also be consulted including but not limited to guidance published by the Finnish tax administration, who were the first Member State to implement the TRACE system. Examples of the guidance published by the Finnish tax administration are available at the following links; [Authorised Intermediary's responsibilities and liabilities Guidance](#), [Secondary legislation regarding the Investor Self Declaration \(ISD\)](#).

Consultation of citizens and stakeholders

The Commission intends to launch a public consultation that will last for a period of 12 weeks during Q4 of 2021 and also invite feedback on this Inception Impact Assessment. The aim of the consultation is to gather views from a broad range of stakeholders on the potential policy options to be covered by the initiative and the scope and technicalities attached to each alternative. In addition, the Commission services are already running targeted consultations of the Member States' tax authorities through regular meetings. Furthermore, the Commission services will continue to consult relevant stakeholders, to gather information from the industry and international and national organisations and associations in order to shape this initiative.

Will an implementation plan be established?

The Commission does not foresee an implementation plan since the proposal at stake would not cover a framework directive or a directive aimed at the full harmonisation of a policy area or a directive having a significant impact on or amending various branches of the national legal order.