COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 18/07/2001
COM(2001) 400

Proposal for a

COUNCIL DIRECTIVE

to ensure effective taxation of savings income in the form of interest payments within the Community

(presented by the Commission)

EXPLANATORY MEMORANDUM

1. INTRODUCTION

1. In its Communication of 5 November 1997 entitled "A package to tackle harmful tax competition in the European Union"[1] the Commission stressed the need for coordinated action at a European level to tackle harmful tax competition in order to help achieve certain objectives such as reducing the continuing distortions in the internal market, preventing excessive losses of tax revenue and encouraging tax systems to develop in a more employment-friendly way. The ECOFIN Council of 1 December 1997[2] held a wide-ranging debate on the basis of that Communication, agreed to a Resolution on a code of conduct for business taxation, approved a text on taxation of savings as the basis for a Directive in this field and considered that the Commission should present a proposal for a Directive on interest and royalty payments between companies. In line with the agreement of 1 December 1997, the Commission adopted on 4 March 1998[3] a proposal for a Directive on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States and on 20 May 1998[4] a proposal for a Directive to ensure a minimum of effective taxation of savings income in the form of interest payments within the Community.

2. On 10 February 1999, the European Parliament issued its opinion on the proposal for a Directive to ensure a minimum of effective taxation of savings income in the form of interest payments within the Community[5]. The Economic and Social Committee issued its opinion on 24 February 1999[6]. The Council started discussing the proposed Directive in July 1998 under the Austrian Presidency. Over the past 3 years the proposal has been the subject of intensive discussions at both political and technical level. In the course of these discussions the Council has developed a significantly different approach to the issue of taxation of savings income.

3. In line with the ECOFIN Conclusions of 1 December 1997, the Commission based its proposal for a Directive on a compromise solution known as the "coexistence model" whereby each Member State would be able to choose between applying a withholding tax on interest payments made to individuals who are resident in other Member States or providing information to the beneficial owner's Member State of residence. However, at the Santa Maria da Feira European Council on 19 and 20 June 2000[7], Member States unanimously agreed that exchange of information, on as wide a basis as possible, should be the ultimate objective of the EU in line with international developments. It was also agreed that only a limited number of named Member States would be allowed to operate a transitional withholding tax and these

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1 COM(1997) 564 final, 5.11.1997
2 OJ C 2, 6.1.1998, p. 1.
3 OJ C 123, 22.4.1998, p. 9.
4 OJ C 212, 8.7.1998, p. 13.
5 OJ C 150, 28.5.1999, p. 184.
6 OJ C 116, 28.4.1999, p. 18.
7 Annex IV to the Presidency Conclusions of the Santa Maria da Feira European Council of 19/20 June 2000, Press release nr: 200/1/00, 19.6.2000, published on the website of the Council of the European Union (http://ue.eu.int).

Member States agreed to implement exchange of information, as soon as conditions permit, and in any case no later than 7 years after the entry into force of the Directive. Member States levying a withholding tax also agreed to transfer an appropriate share of their revenue to the investor's state of residence. In order to preserve the competitiveness of the EU financial markets, it was agreed that, as soon as the Council had reached agreement on the substantial content of the Directive and before its adoption, the Presidency and the Commission would immediately enter into discussions with the US and key third countries (Switzerland, Liechtenstein, Monaco, Andorra and San Marino) to promote the adoption of equivalent measures in those countries; at the same time, the Member States concerned committed themselves to promote the adoption of the same measures in all relevant dependent or associated territories (the Channel Islands, Isle of Man, and the dependent or associated territories in the Caribbean). Once sufficient reassurances with regard to the application of the same measures in dependent or associated territories and of equivalent measures in the named third countries have been obtained, the Council will decide on the adoption and implementation of the Directive no later than 31 December 2002, and do so by unanimity. The Council finally agreed that work should be pursued on this basis with a view to reaching agreement on the tax package as a whole, according to a parallel timetable for the different elements of the package (taxation of savings, Code of Conduct and interest and royalties). The Feira European Council mandated the ECOFIN Council to seek agreement on the substantial content of the Savings Directive, including the rate of withholding tax, by the end of the year 2000.

4. At its meeting of 26 and 27 November 2000[8], the ECOFIN Council unanimously agreed the substantial content of the Savings Directive and the conditions for the implementation of the Directive, including the conditions governing transition from each stage to the next. It was agreed that all Member States would exchange information with each of the other States 7 years after the date on which the Directive enters into force. Only Austria, Belgium and Luxembourg will exercise their option to operate the withholding tax system during the transitional period and it was agreed that the rate of withholding tax to be applied by these three Member States will be 15% for the first three years of the transitional period and 20% for the remainder of the period. It was also agreed that these Member States would transfer 75% of the revenue of the withholding tax to the Member State of residence of the investor. During the transitional period, the other Member States will automatically communicate information to these Member States without requiring reciprocity. The ECOFIN Council agreed that the scope of the Directive should include interest from debt-claims of every kind and in particular income from domestic or international bonds, accrued interest realised at the sale, refund or redemption of such debt-claims, capitalised interest on zero-coupon bonds and similar products, income distributed by investment funds and capitalised interest from capitalisation funds in as far as such income or interest is attached to debt-claims. Similar income from structures used as a substitute for collective investment funds (trusts, partnerships, etc.) will also be brought within the scope of the Directive. In order to avoid market disruption, the ECOFIN Council agreed that, for the duration of the transitional period, a "grandfathering clause" should be provided in order to exclude income from negotiable loan securities for which the prospectuses have been certified before

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8 Conclusions of the ECOFIN Council of 26/27 November 2000, Press release nr: 13861/00 (Presse 453), 26.11.2000, published on the website of the Council of the European Union.

1 March 2001 or, in the absence of any prospectus, which have been issued before that date, from the scope of the Directive (the application of the grandfathering clause to further issues of such securities made after 1 March 2001 has been clarified in supplementary ECOFIN conclusions adopted on 2 March 2001[9]). The ECOFIN Council also confirmed that, in line with the Commission's 1998 proposal and the ECOFIN Conclusions of 1 December 1997, the Directive should remain based on the paying agent principle. The paying agent is the last intermediary in any given chain of intermediaries who pays interest directly to, or secures the payment of interest for the immediate benefit of, the beneficial owner. The ECOFIN Council did however agree to some refinements of the paying agent method with a view to improving the effectiveness of the proposed Directive. The ECOFIN Council also agreed the minimum procedures to be applied by paying agents in order to establish the identity and residence of the beneficial owner of the interest.

5. The Commission fully supports the new approach adopted by the ECOFIN Council which has exchange of information, on as wide an international basis as possible, as its ultimate objective. This approach reflects the international trend towards increased administrative co-operation and exchange of information between tax administrations. It should however be acknowledged that this approach marks a significant departure from the 1998 proposal for a Directive and from the ECOFIN conclusions of 1 December 1997 on which it was based. As noted above, the 1998 proposal for a Directive was based on a co-existence model offering Member States a free choice between levying a withholding tax or providing information on interest payments to individuals resident in other Member States. Under the new approach agreed by ECOFIN all Member States will ultimately be expected to exchange information on cross-border interest payments. The withholding tax system will be operated by a limited number of Member States and for a transitional period only.

6. In view of the above, the Commission feels that its 1998 proposal for a Directive no longer reflects the common opinion among Member States. Given the fundamental nature of the changes agreed by the Council, the Commission has decided to withdraw its 1998 proposal for a Directive and present a new proposal for a Directive. The 1998 proposal for a Directive is being withdrawn at the same time as this new proposal for a Directive is being presented. This new proposal for a Directive aims to reflect as closely as possible the ECOFIN agreement of 26 and 27 November 2000, the key elements of which are set out above.

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[9] Decisions adopted by written procedure, Press release nr: 6744/01 (Presse 85), 2.3.2001, published on the website of the Council of the European Union.

2. COMMENTARY ON THE ARTICLES OF THE PROPOSAL FOR A DIRECTIVE

Chapter I: Introductory provisions

Article 1

1. This Directive is aimed at ensuring effective taxation of savings income in the form of interest payments which are generally included in the taxable income of resident individuals in all 15 Member States. The Directive is limited to cross-border interest payments and does not affect Member States' internal regimes for taxing savings income.

2. The Directive applies to interest payments made within the Community, regardless of the place of establishment of the issuer of the debt-claim giving rise to the interest. Each Member State must take measures to ensure that paying agents established within its territory perform the tasks which have been assigned to them for the purpose of implementing the Directive.

Article 2

1. The beneficial owner is any individual who receives an interest payment for his own benefit. Interest payments made for the benefit of companies or other legal persons are excluded from the scope of the Directive. In order not to impose too high an administrative burden on paying agents, the Directive applies irrespective of whether the interest payments constitute business income or private investment income of the individual. In the interest of simplification for paying agents, the recipient of an interest payment will generally be considered the beneficial owner of that payment unless he demonstrates that he has not received it for his own benefit. The recipient is not considered the beneficial owner if he acts as a paying agent for another individual. In such case he is required to carry out the tasks which the Directive imposes on paying agents. The recipient is also not considered the beneficial owner if he acts on behalf of a legal person, an entity which is taxed on its profits under the general arrangements for business taxation, an undertaking for collective investment in transferable securities (UCITS) within the meaning of Council Directive 85/611/EEC[10], or an entity referred to in Article 4 (2). In these situations the recipient is neither the beneficial owner nor is he acting as a paying agent within the meaning of the Directive as he is not paying interest to an individual. He is in fact an "intermediary" agent. The entities referred to in Article 4 (2) belong to a residual category of entity for which it was felt that further safeguards are required. The obligation on the recipient to report the name and address of the entity referred to in Article 4 (2) to the economic operator making the interest payment and the obligation on the economic operator to communicate such information to its Member State of establishment is designed to ensure that the Member State of establishment of the entity is alerted to the fact that interest has been paid to such an entity. Point (c) is

[10] OJ L 375, 31.12.1985, p. 3.

designed to cover the situation of a recipient acting as a nominee for another individual who is the beneficial owner. This situation differs from point (a) in that the recipient is not an economic operator acting as a paying agent.

2. Paragraph 2 refers to the situation where a paying agent has information suggesting that the recipient of the interest payment may not be the beneficial owner. In that case the paying agent must take reasonable steps to establish the identity of the true beneficial owner. However, if the paying agent is unable to do so, he will continue to treat the recipient as the beneficial owner

Article 3

1. This Article indicates the minimum standards for establishing the identity and the residence of the beneficial owner. Member States which so wish may impose more stringent obligations on paying agents established in their territory. In order to preserve the competitiveness of EU financial markets, it is important that such further requirements should not be too cumbersome for market operators.

2. Paragraph 2 lays down the minimum standards for establishing the identity of the beneficial owner. A distinction is made between contractual relations entered into before and those entered into on or after the date of implementation of the Directive. For contractual relations entered into before the date of implementation of the Directive the identity of the beneficial owner consists of his name and address. The paying agent establishes the name and address of the beneficial owner by using the information it already has at its disposal. Financial institutions are already required to establish the identity of their regular clients under so-called know-your-customer rules pursuant to Directive 91/308/EEC on prevention of the use of the financial system for the purposes of money laundering[11]. As regards their existing client base paying agents should therefore be able to rely as much as possible on information collected for other purposes. For contractual relations entered into on or after the date of implementation of the Directive the identity consists of the name, address and tax or other identification number or, failing such number, date and place of birth of the beneficial owner. A number of Member States attribute a unique taxpayer identification number (TIN) to each taxpayer. Other Member States may not have such TINs but make use of unique identification numbers for other - more general-purposes. If no unique identification number is available, the paying agent must instead establish the date and place of birth of the beneficial owner.

3. Paragraph 3 lays down the minimum standards for establishing the residence of the beneficial owner. Three periods can be distinguished. For contractual relations entered into before 1 January 2001 the paying agent establishes the residence of the beneficial owner by using the information it already has at its disposal, in particular pursuant to Directive 91/308/EEC. For contractual relations entered into on or after the date of implementation of the Directive the paying agent must distinguish between individuals who declare themselves to be resident in a third country, and consequently outside the scope of the Directive, and those who declare themselves to be resident in a Member State. If an individual holding a Community passport or similar official document declares himself to be resident in a third country, residence

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[11] OJ L 166, 28.6.1991, p. 77.

shall be established by means of a residence certificate issued by the competent authority of the third country in which the individual claims to be resident. The aim of this provision is to prevent individuals who have a known connection with a Member State from avoiding the application of the Directive by falsely claiming third country residence. In all other cases the residence will be considered the country where the beneficial owner's permanent address is situated. It is left to Member States to lay down the detailed rules for verifying the beneficial owner's current permanent address. In practice, Member States already use a variety of means of verifying address under their national "know-your-customer" rules including checking the voters roll, making a credit reference agency search, requesting sight of a recent utility bill, local authority tax bill, bank or building society statement or checking a local telephone directory. For contractual relations entered into between 1 January 2001 and the date of implementation of the Directive, the paying agent must check the residence of the beneficial owner according to the procedure laid down for contractual relations entered into on or after the date of implementation. The legal obligation on the paying agent to apply the procedures laid down in the Directive only arises on the date of implementation by its Member State of establishment. From that date onwards it will have to establish the residence of its new clients and check the residence of its existing clients with whom it has entered into contractual relations on or after 1 January 2001 on the basis of the procedure laid down in sub-paragraph (b).

Article 4

1. The paying agent is any economic operator who pays interest to, or secures the payment of interest for the immediate benefit of, the beneficial owner. An economic operator is any natural or legal person who pays interest in the course of its profession or business. An economic operator is considered to "secure the payment of interest" if it is charged with collecting the interest on behalf of the beneficial owner. In market terms such an economic operator would often be referred to as a "collecting agent". The aim of this definition is to guarantee the identification of a single paying agent in any given chain of intermediaries. Where the interest payment to the beneficial owner is made directly by the debtor, he is identified as the paying agent. If on the other hand, the interest payment is made via a number of intermediaries charged by the debtor or the beneficial owner with paying interest or securing the payment of interest, "paying agent" means only the last intermediary which pays interest directly to, or secures the payment of interest for the immediate benefit of, the beneficial owner. However, it should be emphasised that a bank or other deposit taker is not a "paying agent" in relation to amounts of interests it credits to its client's account unless it has itself paid or secured the payment of that interest.

2. Paragraph 2 extends the definition of paying agent. An entity covered by this provision shall be considered a paying agent upon receipt of the interest rather than upon payment of the interest to a beneficial owner. This paragraph is designed to cover a residual category of entities which may not be subject to such close supervision by the tax authorities. The aim of this provision is to ensure that such entities comply with their paying agent obligations. It therefore only applies to entities which are established in a Member State. A series of successive tests shall be applied to determine whether an entity falls within the scope of this provision. There may be some overlap between these tests and it is sufficient for an entity to be taken out on any one of the tests. The detailed mechanisms for applying these tests are left

to Member States. However, the underlying principle of such mechanisms should be one of reducing the administrative burden for paying agents. An entity is considered a paying agent under this paragraph when it is neither a legal person, nor an entity which is taxed on its profits under the general arrangements for business taxation, nor a UCITS within the meaning of Directive 85/611/EEC. In order to inform the Member State of establishment of the entity of the fact that an entity on its territory is to be considered a paying agent upon receipt, the economic operator paying interest to such an entity must communicate the name and address of, and the total amount of interest paid to the entity to its Member State of establishment. This information will then be passed on to the entity's Member State of establishment. An entity which is considered a paying agent under this paragraph and which has not exercised the option under paragraph 3 will not have to perform the tasks of the Directive if it subsequently pays interest to, or secures the payment of interest for the immediate benefit of, a beneficial owner. Such subsequent payments are outside the scope of the Directive.

3. The entity referred to in paragraph 2 has the option of being treated as a UCITS for the purposes of this Directive (even though it does not constitute a UCITS within the meaning of Directive 85/611/EEC). Member States must lay down the detailed rules for the exercise of this option. Under such rules Member States are free to allow the exercise of the option in certain circumstances but not in others, in particular in order to prevent abuse. If the entity exercises this option it will not be considered a paying agent under paragraph 2 but it will become a paying agent under paragraph 1 if it subsequently pays interest to, or secures the payment of interest for the immediate benefit of, a beneficial owner. When the entity exercises this option, it is bound to perform the series of successive tests of paragraph 2 for any interest payment it makes subsequently in order to determine whether such payment falls within the scope of the Directive. The entity must inform its Member State of establishment that it wishes to exercise the option.

4. When the economic operator paying the interest and the entity referred to in paragraph 2 are established in the same Member State, the Directive imposes no reporting requirements on the economic operator. In view of the principle of subsidiarity, it is left to the Member State in question to take the necessary measures to ensure that the entity complies with the paying agent obligations.

Article 5

Member States are required to notify to the Commission their competent authorities for the purposes of the Directive. In order to ensure transparency, the Commission intends to establish and publish a list of the competent authorities notified by the Member States. For third countries "competent authority" means the competent authority for the purposes of bilateral or multilateral tax conventions. If a third country has not concluded any such conventions, the competent authority will be that which is competent to issue certificates of residence for tax purposes.

Article 6

1. This Article contains the definition of "interest payment" for the purpose of this Directive.

a) This subparagraph defines the scope of the debt-claims covered by the Directive. This definition follows the definition of interest in Article 11 (3) of the OECD Model Tax Convention on Income and on Capital. It clearly encompasses cash deposits and security in the form of money, but also all types of corporate and governments bonds and debentures and similar negotiable debt securities. Bonds which carry a right to participate in the debtor's profits are to be regarded as producing interest and not dividends, unless the funds loaned actually bear a share of the risks incurred by the debtor.

b) Subparagraph b) provides that accrued or capitalised interest realised at the sale, refund or redemption of the debt-claims referred to in a) is also included in the definition of "interest payment". This includes accrued or capitalised interest which is realised at the sale, refund or redemption of zero-coupon bonds, discounted bonds and similar debt-claims.

c) Subparagraph c) extends the definition of "interest payment" to income distributed by UCITS within the meaning of Directive 85/611/EEC, entities which have opted to be treated as such under Article 4 (3), and undertakings for collective investment established outside the EU. This provision is designed to ensure that savings income received indirectly via such undertakings and entities is also included in the scope of the Directive.

For the purposes of this Directive, the term "UCITS" encompasses all undertakings for collective investment which meet the general requirements of Directive 85/611/EEC. The term "undertaking for collective investment established outside the territory referred to in Article 7" encompasses all undertakings for collective investment irrespective of their legal form and the composition of their assets. This includes undertakings which had they been established in a Member State would have been considered UCITS within the meaning of Directive 85/611/EEC, but also all other types of collective investment vehicle (e.g. investment clubs).

Income distributed by the above undertakings and entities is included in the definition of interest payment in so far as such income derives from interest payments, either directly or through an entity referred to in Article 4 (2) (a so-called "look-through approach"). The reference to "interest payments" is designed to cover all types of interest payment referred to in Article 6. This comprises any interest paid to such undertakings or entities on debt-claims which they hold, but also any accrued or capitalised interest they realise at the sale, refund or redemption of such debt claims. Moreover, it also includes any income distributed to such undertakings or entities by other similar undertakings or entities in so far as such income is derived from interest payments, or any income realised by the undertakings or entities on the sale, refund or redemption of shares in other similar undertakings or entities, if the latter have invested more than 40% of their assets in debt-claims. Without the inclusion of such participations it would be possible for the above undertakings or entities to avoid the application of the Directive by not holding the debt-claims directly but through other similar undertakings or entities.

The reference to interest payments "through an entity referred to in Article 4 (2)" is designed to ensure the inclusion of income distributed by the above undertakings or entities which derives from their participations in

investment vehicles which belong to the residual category of entities defined in Article 4 (2).

d) Subparagraph d) extends the definition of "interest payment" to income realised at the sale, refund or redemption of shares or units in UCITS within the meaning of Directive 85/611/EEC, entities which have opted to be treated as such under Article 4 (3), and undertakings for collective investment established outside the EU, if these undertakings and entities have invested more than 40% of their assets in debt-claims. This provision is designed to ensure that accrued or capitalised interest realised at the sale, refund or redemption of shares in the above undertakings and entities is also included within the scope of the Directive. In the interest of simplification for paying agents, the 40% threshold avoids the need for establishing the origin of the income realised at the sale, refund or redemption of the shares in such undertakings or entities. If an undertaking or entity meets the 40% threshold, the entire income will be considered an "interest payment".

The 40% threshold does not only apply to debt-claims but also to participations in other similar undertakings and entities. If the asset test were only applied to debt-claims held directly, it would be possible for a capitalising undertaking to avoid the application of the Directive by holding the debt-claims through other similar undertakings or entities. The 40% threshold must be applied at each subsequent level; i.e. if an undertaking holds shares in another undertaking which meets the 40% threshold, such shares will be fully included in applying the 40% threshold to the former undertaking; if, on the other hand, the second undertaking does not meet the threshold, the shares will be fully excluded in applying the threshold to the former undertaking.

It may be noted that a particular undertaking or entity can be covered by subparagraphs c) and d) in so far as it distributes part of its income derived from interest on debt-claims and capitalises the remainder.

2. In certain situations, the paying agent may be unable to establish which part of the income referred to in Paragraph 1 (c) is derived from interest payments. This Paragraph stipulates that in such situations the total amount of the income distributed by the undertakings or entities concerned will be considered an interest payment.

3. There may be situations in which a paying agent has no information concerning the percentage of assets which the undertakings or entities referred to in paragraph 1 (d) have invested in debt-claims; e.g. if an undertaking for collective investment established outside the EU refuses to disclose the composition of its assets. In such situations, paragraph 3 provides that the percentage will be considered to be above 40% . Consequently, the income from the undertaking or entity concerned will be included in the definition of interest payment.

4. Paragraph 4 extends the definition of "interest payment" to interest which is received by an entity referred to in Article 4 (2) which is considered a paying agent upon receipt of the interest. For the purposes of the Directive, the receipt of the interest shall be considered an interest payment by the entity.

5. As regards paragraph 1 b) and d) this paragraph offers Member States the option of requiring their paying agents to annualise the interest over a period which may not

exceed one year. Member States which so wish can exercise this option only for certain types of savings instruments but not for others.

6. Paragraph 6 contains a so-called " *de minimis* " rule. Member States have the option of excluding from the definition of "interest payment" income from UCITS, and entities which have opted to be treated as such under Article 4 (3), where the investment in debt-claims of such entities has not exceeded 15% of their portfolio. The aim of this provision is to offer Member States the possibility of excluding undertakings which invest predominantly in equity but which may hold some debt for liquidity purposes. If a Member State chooses to exercise this option with respect to UCITS established within its territory, this choice will be binding on other Member States. This means that those other Member States cannot require paying agents established within their territories to provide information or levy withholding tax on such income.

7. The 40% threshold referred to in paragraph 1 d) and paragraph 3 was agreed by the ECOFIN Council in its conclusions of 26/27 November 2000. According to the ECOFIN conclusions, this percentage should be lowered after the end of the transitional period. The Commission proposes to lower the percentage to 15%. This percentage appears sufficient to cover the liquidity requirements of the undertakings and entities concerned.

8. Paragraph 8 stipulates that the percentages of paragraph 1 d) and paragraph 6 are in principle determined by reference to the investment policy as laid down in the fund rules or instruments of incorporation of the undertakings or entities concerned. Often the fund rules or instruments of incorporation of an undertaking will indicate what percentage of debt or equity it is allowed or obliged to hold. If there are no such rules or instruments or if they do not lay down the investment policy of the undertakings, the percentages are determined by reference to the actual composition of their assets. It is left to Member States to lay down the detailed rules for the application of this provision. Such rules should *inter alia* be designed to prevent abuse in situations where the actual investment policy of an undertaking deviates from the investment policy laid down in the fund rules or instruments of incorporation..

Article 7

The scope of the Directive is the territory to which the provisions of the Treaty establishing the European Community apply, having due regard to Article 299 of that Treaty.

Chapter II: Exchange of information

Article 8

1. In keeping with the principle of subsidiarity, this Article specifies the minimum amount of information which the paying agent has to report to its Member State of establishment. Member States which so wish may impose further reporting requirements on paying agents established in their territory. In order to preserve the

competitiveness of EU financial markets, it is however important that such further requirements should not be too cumbersome for market operators. Paragraph 1 indicates the minimum amount of information to be reported with respect to the beneficial owner, the paying agent and the debt-claim giving rise to the interest payment.

2. Paragraph 2 indicates the minimum amount of information to be reported concerning the different categories of interest payment identified in Article 6. Point (b) refers to accrued and capitalised interest realised at the sale, refund or redemption of debt-claims and income realised at the sale, refund or redemption of shares in UCITS, entities which have opted to be treated as such under Article 4 (3) and undertakings for collective investment established outside the EU. It offers Member States a choice between requiring their paying agent to report the amount of interest or income referred to in Article 6 (1) (b) and (d) or the full amount of the sale, refund or redemption. Point (c) refers to income distributed by UCITS, entities which have opted to be treated as such under Article 4 (3) and undertakings for collective investment established outside the EU. It offers Member States a choice between requiring their paying agents to report the amount of income, determined by the so-called "look-through approach" of Article 6 (1) (c), or the full amount of the distribution. Point (d) refers to the (deemed) interest payments by the entities referred to in Article 4 (2) which have not exercised the option under Article 4 (3). Such entities are required to report the amount of interest attributable to each of the members of the entity who are beneficial owners within the meaning of Article 2 (1) and who are resident in a Member State other than the one where the entity is established.

Article 9

1. Member States must communicate the information reported by paying agents established in their territory to any other Member State in which the beneficial owner is resident for the purposes of this Directive.

2. Paragraph 2 lays down the basic principle that the communication of information must be automatic and take place at least once a year, within 6 months following the end of the tax year of the Member State of the paying agent. The provision of information on request only would not be compatible with the aim of the Directive, since it would not give sufficient assurance that the interest payments in question could be taxed by the Member State of residence of the beneficial owner. Work is continuing on the detailed arrangements of the automatic communication of information.

3. Paragraph 3 stipulates that Article 8 of Directive 77/799/EEC concerning mutual assistance by the competent authorities of Member States in the field of direct and indirect taxation[12] does not apply to information which must be communicated under this Directive. The application of that Article which imposes limits to the exchange of information could undermine achievement of the aim of this Directive. This applies in particular to the possibility allowed by Article 8 (3) of Directive 77/799/EEC to provide information on a reciprocal basis only

[12] OJ L 336, 27.12.1977, p. 15.

Chapter III : Transitional provisions

Article 10

During a transitional period of 7 years after the entry into force of the Directive, Belgium, Luxembourg and Austria are not required to apply the provisions of Chapter II. They are therefore not obliged to exchange information during that period, but they are entitled to receive information from the other Member States. They will however be required to exchange information in so far as the procedure referred to in Article 13 (1) (a) is being applied. At the end of the transitional period the provisions of Chapter III cease to be applicable and Belgium, Luxembourg and Austria will be required to apply the provisions of Chapter II.

Article 11

1. Instead of exchanging information, Belgium, Luxembourg and Austria will levy a withholding tax at a rate of 15% during the first three years of the transitional period and at a rate of 20% for the remainder of that period.

2. In accordance with the general principles of the Directive, the withholding tax is levied by the paying agent. The paying agent must ensure that the tax it withholds is transferred to its Member State of establishment within a period consistent with the 6-month period of Article 12. Paragraph 2 indicates how tax should be withheld on the various categories of interest payment identified in Article 6. Point (b) refers to "a levy of equivalent effect to be borne by the recipient". Member States which so wish may impose a levy on the full amount of the proceeds of the sale, redemption or refund instead of imposing a withholding tax on the interest payments. Such a levy must however be entirely borne by the beneficial owner and of equivalent effect to a withholding tax on the amount of accrued or capitalised interest, i.e. it may not lead to a lower tax charge on the interest in the Member State of the paying agent. The levy is considered a withholding tax for the purposes of this Directive and is therefore covered by the provisions of Chapter III including those on revenue sharing and elimination of double taxation.

3. The aim of Paragraph 3 is to avoid accumulation of withholding tax in situations where debt-claims have changed hands during their period of existence. In principle, withholding tax should only be levied on the amount of interest which corresponds to the beneficial owner's period of holding. Only when the paying agent is unable to determine the period of holding, must it treat the beneficial owner as having held the debt-claim throughout its period of existence. In such situations the beneficial owner can however provide evidence of the date of acquisition.

4. The withholding tax levied by the Member State of the paying agent does not discharge the beneficial owner's tax liability in his Member State of residence. The Member State of residence remains fully entitled to tax the income received by the beneficial owner in accordance with its national laws. It is however obliged to eliminate any double taxation which might result from the imposition of the withholding tax by the Member State of the paying agent.

Article 12

75% of the revenue of the withholding tax levied by the Member State of the paying agent in accordance with Article 11 must be transferred to the Member State of residence of the beneficial owner. In transferring this revenue, the Member State levying the withholding tax is not required to provide any information on the identity of the beneficial owner. In keeping with the principle of subsidiarity, it is for the Member States levying withholding tax to choose the most suitable practical arrangements in order to ensure the proper functioning of the revenue sharing system.

Article 13

1. The imposition of withholding tax in accordance with Article 11 is to be regarded as a practical means of ensuring a minimum of effective taxation of cross-border interest payments in the Community. The objective of the Directive, however, is to ensure effective taxation of such payments in the Member State of residence of the beneficial owner. In order to help in achieving this objective, Member States levying withholding tax must provide for either of the procedures referred to in this paragraph in order to allow the beneficial owners to avoid the application of withholding tax by declaring the interest income in their Member State of residence. If a Member State provides for the procedure specified in point (a) and a beneficial owner authorises his paying agent to report information in accordance with Article 8, that Member State is required to communicate such information to the beneficial owner's Member State of residence in accordance with Article 9.

2. This paragraph is intended to specify the information which must feature in the certificate to be issued by the competent authority of the beneficial owner's Member State of residence. The certificate is valid for a period of three years provided the information in respect of which it is issued remains unchanged. If there is any change in the information featured in the certificate, the beneficial owner can no longer rely on it and must immediately request a new one.

Article 14

1. Paragraph 1 imposes a general obligation on the Member State of residence of the beneficial owner to eliminate any double taxation which might result from the imposition of withholding tax in accordance with Article 11.

2. Paragraph 2 stipulates the method by which the Member State of residence is to eliminate double taxation. It must grant a tax credit equal to the amount of tax withheld up to the amount of tax due on such interest in its territory. If the amount of tax withheld exceeds the amount of tax due, it shall repay the excess amount of tax withheld to the beneficial owner. For example: if the amount of tax withheld is 10 and the amount of tax due in the Member State of residence is 15, the Member State of residence shall credit the full amount of tax withheld (residual tax due in Member State of residence is 15 - 10 = 5). If the amount of tax withheld is 15 and the amount of tax due is 10, the Member State of residence shall credit 10 of the tax withheld (residual tax due in Member State of residence is 10 - 10 = 0) and repay the excess 5 of tax withheld to the beneficial owner.

3. Paragraph 3 specifies the order of granting relief if, in addition to the withholding tax referred to in Article 11, the interest has been subject to any other type of withholding tax and the Member State of residence grants a tax credit for such withholding tax in accordance with its national law or double taxation conventions. This provision is specifically intended to deal with situations where interest has been subject to a debtor-type withholding tax in another Member State or in a third country. Paragraph 3 indicates that these other types of withholding tax must be credited first. For example: a paying agent in Member State A pays interest to a beneficial owner in Member State B on a debt-claim which has been issued in Member State C. Member State C levies a debtor-style withholding tax of 15. Member State A levies a withholding tax of 20 in accordance with Article 11. The tax due in Member State B is 25. In accordance with paragraph 3, Member State B must first credit the debtor-style withholding tax of 15 levied in Member State C (residual tax due in Member State B is 25 - 15 = 10). Member State B must then eliminate any double taxation which might result from the imposition of the withholding tax by Member State A. In accordance with paragraph 2, Member State B shall credit 10 of the tax withheld (residual tax due in Member State of residence is 10 - 10 = 0) and repay the excess 10 of tax withheld to the beneficial owner.

Article 15

1. Most existing issues of domestic and international bonds and other negotiable debt securities contain so-called “gross-up” and “early redemption” clauses. A gross-up clause commits the issuer to compensate the investor ("gross-up") for any tax withheld by the issuer's state of establishment. However, an early redemption clause usually allows the issuer to redeem (or "call") the issue at its par value instead. There is a risk that the imposition of the withholding tax referred to in Article 11 could trigger the application of such clauses, in particular in situations where the debtor or the debtor’s paying agent pay interest directly to a beneficial owner referred to in Article 2. In order to avoid the market disruption which the triggering of such clauses may cause, this Article provides for an exemption of existing negotiable debt securities from the scope of the Directive for the duration of the transitional period. During the transitional period, such securities are not considered debt-claims within the meaning of Article 6 (1) (a). This means that income from such "grandfathered" securities is not included within the scope of the Directive, irrespective of whether such securities are held directly by the individual or indirectly via UCITS within the meaning of Directive 85/611/EEC or entities which have opted to be treated as such under Article 4 (3). It also means that such securities are not considered debt-claims for the purpose of calculating the percentages referred to in Article 6 (1) (d) and (6).

   In order to avoid distortions of competition between paying agents, the grandfathering applies irrespective of whether the paying agents are established in Member States which levy a withholding tax or engage in exchange of information. For practical purposes, this Article applies to all negotiable debt securities irrespective of whether they actually contain gross-up or early redemption clauses that are likely to be triggered by the application of this Directive. The term “negotiable debt securities” encompasses all types of debt security which may be traded freely on the secondary markets or which may be transferred by the holder of the security without the prior consent of the issuer. This includes all domestic and

international bonds, but also other types of negotiable debt security such as Euro commercial papers, Euro medium term notes and "*bons de caisse*".

The grandfathering applies to all negotiable debt securities which are first issued before 1 March 2001 or for which the original issuing prospectuses were certified before that date. Negotiable debt securities which are issued on or after 1 March 2001 are therefore not grandfathered, unless the original prospectus was certified before that date.

The grandfathering of the aforementioned securities is conditioned on whether any further issues of such securities are made on or after 1 March 2002. It is common practice for government and corporate issuers to increase or "tap" existing issues. If an existing issue is popular with investors but has become illiquid, a re-opening can improve the liquidity of the issue. Re-opening of bond issues has become the most common technique among sovereign issuers as well as other large investors for building the size of a benchmark bond issue to amounts that achieve the desired liquidity. Where a further issue or "tap" is made on terms that are identical to, and with the intention that it will be interchangeable with, an earlier issue, the two issues will fungible. In practice, both issues will trade under the same identifying number and, if physical delivery is called for, delivery of bonds from either issue will satisfy the delivery obligation. For all practical purposes, the bonds are traded as a single issue.

The Article distinguishes between negotiable debt securities issued by Governments or related entities and those issued by other issuers (i.e. corporate issuers). The term "related entities" refers to public bodies which have been authorised by Governments to issue government debt. It does not refer to state-owned companies issuing (corporate) bonds. If a further issue is made on or after 1 March 2002 of an aforementioned security issued by a Government or a related entity, the entire issue, consisting of the original issue and any further issues, will no longer be grandfathered. It is clear that in such situations there is a risk that some individual investors may wish to invoke the gross-up clauses. It is however expected that in order to avoid market disruption Member States and their related entities will commit not to call or redeem such issues for tax reasons. Third countries and their related entities are of course free to make the same commitment. If a further issue is made on or after 1 March 2002 of an aforementioned security issued by any other issuer (i.e. corporate issuers), such further issue will not be grandfathered, whereas the original issue and any further issues made before 1 March 2002 will remain grandfathered. Such further issues will therefore not "infect" previous issues. It is expected that corporate issuers and national and international numbering agencies will facilitate the application of this provision by ensuring that such further issues made after 1 March 2002 are not made fungible with previous issues. They can make such further issues separately identifiable by registering them under an ISIN or a national registration number which is different from that of the original issue.

2. This Article only provides an exemption for the purposes of the Directive. It has no bearing on the application of Member States' tax laws. Member States remain fully entitled to tax income from grandfathered securities in accordance with their national laws.

Article 16

This Article applies to a number of international organisations which under their articles of agreement are exempt from the obligation to deduct any withholding tax on interest paid on debt-claims that they issue. These international organisations include the International Bank for Reconstruction and Development (IBRD) and the International Finance Corporation (IFC) (both members of the World Bank group), the Inter-American Development Bank, the International Investment Corporation, the Asian Development Bank and the African Development Bank. All EU Member States have signed and ratified the international agreements establishing the IBRD and the IFC, and most Member States are also a member of the other international organisations. This Article allows Member States levying a withholding tax within the meaning of Article 11 which are bound by international agreements governing such organisations to respect their international obligations by exempting paying agents acting on behalf of such organisations from the obligation to levy withholding tax if such an obligation would be contrary to those agreements. The scope of this exemption is limited because it only covers situations where the international organisation itself, or a paying agent it has appointed, pays interest directly to the beneficial owner. The exemption does not apply where any other paying agent is charged with paying interest on a debt-claim issued by an international organisation.

Chapter IV: Miscellaneous and final provisions

Article 17

Member States which so wish are free to levy other types of withholding tax than that referred to in Article 11 in accordance with their national laws or double taxation conventions. This refers in particular to debtor-type withholding taxes which Member States may impose on interest arising within their territories. Such debtor-type withholding taxes are often used under double taxation conventions to divide the taxing rights between the state of residence of the beneficial owner and the state of source of the debt-claim producing the interest.

Article 18

This Article lays down the timetable and the requirements for transposing the Directive into Member States' national laws. Member States are required to forthwith inform the Commission of the transposition of the Directive in their national laws and submit a correlation table between this Directive and the national provisions adopted.

Article 19

The Commission shall report every three years on the operation of this Directive. In its reports the Commission shall pay particular attention to international developments in the area of exchange of information. Where appropriate, it shall propose amendments to the Directive in order to better to ensure effective taxation of savings income and to remove undesirable distortions of competition.

Proposal for a

COUNCIL DIRECTIVE

To ensure effective taxation of savings income in the form of interest payments within the Community

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 94 thereof,

Having regard to the proposal from the Commission[1],

Having regard to the opinion of the European Parliament[2],

Having regard to the opinion of the Economic and Social Committee[3],

Whereas:

(1) Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty[4] has allowed the complete liberalisation of capital movements, including direct investment, taking place in the Community between residents of Member States since 1990; the free movement of capital is now enshrined in Articles 56 to 60 of the Treaty.

(2) Savings income in the form of interest payments from debt-claims constitutes taxable income for residents of all Member States.

(3) By virtue of Article 58 (1) of the Treaty, Member States have the right to apply the relevant provisions of their tax law which distinguish between taxpayers who are not in the same situation with regard to their place of residence or with regard to the place where their capital is invested, and to take all requisite measures to prevent infringements of national law and regulations, in particular in the field of taxation.

(4) In accordance with Article 58 (3) of the Treaty, the provisions of Member States' national tax law designed to counter abuse or fraud should not constitute a means of arbitrary discrimination or a disguised restriction on the free movement of capital and payments as established by Article 56 of the Treaty.

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1 OJ C […], […], p. […].
2 OJ C […], […], p. […].
3 OJ C […], […], p. […].
4 OJ L 178, 8.7.1988, p. 5.

(5) In the absence of any co-ordination of national tax systems for taxation of savings income in the form of interest payments, particularly as far as the treatment of interest received by non-residents is concerned, residents of Member States are currently often able to avoid any form of taxation in their Member State of residence on interest they receive in another Member State.

(6) This scope for tax avoidance is creating distortions in the capital movements between Member States which are incompatible with the internal market.

(7) In line with the ECOFIN conclusions of 1 December 1997, the Commission adopted on 20 May 1998[5] a proposal for a Directive to ensure a minimum of effective taxation of savings income in the form of interest payments within the Community.

(8) That proposal was the subject of intensive discussions at political and technical level from July 1998 onwards but failed to win the unanimous support of Member States.

(9) Therefore this 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 of 26 and 27 November 2000.

(10) The objective of this Directive is to ensure that cross-border savings income in the form of interest payments can be subject to effective taxation in the Member State of residence of the taxpayer in accordance with its national laws.

(11) The scope of this Directive is limited to interest payments made by a paying agent established in one Member State to beneficial owners who are individuals resident in another Member State.

(12) Since the objective of this Directive, which is that of the effective taxation of cross-border savings income within the Community, cannot be sufficiently achieved by the Member States, because of the absence of any co-ordination of national systems for the taxation of savings income, and can therefore be better achieved at Community level, the Community may adopt measures in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty. In accordance with the principle of proportionality, as set out in that Article this Directive confines itself to the minimum required in order to achieve those objectives and does not go beyond what is necessary for that purpose.

(13) The paying agent is the economic operator who pays interest to, or secures the payment of interest for the immediate benefit of, the beneficial owner; the payment of interest does not include the mere passive receipt of a payment by a bank or financial institution into the beneficial owner's account.

(14) In defining the notion of interest payment and the paying agent mechanism reference should be made, where appropriate, to Council Directive 85/611/EEC of 20 December 1985 on the co-ordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)[6].

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5 OJ C 212, 8.7.1998, p. 13.

6 OJ L 375, 31.12.1985, p.3.

(15) The scope of this Directive should be limited to taxation of savings income in the form of interest payments on debt-claims, to the exclusion of the issues relating to the taxation of pension and insurance benefits.

(16) The objective of ensuring effective taxation of interest payments can be achieved thanks to the exchange of information concerning interest payments between Member States.

(17) Council Directive 77/799/EEC of 19 December 1977 concerning mutual assistance by the competent authorities in the field of direct and indirect taxation[7] already provides a basis for Member States to exchange information for tax purposes and should as a general rule apply equally to the exchange of information under this Directive.

(18) The automatic exchange of information between Member States concerning interest payments covered by this Directive constitutes a *conditio sine qua non* for ensuring effective taxation of cross-border interest payments.

(19) It should therefore be stipulated that Member States which exchange information pursuant to this Directive should not be permitted to rely on the limits to the exchange of information as set out in Article 8 of Directive 77/799/EEC.

(20) In order to allow them more time to adapt their legislation Belgium, Luxembourg and Austria should not be required to exchange information for the purposes of this Directive during a transitional period of seven years after the entry into force of this Directive, but should receive such information from the other Member States.

(21) During this transitional period, these three Member States should be required to ensure a minimum of effective taxation of savings income in the form of interest payments by levying a withholding tax .

(22) Those Member States should transfer the greater part of the revenue of this withholding tax to the Member State of residence of the beneficial owner of the interest.

(23) Those Member States should provide for a procedure allowing beneficial owners resident in other Member States to avoid the imposition of this withholding tax by authorising their paying agent to report the interest payments or by presenting a certificate issued by the competent authority of their Member State of residence.

(24) The Member State of residence of the beneficial owner should ensure the elimination of any double taxation of the interest payments which might result from the imposition of this withholding tax in accordance with the procedures laid down in this Directive; it should do so by crediting this withholding tax up to the amount of tax due in its territory on such interest and by reimbursing to the beneficial owner any excess amount of tax withheld.

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7 OJ L 336, 27.12.1977, p. 15.

(25) In order to avoid market disruption, this Directive should, during the transitional period, not apply to interest payments on existing domestic and international bonds and other negotiable debt securities for which the issuing prospectuses have been certified before 1 March 2001 or which, in the absence of any prospectus, have been issued before that date.

(26) Provision should be made in order to allow Member States levying withholding tax to exempt paying agents acting on behalf of international organisations issuing debt-claims from the obligation to withhold tax on interest paid on such debt-claims, where such an obligation would be contrary to international agreements concluded by those Member States with respect to such organisations.

(27) This Directive should not preclude Member States from levying other types of withholding tax than that referred to in this Directive on interest arising in their territories.

(28) The Commission should report every three years on the operation of this Directive and propose to the Council any amendments that prove necessary in order better to ensure effective taxation of savings income and to remove undesirable distortions of competition.

(29) This Directive respects the fundamental rights and principles which are recognised, in particular, by the Charter of Fundamental Rights of the European Union,

HAS ADOPTED THIS DIRECTIVE:

Chapter I: Introductory provisions

Article 1

Aim

1. The aim of the Directive is to ensure that savings income in the form of interest payments made in one Member State to beneficial owners who are individuals resident in another Member State can be subject to effective taxation in accordance with the national laws of the latter Member State.

2. Member States shall take the necessary measures to ensure that the tasks necessary for the implementation of this Directive are carried out by paying agents established within their territory, irrespective of the place of establishment of the debtor of the debt-claim producing the interest.

Article 2

Definition of beneficial owner

1. For the purposes of this Directive, "beneficial owner" means any individual who receives an interest payment or any individual for whose benefit an interest payment is secured, unless he can provide evidence that he has not received it for his own benefit. He shall not be regarded as a beneficial owner where:

   (a) he acts as a paying agent within the meaning of Article 4 (1), or

   (b) he acts on behalf of a legal person, an entity which is taxed on its profits under the general arrangements for business taxation, a UCITS within the meaning of Council Directive 85/611/EEC or an entity referred to in Article 4 (2) of this Directive and, in the latter case, discloses the name and address of that entity to the economic operator making the interest payment and the latter communicates such information to its Member State of establishment, or

   (c) he acts on behalf of another individual who is the beneficial owner and discloses to the paying agent the identity of that beneficial owner in accordance with Article 3 (2).

2. Where a paying agent has information suggesting that the individual who receives an interest payment or for whom an interest payment is secured may not be the beneficial owner, it shall take reasonable steps to establish the identity of the beneficial owner in accordance with Article 3 (2). If the paying agent is unable to identify the beneficial owner, it shall treat the individual in question as the beneficial owner.

Article 3

Identity and residence of beneficial owners

1. Each Member State shall, within its territory, adopt and ensure the application of the procedures necessary to allow the paying agent to identify the beneficial owners and their residence for the purposes of this Directive.

   Such procedures shall comply with the minimum standards established in paragraphs 2 and 3.

2. In order to establish the identity of the beneficial owner, the following minimum standards shall apply:

   (a) for contractual relations entered into before the date of implementation of the Directive, the paying agent shall establish the identity of the beneficial owner, consisting of his name and address, by using the information at its disposal, in particular pursuant to the regulations in force in its state of establishment and to Council Directive 91/308/EEC[8];

[8] OJ L 166, 28.6.1991, p. 77.

(b) for contractual relations entered into on or after the date of implementation of the Directive, the paying agent shall establish the identity of the beneficial owner, consisting of name, address and tax or other identification number or, failing such number, the date and place of birth of the beneficial owner.

3. In order to establish the residence of the beneficial owner for the purposes of this Directive, the following minimum standards shall apply:

(a) for contractual relations entered into before 1 January 2001, the paying agent shall establish the residence of the beneficial owner by using the information at its disposal, in particular pursuant to the regulations in force in its state of establishment and to Directive 91/308/EEC;

(b) for contractual relations entered into on or after the date of implementation of the Directive, the paying agent shall establish the residence of the beneficial owner according to the following procedure:

(i) for individuals holding a passport or similar official document issued by a Member State who declare themselves to be resident in a third country , residence shall be established by means of a residence certificate issued by the competent authority of the third country in which the individual claims to be resident;

(ii) in all other cases the residence shall be considered the country where the beneficial owner's permanent address is situated.

(c) For contractual relations entered into between 1 January 2001 and the date of implementation of the Directive, the paying agent shall check the residence of the beneficial owner according to the procedure laid down for contractual relations entered into on or after the date of implementation of the Directive.

Article 4

Definition of paying agent

1. For the purposes of this Directive, “paying agent” means any economic operator who pays interest to, or secures the payment of interest for the immediate benefit of, the beneficial owner, whether it be the debtor of the debt-claim which produces the interest or the operator charged by the debtor or the beneficial owner with paying interest or securing the payment of interest.

2. Any entity established in a Member State to which interest is paid or for which interest is secured for the benefit of the beneficial owner shall also be considered a paying agent upon such payment or securing of such payment, provided that it is not:

(a) a legal person,

(b) taxed on its profits under the general arrangements for business taxation,

(c) a UCITS within the meaning of Directive 85/611/EEC.

An economic operator paying interest to, or securing interest for, such an entity established in another Member State which is considered a paying agent under this paragraph shall communicate the name and address of the entity and the total amount of interest paid to, or secured for, the entity to the competent authority of its Member State of establishment, which shall pass this information on to the competent authority of the Member State where the entity is established.

3. The entity referred to in Paragraph 2 shall, however, have the option of being treated for the purposes of this Directive as a UCITS within the meaning of Directive 85/611/EEC. The exercise of such option shall be notified to the Member State of establishment of the entity.

Member States shall lay down the detailed rules for the exercise of this option.

4. Where the economic operator and the entity referred to in Paragraph 2 are established in the same Member State, that Member State shall take the necessary measures to ensure that the entity complies with the provisions of this Directive when it acts as a paying agent.

Article 5

Definition of competent authority

For the purposes of this Directive "competent authority" means:

(a) for Member States any of the authorities notified by the Member States to the Commission, and

(b) for third countries the competent authority for the purposes of bilateral or multilateral tax conventions or, failing that, such other authority as is competent to issue certificates of residence for tax purposes.

Article 6

Definition of interest payment

1. For the purposes of this Directive, "interest payment" means:

(a) interest paid, or credited to an account, relating to debt-claims of every kind, whether or not secured by mortgage and 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 shall not be regarded as interest payments;

(b) interest accrued or capitalised at the sale, refund or redemption of the debt-claims referred to in (a);

(c) income deriving from interest payments, either directly or through an entity referred to in Article 4 (2), distributed by

(i) UCITS within the meaning of Directive 85/611/EEC,

(ii) entities which have exercised the option of Article 4 (3), and

(iii) undertakings for collective investment established outside the territory referred to in Article 7;

(d) income realised upon the sale, refund or redemption of shares or units in the following undertakings and entities, if they have invested more than 40% of their assets in debt-claims referred to in (a) or in other shares or units as defined in this sub-paragraph:

(i) UCITS within the meaning of Directive 85/611/EEC,

(ii) entities which have exercised the option under Article 4 (3),

(iii) undertakings for collective investment established outside the territory referred to in Article 7.

2. As regards paragraph 1 (c), when a paying agent has no information concerning the proportion of the income which derives from interest payments, the total amount of the income shall be considered an interest payment.

3. As regards paragraph 1 (d), when a paying agent has no information concerning the percentage of the assets invested in debt-claims or in shares or units as defined in that paragraph, that percentage shall be considered to be above 40%.

4. When interest as defined in paragraph 1 is paid to or credited to an account held by an entity referred to in Article 4 (2), such entity not having exercised the option under Article 4 (3), it shall be considered an interest payment by such entity.

5. As regards paragraph 1 (b) and (d) Member States shall have the option of requiring paying agents in their territory to annualise the interest over a period of time which may not exceed one year, and treating such annualised interest as an interest payment even if no sale, redemption or refund occurs during that period.

6. By way of derogation from paragraphs 1 (c) and (d), Member States shall have the option of excluding from the definition of interest payment any income referred to in those provisions from undertakings or entities established within their territory where the investment in debt-claims referred to in paragraph 1 (a) of such entities has not exceeded 15% of their portfolio.

The exercise of such option by a Member State shall be binding on other Member States.

7. The percentage referred to in paragraph 1 (d) and paragraph 3 shall after the end of the transitional period referred to in Article 10 be 15%.

8. The percentages referred to in paragraph 1 (d) and in paragraph 6 are determined by reference to the investment policy as laid down in the fund rules or instruments of incorporation of the undertakings or entities concerned and, failing which, by reference to the actual composition of the assets of the undertakings or entities concerned.

Article 7

Territorial scope

This Directive shall apply to interest paid by a paying agent established within the territory to which the Treaty applies by virtue of Article 299 thereof.

Chapter II: Exchange of information

Article 8

Information reporting by the paying agent

1. The minimum amount of information to be reported by the paying agent to the competent authority of its Member State of establishment shall consist of:

   (a) the identity and residence of the beneficial owner established in accordance with Article 3;

   (b) the name and address of the paying agent;

   (c) the account number of the beneficial owner or, where there is none, identification of the debt-claim giving rise to the interest, and

   (d) information concerning the interest payment in accordance with the second paragraph.

2. The paying agent shall report at least the following information concerning the interest payment:

   (a) in the case of an interest payment within the meaning of Article 6 (1) (a): the amount of interest paid or credited;

   (b) in the case of an interest payment within the meaning of Article 6 (1) (b) or (d): either the amount of interest or income referred to in those paragraphs or the full amount of the sale, redemption or refund;

   (c) in the case of an interest payment within the meaning of Article 6 (1) (c): either the amount of income referred to in that paragraph or the full amount of the distribution;

(d) in the case of an interest payment within the meaning of Article 6 (4): the amount of interest attributable to each of the members of the entity referred to in Article 4 (2) who meet the conditions of Articles 1 (1) and 2 (1);

(e) where a Member State has exercised the option under Article 6 (5): the amount of annualised interest.

Article 9

Automatic exchange of information

1. The competent authority of the Member State of the paying agent shall communicate the information referred to in Article 8 to the competent authority of the Member State of residence of the beneficial owner.

2. The communication of information shall be automatic and shall take place at least once a year, within 6 months following the end of the tax year of the Member State of the paying agent, for all interest payments made during that year.

3. Article 8 of Directive 77/799/EEC[9] shall not apply to the information to be provided pursuant to this Chapter.

Chapter III: Transitional provisions

Article 10

Transitional period

During a transitional period of seven years after the date of entry into force of this Directive and subject to Article 13 (1), Belgium, Luxembourg and Austria shall not be required to apply the provisions of Chapter II.

They shall, however, receive information from the other Member States in accordance with Chapter II.

Article 11

Withholding tax

1. During the transitional period referred to in Article 10, Belgium, Luxembourg and Austria shall ensure a minimum of effective taxation of savings income in the form of interest payments by levying a withholding tax at a rate of 15% during the first three years of the transitional period and 20% for the remainder of the period.

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9 OJ L 336, 27.12.1977, p. 15.

2. The paying agent shall levy withholding tax as follows:

(a) in the case of an interest payment within the meaning of Article 6 (1) (a): on the amount of interest paid or credited;

(b) in the case of an interest payment within the meaning of Article 6 (1) (b) or (d): on the amount of interest or income referred to in those paragraphs or by a levy of equivalent effect to be borne by the recipient on the full amount of the proceeds of the sale, redemption or refund;

(c) in the case of an interest payment within the meaning of Article 6 (1) (c): on the amount of income referred to in that paragraph;

(d) in the case of an interest payment within the meaning of Article 6 (4): on the amount of interest attributable to each of the members of the entity referred to in Article 4 (2) who meet the conditions of Articles 1 (1) and 2 (1);

(e) where a Member State has exercised the option under Article 6 (5): on the amount of annualised interest.

3. For the purposes of points (a) and (b) of paragraph 2, withholding tax is levied pro rata to the period of holding of the debt-claim by the beneficial owner.

When the paying agent is unable to determine the period of holding on the basis of information in its possession, it shall treat the beneficial owner as having held the debt-claim throughout its period of existence unless he provides evidence of the date of acquisition.

4. The imposition of withholding tax by the Member State of the paying agent shall not preclude the Member State of residence of the beneficial owner from taxing the income in accordance with its domestic law, subject to compliance with the Treaty.

Article 12

Revenue sharing

Member States levying withholding tax in accordance with Article 11 shall retain 25% of the revenue of such tax and transfer 75% of the revenue to the Member State of residence of the beneficial owner of the interest. Such transfer shall take place at the latest within a period of 6 months following the end of the tax year of the Member State of the paying agent.

Member States levying withholding tax shall take the necessary measures to ensure the proper functioning of the revenue sharing system.

Article 13

Exceptions to the withholding tax procedure

1. Member States levying withholding tax in accordance with Article 11 shall provide for either of the following procedures in order to ensure that the beneficial owners may request that no tax be withheld:

(a) a procedure which allows the beneficial owner expressly to authorise the paying agent to report information in accordance with Chapter II, such authorisation being valid for a period of three years and covering all interest paid to the beneficial owner by that paying agent; in such a case, the provisions of Article 9 shall apply;

(b) a procedure which ensures that withholding tax shall not be levied where the beneficial owner presents to his paying agent a certificate drawn up in his name by the competent authority of his Member State of residence in accordance with paragraph 2.

2. At the request of the beneficial owner, the competent authority of his Member State of residence shall issue a certificate indicating:

(a) name, address and tax or other identification number or, failing such, date and place of birth of the beneficial owner;

(b) name and address of the paying agent;

(c) account number of the beneficial owner or, where there is none, identification of the security.

Such certificate shall be valid for a period of three years provided the information in respect of which it was issued remains unchanged. It shall be issued to any beneficial owner who has requested it, within two months following such request.

Article 14

Elimination of double taxation

1. During the transitional period referred to in Article 10, the Member State of residence of the beneficial owner shall ensure the elimination of any double taxation which might result from the imposition of the withholding tax referred to in Article 11, in accordance with the provisions of paragraphs 2 and 3.

2. If interest received by a beneficial owner has been subject to withholding tax in the Member State of the paying agent, the Member State of residence of the beneficial owner shall grant him a tax credit equal to the amount of the tax withheld up to the amount of tax due on such interest in its territory, in accordance with its national law. Where the amount of tax withheld exceeds the amount of tax due, the Member State of residence shall repay the excess amount of tax withheld to the beneficial owner.

3. If, in addition to the withholding tax referred to in Article 11, interest received by a beneficial owner has been subject to any other type of withholding tax and the Member State of residence grants a tax credit for such withholding tax in accordance with its national law or double taxation conventions, such withholding tax shall be credited before the procedure in paragraph 2 is applied.

Article 15

Negotiable debt securities

1 During the transitional period referred to in Article 10, domestic and international bonds and other negotiable debt securities which have been first issued before 1 March 2001 or for which the original issuing prospectuses have been approved before that date by the competent authorities within the meaning of Council Directive 80/390/EEC[10], or by the responsible authorities in third countries, shall not be considered as debt-claims within the meaning of Article 6 (1) (a), provided that no further issues of such negotiable debt securities are made on or after 1 March 2002.

If a further issue is made on or after 1 March 2002 of an aforementioned negotiable debt security issued by a Government or a related entity, the entire issue of such security, consisting of the original issue and any further issue, shall be considered a debt-claim within the meaning of Article 6 (1) (a).

If a further issue is made on or after 1 March 2002 of an aforementioned negotiable debt security issued by any other issuer not covered by the previous sentence, such further issue shall be considered a debt-claim within the meaning of Article 6 (1) (a).

2. Nothing in this Article shall prevent Member States from taxing the income from the negotiable debt securities referred to in the first paragraph in accordance with their national laws.

Article 16

International organisations

During the transitional period referred to in Article 10, Member States levying the withholding tax referred to in Article 11 shall be free to exempt paying agents acting on behalf of international organisations issuing debt-claims from the obligation to withhold tax on interest paid on such debt-claims, if this obligation would be contrary to international agreements concluded by those Member States with respect to such organisations.

Chapter IV: Miscellaneous and final provisions

Article 17

Other withholding taxes

This Directive shall not preclude Member States from levying other types of withholding tax than that referred to in Article 11 in accordance with their national laws or double taxation conventions.

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10 OJ L 100, 17.4.1980, p. 1.

Article 18

Transposition

1. Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive by 1 January 2004 at the latest.

   When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.

2. Member States shall forthwith inform the Commission thereof and communicate to the Commission the main provisions of national law which they adopt in the field covered by this Directive and a correlation table between this Directive and the national provisions adopted.

Article 19

Review

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.

Article 20

Entry into force

This Directive shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Communities*.

Article 21

Addressees

This Directive is addressed to the Member States.

Done at Brussels, […]

For the Council
The President

FINANCIAL STATEMENT

This proposal for a Council Directive has no financial implications for the Community budget.

IMPACT ASSESSMENT FORM

THE IMPACT OF THE PROPOSAL ON BUSINESS WITH SPECIAL REFERENCE TO SMALL AND MEDIUM-SIZED ENTERPRISES (SMEs)

TITLE OF PROPOSAL

Proposal for a Council Directive to ensure effective taxation of savings income in the form of interest payments within the Community.

DOCUMENT REFERENCE NUMBER

[…]

THE PROPOSAL

1. Taking account of the principle of subsidiarity, why is Community legislation necessary in this area and what are its main aims?

   The aim of this proposal for a Directive is to ensure that savings income in the form of interest payments made in one Member State to beneficial owners who are individuals resident in another Member State can be subject to effective taxation in accordance with the national laws of the latter Member State.

   Due to the present lack of co-ordination between Member States, individuals are often able to avoid any form of taxation in their Member State of residence on interest paid to them in another Member State. This is causing distortions in the operation of the single market and losses in tax revenue for Member States. It is clear that the European financial are cannot deliver its full benefits if savers' decisions are determined by the possibility of avoiding tax instead of being taken in the light of a comparison between investment alternatives based on their intrinsic merits.

   This proposal for a Directive is designed to help overcome these problems and allow Member States to tax their residents on cross-border savings income in accordance with their own laws. The proposal is not aimed at harmonising Member States' domestic tax treatment of such income.

THE IMPACT ON BUSINESS

2. Who will be affected by the proposal?

   – which sectors of business

   – which sizes of business (what is the concentration of small and medium-sized firms)

   – are there particular geographical areas of the Community where these businesses are found

The Directive applies to cross-border interest payments to individuals. Interest payments to legal persons fall outside the scope of the Directive. In order not to impose too high an administrative burden on paying agents, the Directive applies irrespective of whether the interest payments constitute business income or private investment income of the individual. Consequently, cross-border interest payments to sole proprietorships fall within the scope of the Directive. The Directive however provides for procedures which allow sole proprietors and other individuals to avoid the imposition of the transitional withholding tax by authorising their paying agents to report the interest payments or by obtaining a certificate from their Member State of residence. Moreover, the Directive imposes an obligation on the Member State of residence to eliminate any double taxation which may arise as a result of the imposition of the transitional withholding tax. Sole proprietors and other individuals will therefore not be subject to a higher tax charge as a result of this Directive.

Paying agents play a key role in the implementation of this Directive. They are charged with providing information or, under the transitional arrangements, deducting withholding tax on interest payments to individuals. For the purposes of this Directive, a paying agent is any economic operator who pays interest to, or secures the payment of interest for the immediate benefit of, the beneficial owner, whether it be the debtor of the debt-claim which produces the interest or the operator charged by the debtor or the beneficial owner with paying interest or securing the payment of interest. The Directive only affects economic operators paying interest directly to individuals, i.e. the last intermediary in any given chain of intermediaries. The majority of issuers of securities and other economic operators will therefore suffer no additional administrative costs as a result of this Directive.

The obligations placed on paying agents will entail some additional administrative costs for the economic operators concerned and may require them to adapt their administrative procedures and computerised systems. However, every effort has been made to minimise the compliance cost for paying agents, in particular by simplifying the identification and reporting obligations and by basing them as much as possible on existing obligations under international and national anti-money laundering and "know-your-customer" rules. When transposing the Directive into national law, Member States should take account of the need to keep costs and extra burdens to a minimum.

3. What will business have to do to comply with the proposal?

Economic operators who act as paying agents will have to comply with the identification and reporting requirements of the Directive. They must establish the identity and residence of the beneficial owners in accordance with the minimum procedures laid down in the Directive and report the interest payments they make to such individuals to the tax authorities of their Member State of establishment. During the 7-year transitional period, paying agents in Belgium, Luxembourg and Austria will not be required to report the interest payments but levy a withholding tax. As noted above, these obligations will probably require paying agents to adapt their administrative procedures and computer programs, although every effort has been made to minimise the additional cost involved.

4. What economic effects is the proposal likely to have?

– on employment

– on investment and the creation of new businesses

– on the competitiveness of businesses

The present scope for non-taxation of cross-border interest payments results in a loss of tax revenue for Member States and may even force some Member States to reduce their tax rates on domestic interest payments in order to avoid the risk of a further outflow of savings. By ensuring effective taxation of cross-border interest payments, the Directive can contribute to Member States' efforts to restore the balance between the burden of taxation on the different factors of production and thereby to achieve a reduction in the taxation on income from employment. This would be certain to have a positive effect on job creation and the fight against unemployment. The Directive should also have a favourable impact on the European financial area, because savers' decisions will no longer be determined by the possibility of avoiding tax but will instead be based on the intrinsic merits of the investments. This should help financial institutions, investment funds and other market operators to compete on equal terms.

Since the scope of the Directive includes all cross-border interest payments, irrespective of the place of establishment of the issuer of the debt-claim giving rise to the interest, debtors established in the EU are not placed at a competitive disadvantage in relation to issuers outside the Community. Moreover, the scope of the Directive also includes income from investment funds established outside the Community when such income is paid in a Member State. The Directive should therefore not involve any particular risk of relocation of debt-issuing or investment fund activities to countries outside the Community. The risk of relocation of paying agent activities is reduced by the efforts that have been made to keep additional administrative costs to a minimum and by the continuing efforts to promote the adoption of equivalent measures at a wider international level.

5. Does the proposal contain measures to take account of the specific situation of small and medium-sized firms (reduced or different requirements etc)?

The proposal contains no specific measures for small and medium-sized firms. However, every effort has been made to keep costs and extra burdens to a minimum for all enterprises. This should particularly benefit small and medium-sized firms which are generally more affected by such costs.

CONSULTATION

6. List the organisations which have been consulted about the proposal and outline their main views.

The principles underlying this proposal were agreed by the ECOFIN Council of 26 and 27 November 2000. The ECOFIN conclusions take account of the need for minimising the additional administrative costs for market operators. This has been an overriding concern throughout the Council discussions. Throughout these discussions, Member States have been encouraged to consult their market operators.

The Commission has also received numerous written submissions from individual market operators and representative bodies such as the European Banking Federation, the European Federation of Investment Funds and Companies (FEFSI), the London Investment Banking Association (LIBA) and the International Primary Markets Association (IPMA).

The Commission has constantly informed the Council of its consultations with market operators and the Council working group has spent considerable time examining how to accommodate the concerns expressed by the industry. A very useful meeting between Members of the Council working group and industry representatives was held on 18 November 1999 in order to examine these issues and particularly to discuss possible ways to reduce the impact of the Directive on market operators.
