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IMPACT ASSESSMENT

Accompanying the document

Proposal for a Council Directive on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States

(Recast version)

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This report commits only the Commission's services involved in its preparation and does not prejudge the final form of any decision to be taken by the Commission.

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1. PROCEDURAL ISSUES AND CONSULTATIONS OF INTERESTED PARTIES

1.1. Organisation and timing

On 3rd June 2003, the Council adopted the Directive 2003/49/EC on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States[1] (hereinafter, the Directive or the Interest and Royalties Directive) which was due to be implemented by 1 January 2004. Later, the Council amended this legislation through the Directives 2004/66/EC[2] and 2004/76/EC[3]. The former extended its application to companies and taxes of the new Member States, while the latter granted some of the new Member States temporary derogations from one or more provisions of the Directive. More recently, the Council Directive 2006/98/EC[4] extended its application to companies and taxes of Bulgaria and Romania. In addition, the Accession Treaty of Bulgaria and Romania included temporary derogations in its annexes VI and VII[5].

The Commission adopted an amending proposal to the Directive, COM (2003) 841 on 30 December 2003 aiming at its extension to cover a larger range of companies (i.e, the European Company, SE and the European Co-operative Society, SCE). This proposal also intended to exclude from its benefits companies already exempted from tax on interest and royalties received in order to exclude tax avoidance opportunities. The discussions in the working groups of the Council between 2004 and 2006 were unsuccessful and were blocked due to this latter issue.

Article 8 of the Directive states that: the Commission should report to the Council on its operation, in particular with a view to extending its coverage to companies or undertakings other than those under its scope. In order to obtain the required information to draft the report, DG TAXUD asked the International Bureau of Fiscal Documentation (IBFD) to carry out a survey of the implementation of the Directive (the Directive survey) which was delivered in June 2006. The Directive survey indicates that overall implementation has been satisfactory and refers to possible amendments in order to extend its coverage.

The report on the functioning of the Directive was presented on 23 April 2009 (COM (2009) 179 – the Commission's report of the Directive). Its adoption was delayed in order to facilitate discussion in the Council on the 2003 proposal and was only finished when agreement on this latter text did not seem feasible. The main elements of the report were discussed during a Financial Questions Group called by the Swedish Presidency on 23 November 2009.

On December 2009, Directorate D of TAXUD launched a study to prepare for an impact assessment of the possible amendments to the Directive. This was requested to provide technical assistance and input, information and analyses in a manner that would make it possible for the Commission services to draft such an impact assessment.

On 22 April 2010, TAXUD called for the creation of a steering group within the Commission services to follow the work and feed in views from other services of the Commission in order

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1 OJ L 157, 26.6.2003, p. 49.
2 OJ L 168, 1.5.2004, p. 35.
3 OJ L 157, 30.4.2004, p. 106.
4 OJ L 363, 20.12.2006, p. 129.
5 OJ L 157, 21.6.2005, p. 278 and p. 311.

to prepare the impact assessment of the proposal. The SG, SJ, COMP, ECFIN, EMPL, ENTR. MARKT, TRADE, INFSO and RTD departments were invited. On May 4, the first meeting of the steering group to discuss the intermediate report of the impact assessment study was held. A group formed by officials from TAXUD (D1 and D4), LS, COMP, TRADE and INFSO participated in the meeting. On 7 July, a second meeting of the steering group to discuss the draft final report of the impact assessment study was held. The group was formed by officials from TAXUD (D1 and D4), LS and RTD. A third meeting of the steering group was held on 12 November to agree on this impact assessment. The group was formed by officials from TAXUD (D1 and D4), RTD and COMP.

1.2. Consultation and expertise

International double taxation on cross-border interest and royalty payments is an identified and well-known obstacle to the smooth functioning of the internal market. We can refer to abundant academic studies such as, among others, the *Report of the Committee of Independent Experts on Company Taxation*, the Ruding Report, March 1992; to *EC Tax Law*, by Paul Farmer and Richard Lyal, Clarendon Press, Oxford 1994; to *Company Taxes in the European Union: Criteria and Options for Reform*, by S. Cnossen, ed. Fiscal Studies (1996), vol. 17; to *European Tax Law,* by B. Terra and P. Wattel, 5th edition, Kluwer Law International, 2007; and to the comments by Bruno da Silva on the Report Functioning of the Interest and Royalties Directive, *Highlights Insights on European Taxation*, number 6, 2009.

The Directive IBFD survey released after its implementation has been a source of information on its operation and on the issues that could require further policy action to better achieve its objective of eliminating this tax obstacle to cross-border activities.

The study for an impact assessment of the possible amendments to the Directive launched by TAXUD has been made by Copenhagen Economics (the CE survey)[6]. It offers a broad overview of the withholding taxes effects on cross-border transactions and measures, where possible, its economic impact for business. At the request of TAXUD, it analyses the possible consequences of different policy options targeted to the difficulties linked to such tax charges and offers some quantitative estimations derived from its implementation.

The TAXUD services have also taken active part in seminars and events concerning the functioning of the Directive. It is relevant to mention the meeting of the Tax Policy Working Group of Business Europe, held on 2 October 2008: there was a debate with experts involved in tax issues concerning multinational companies after a presentation by the Commission services on these topics. On 4 December 2008, a working session followed with a steering group from Business Europe aiming at a more in depth discussion on future improvements to the Directive. A similar event was organized by the Confédération Fiscale Européenne, CFE, in Brussels on 16 April 2010, organization that gathers European tax advisors and practitioner of companies with interests in cross-border activities. Other informal meetings have also been held with interested parties to capture their views and sound out any problems they have encountered. There have been also some in-house events to discuss issues concerning the Directive with tax experts of different areas concerning the Commission tax policy and action.

[6] Copenhagen Economics: *Taxation of interest and royalties – impact assessment of amendments to the present Directive,* October 2010.

A public consultation on proposed amendments to the current legislation, including the areas covered by the impact assessment run from 24 August until 31 October 2010 on the "Your Voice in Europe" web portal and on the DG TAXUD website. 71 responses were received from various stakeholders, including multinationals (25 replies), large firms (3 replies), business and industry associations (18 replies), tax practitioners (16 replies), professional associations (8 replies) and one civil servant from a Member State. The comments were generally supportive of the objectives of this Commission service's initiative. The responses were also used to finalise the policy option parameters on certain specific issues.

1.3. Impact Assessment Board

The draft impact assessment (IA) was discussed with the Impact Assessment Board (IAB) of the Commission on 12 January 2011. This revised IA report takes into account the comments of the IAB as follows.

Concerning the problem definition included in the IA

a) The IAB required that the IA presents a fuller explanation of the context of this initiative and the interrelations of the Directive with the Directive 90/435/CEE on the common tax regime applicable in the case of parent companies and subsidiaries of different Member States (the Parent-Subsidiary Directive)[7]. In particular, the report should refer to the reasons why the issue of extending the scope of the Directive to intra-company payments is not subject to analysis, as recommended by the report on the functioning of the Directive.

For this purpose, section 2.1 of the IA on the identification of the problem has been completed with references to the general taxation of the three types of capital flows – dividends, interest and royalties – and the context in which the existing Directives were adopted and modified. Concerning the issue of the intra-company payments, it has been decided to modify section 4.2 and consider it as a policy option discarded at an earlier stage.

b) The IAB required more clarity on the types and scale of distortions being addressed including why they cannot be addressed satisfactorily by Member States to establish a better evidence base and rationale for EU action.

For this purposes, section 2.2 on the underlying causes of the problems identified has been reorganized and completed with new text. The economic problems and distortions caused by withholding taxes have been identified in three subsections. A new subsection has been incorporated including data to illustrate the dimension of the problem.

Further explanation is given in section 2.3 to illustrate the baseline scenario. Section 2.5 gathers new arguments to justify EU action on the basis of the subsidiary principle.

Concerning the objectives of the recast

The IAB required further clarification on the objectives. It asked if the alignment of the Directive and the Parent-Subsidiary Directive is an objective. It also asked to present the

[7] OJ L 225, 20.8.1990, p. 6, as amended by Council Directive 2003/123/EC of 22 December 2003 amending Directive 90/435/EEC on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, OJ L 7, 13.1.2004, p. 41.

position of Member States on the options, and explain why certain options have not been considered for analysis.

In this regard, sections 3.1 and 3.2 of the IA have been redrafted to clarify the objectives pursued. Also, section 4.2 refers now to other policy options which had been discarded. Section 5.2 on the comparison of options includes a new paragraph referring to the Member State known positions on the considered options.

Concerning the comparison of options

The IAB required elaborating on the non-quantified benefits of the preferred option, how its impacts would be distributed by Member State, and why it has less negative side-effects than option 2. The report should assess the importance of the benefits related to the removal of the different types of distortions and in what proportion they are likely to be achieved under the preferred option. The report should also show how the impacts of the preferred option will be distributed over Member States. It should better explain the negative side-effects associated with the removal of distortions due to different withholding tax rates, including why they could be used as an argument against option 2. The report should also specify more systematically the assumptions made for the calculation of the monetised impacts.

For this purpose, section 5.1 on the analyses of impacts and section 5.2 on the preferred option include new text in order to explain the effects of the options in the Member States in the extent possible. New text has been added to section 5.2 on the comparison of options in order to evaluate further on the impact of the preferred option on the distortions detected.

2. PROBLEM DEFINITION

2.1. Identification of the problems that may require action

The problems addressed by this initiative to recast the Interest and Royalties Directive arise from the existence of particular corporate tax obstacles to the functioning of the internal market: cross-border interest and royalty payments are subject to a more burdensome taxation as compared to that borne by domestic transactions. In case of purely domestic operations, the recipient of the payment is subject to corporate tax as a resident taxpayer in the Member State where it is resident for tax purposes (the home State). In case of international payments, they may be also subject to withholding taxes in the Member State from which it is made (the source State or the host country) and there is a risk of double taxation.

It may be that the residence State allows the taxpayer to reduce the corporate tax liability with a tax credit related to the withholding tax charged at source. Alternatively, it may exempt foreign income. The taxpayer must attest the right to this tax relief through the corresponding documentation. There is also a period elapsing from the withholding date to that in which the taxpayer applies the tax credit to reduce its tax liability.

The bilateral tax relations between the source State and the residence State are usually ruled by double tax conventions (DTCs). These agreements provide for the reduction or the exemption of the withholding taxes charged at source. However, the reduction or exemption requires attesting the conditions established in the DTC through administrative procedures. If those are not attested when the withholding is due, this is charged. The reimbursement required to make effective the tax reduction is only obtained after a claim is submitted and the tax authorities verify the right to the tax relief. So, there are additional compliance and liquidity costs.

In recognition of the double taxation burden and the inefficiencies caused by high withholding taxes on dividends, interests and royalties, the EU Council of Ministers has adopted two sets of legislation. In first instance, in 1990, the Council adopted the Parent-Subsidiary Directive which aims at eliminating withholding taxes on dividend payments between associated entities in EU Member States. This Directive was adopted together with the Directive on the tax regime applicable to mergers and other business reorganizations[8]. Both pieces of legislation aim at easing the grouping together of companies of different Member State in order to guarantee conditions for companies to adopt an European dimension. These Directives are applicable to companies which are resident for tax purposes in a Member State, are subject to corporate tax and have a specific legal form as included in the list annexed to them. The Parent-Subsidiary Directive requires that the parent company holds at least, directly or indirectly, 10% of the capital or voting rights of the subsidiary.

At the same time, there are other capital flows subject to withholding taxes according to general international tax practice which limits the smooth functioning of the internal market. The Commission had presented proposals to harmonize the tax regime of interest and royalty payments. These two items together with dividend payments, already covered by the Parent – Subsidiary Directive, are the main types of capital flows arisen from business activities subject to withholding taxes at source. Only recently, in 2003, the Council adopted the Interests and Royalties Directive. However, its coverage is narrower than that foreseen by the Commission initial proposal. Thus, at the time of adoption of the Directive, the Commission made a protocol declaration that further measures for extending the scope of the Directive would be pursued and the legal text included Article 8, referred above.

The results of the different legislative procedures lead to having two directives which have followed different policy initiatives. In addition, the Parent-Subsidiary Directive was amended in 2003 and its scope was widened and now is broader than that of the Interest and Royalties Directive: the latter requires a minimum direct holding of 25% to consider companies as associated and the list of legal form to which it applies is narrower. It may be noted that in 2003 the Commission adopted an amending proposal to the Interest and Royalty Directive (COM (2003) 841) which inter alia provided for an update of the coverage of the types of companies. This proposal intended also to require that the recipient of the payment would only enjoy the Directive benefits where it would be subject to tax on the payment received in its Member State. This element was subject of some controversy since a Member State had introduced a special regime to calculate the tax base and there were reasonable doubts on the fulfilment of such requirement by the eligible companies if introduced. Thus, the proposal did never reach an unanimous agreement and was not adopted by the Council.

Currently, the Directive scope is limited and does not cover payments between companies which in turn do enjoy the benefits of the Parent-Subsidiary Directive. If entities seek to enjoy the full benefits of tax harmonization they have to meet the conditions of the former Directive so that the amendments introduced to the latter in 2003 are ineffective for them.

8 Council Directive 90/434/EEC of 23 July 1990 on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States, OJ L 225, 20.8.1990, p.1.

This tax situation may increase the costs of doing business by raising the pre-tax required return on cross-border investments and may limit cross-border activities. These are important factors for distortions on the allocation of resources between the multinational and the domestic sector. This situation reduces the level of international economic integration and the effectiveness of the internal market.

2.2. Description, underlying causes and measurement of the problems identified

2.2.1. Dimension of the economic problems caused by withholding taxes

The withholding tax rate charged on non-resident corporations is established in national tax laws. As mentioned, these charges are modified in DTCs prevailing over domestic rules. These treaties provide for lower rates between the relevant countries. In the EU context, the Directive already provides for the exemption of withholding taxes. Thus, while the withholding tax on outgoing interest payments fixed in domestic laws ranges from zero (e.g. in Austria, Finland, Luxembourg, Malta and the Netherlands) to 30% in Hungary (see annex 1) and the withholding tax on outgoing royalty payments ranges from zero (e.g. in Luxembourg, Malta and the Netherlands) to 33.3% in France (see annex 2), the applicable rates provided for in DTCs are lower and range mainly from 0 to 15% (see annex 3 for rates on interest payments and annex 4 for rates on royalty payments).

Concerning the companies and capital flows affected, we should recall that those under the scope of the Directive already enjoy a tax exemption. The requirements for the tax exemption are to have a specific legal form and to be associated with the payer of the income. The legal forms covered are listed in the annex of the Directive. According to the CE survey, in 82% of the cases, both the parent company and the subsidiary have a legal form that falls under the scope of the Directive; nearly 95% of the royalty payments and approximately 90% of the interest payments are covered by the Directive. In fact, the main part of the economic activity (82% of total employment and 85% of total turnover) is concentrated in the subsidiaries that already fall under the Directive (see annex 15). As regards the association requirement, in the Amadeus database used in the CE study non-associated companies (0 to 25% holding) represent 12% of holding links. These companies represent, however, a large share of employment and turnover: 32% and 28 % respectively[9]. It should also be added that most of the interest payments between non-financial institutions that fall outside the scope of the present Directive will take place between associated companies since direct loans between non-associated companies are relatively rare. The CE study expects 80-90% of these payments to take place between associated companies. The opposite is the case for royalty payments. OECD[10] finds that the proportion of EU companies' patent portfolio that is being licensed to non-associated companies lies in the range 80-100% and are outside the scope of the Directive.

2.2.2. Reference to the economic distortions caused by withholding taxes

a. Economic distortions due to differences in withholding taxes

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[9] These shares are lower, however, if weighted by intangible assets (28% and 13% respectively) and also compared with the share weighted by financial assets (32% and 15% respectively) implying that cross-border payments between the companies mainly take the shape of interest payments. See annexes 13 and 19.

[10] OECD: *Who Licenses Out Patents and Why? Lessons from a Business Survey- STI Working Paper 2009/5- Statistical Analysis of Science, Technology and Industry.*

In the first place, each DTC signed on a bilateral basis fixes its own withholding tax rate. In consequence, each bilateral relation between the Member Stats may be subject to a different withholding tax rate, that fixed by each national law or that provided for in each DTC. This tax situation may distort patterns of cross-border investment flows in two ways. To the extent that investment is attracted to certain locations by the promise of low tax charges rather than low production costs, production will be less efficient as a result. Firms may undertake sub-optimally low levels of real investment in countries with high effective withholding taxes and sub-optimally high levels of real investment in countries with low effective withholding taxes. The result is a misallocation of real investment that reduces the average productivity of capital. Although the low-tax country gains from the increased investment, resources are wasted since companies do not operate as efficiently as they could otherwise. Real resources employed with the sole aim of reducing tax liabilities generate a welfare loss equal to the productivity of these resources in the best alternative use. Second, for a given location of real investment firms may incur in costs of implementing avoidance techniques that reduces effective taxation on cross-border capital flows: instead of making a direct payment to a Member State that is subject to withholding taxes, company groups may establish an intermediate conduit entity in a different Member State so that the payment received by it enjoys a tax exemption (tax planning). On the government side, opportunities for tax avoidance result in a loss of tax revenues. On the firm side, tax planning activities result in suboptimal choices by EU firms, and the administrative and compliance costs of tax planning largely represent unproductive use of scarce resources.

b. *Economic distortions deriving from the conditions to enjoy tax relief provided for in DTC and in the Directive*

DTCs and the Directive condition the relief from withholding taxes on ownership shares, holding periods and organisational form of the entities involved. These provisions introduce an incentive for firms to distort holding structures and organisational forms in order to qualify for the relief. Requirements related to holding structure impose economic costs on firms in the event of restructurings and mergers where flexibility may be severely limited. Requirements related to organisational form may induce firms to make use of types of legal entities that are suboptimal compared to the first choice of the company.

In particular, the European Company (SE) and the European Cooperative Society (SCE) are legal forms which are not in the Directive scope. These legal types were created after the adoption of the Directive by the ECOFIN Council and were not included in its text. The aims pursued with these two European legal types - creation and management of companies with a European dimension, free from the obstacles arising from the disparity and the limited territorial application of national law – will not be fully achieved since they will have to face the economic distortions derived from withholding taxes[11].

A number of studies show how the tax system affects the organisational choice of firms. Some of these papers focus on the choice between corporations and non-corporations. Effective taxation of capital invested in corporations is determined by the statutory tax at the company level and the withholding tax at the investor level, whereas the effective taxation of capital invested in non-corporations is given by the income tax. To the extent that the

11 Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company – see paragraph 7 of the explanatory memorandum and Council Regulation (EC) No 1435/2003 of 22 July 2003 on the Statute for a European Cooperative Society – see paragraph 6 of the explanatory memorandum.

effective taxation differs, there is an incentive to shift income between the two organisational forms. De Mooij and Nicodème[12] find that an increase in the corporate tax of 1 percentage point reduces the corporate tax base by 1%, reflecting income shifting from the corporate sector to the non-corporate sector. In sum, there is robust evidence that the tax system, including withholding taxes, affects the organisational choice of firms. Thus, payments not covered by the Directive and suffering from withholding taxes will induce business agents to opt for organization forms which are eligible for the tax relief.

c. Economic distortions caused by different taxation of dividends, interest and royalties; the different scope of the Directive and the Parent-Subsidiary Directive.

Withholding taxes might also distort the capital structure and allocation of intangibles. The applicable withholding taxes rates and the specific method to provide relief for double taxation differ across types of capital flows (dividends, interest and royalties). In addition, they are often subject to different tax regimes; dividends are not deductible from the corporate tax base at the level of the paying entity and are taxable at a low rate or are exempt at the level of the receiving entity; interest payments are deductible from the corporate tax base at the level of the paying entity and fully taxable at the level of the receiving entity; royalty payments are generally treated like interest payments for tax purposes although some jurisdictions apply a favourable tax rate to royalty income. In addition, the Directive and the Parent-Subsidiary Directive establish different conditions in order to enjoy the benefits of the withholding tax exemptions charged at source. Since the three types of capital are to some extent substitutes, tax differences might cause distortions of capital structure. Collins and Shackelford[13] find that dividend, royalty, and sometimes interest cross-border payments are structured to mitigate net tax transfer costs (i.e., payer deductions and withholding taxes, and payee income taxes and credits). Thus, taxes affect the location of the supplier and the terms of the contracts for the provision of equity and intangible capital within the worldwide organisation.

If the effective taxation of intra-firm dividend payments is higher than effective taxation of intra-firm interest payments, firms may employ sub-optimally high levels of debt. Desai, Foley and Hines[14] find that a 10% increase in tax rates is associated with 2.8% higher debt-asset ratios in their sample of US multinationals. External borrowing is more sensitive (1.9%) than borrowing from parent companies (0.35%). Also, Ramb and Weichenreider[15] find that the corporate tax rate in the home counties of the parent company has no significant impact on the financial structure of a German subsidiary. However, if intra-firm royalty payments are taxed more lightly than intra-firm dividend payments, firms may rely too much on intra-firm licensing of intellectual property. The economic costs associated with a distorted capital structure may be considerable. For instance, the role of debt as a corporate governance tool is often emphasised in the corporate finance literature, which suggests that tax motivated departures from the optimal capital structure may have adverse consequences in terms of

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[12] De Mooij, R. A. and Nicodème, G. (2008), "Corporate Tax Policy and Incorporation in the EU", International Tax Public Finance 15, 478-498.

[13] Collins, J. H., and Shackelford, D. A. (1998), "Global Organizations and Taxes: An Analysis of the Dividend, Interest, Royalty and Management Fee Payments between US Multinationals' Foreign Affiliates", Journal of Accounting and Economics 24, 151-173.

[14] Desai, M. A., Foley, C. F. and Hines Jr., J. R. (2004), "A Multinational Perspective on Capital Structure Choice and Internal Capital Markets", The Journal of Finance 6.

[15] Ramb, F. and Weichenrieder, A. J. (2005), *Taxes and the Financial Structure of German Inward FDI*, Kiel Institute for World Economic.

suboptimal governance[16]. Dischinger and Riedel[17] find that an increase in the average tax differential to other European group affiliates by 10 percentage points reduces a subsidiary's intangible property investment by around 11% on average.

In addition, the Directive scope is limited and does not cover payments between companies which in turn do enjoy the benefits of the Parent-Subsidiary Directive. If entities seek to enjoy the full benefits of tax harmonization they have to meet the conditions of the former Directive so that the amendments introduced to the latter in 2003 are ineffective for them. The Directive functioning, as already evaluated through the Commission's report, reveals the need to improve its coverage in order to better achieve its objectives. In particular, the limited scope of the Interest and Royalties Directive as compared to that of the Parent-Subsidiary Directive may affect and distort business decisions, guided by the objective of avoiding withholding taxes at source: it may distort the intra-firm capital structure and the allocation of intangibles.

2.2.3. Compliance costs linked to withholding taxes

International taxation is usually made effective through withholding taxes charged on the crossborder payments according to the tax rate provided for in domestic laws. If the taxpayer is eligible for a tax relief provided for in a double tax treaty, the resulting reimbursement has to be made effective through a tax claim for refund. In this procedure, the taxpayer rights have to be credited through documentation – tax residence certificates – and the payment has to be identified. The tax administration has to control the claim and after verifying it, it will order the refund. The final tax charged at source may be credited against the corporate tax liability due in the Member State where the taxpayer is considered as tax resident. There is a period elapsing since the tax is withheld at source and the annual tax return in the State of residence is only submitted after the closing of the tax period concerned. At the same time, the relief may require to submit documents crediting the tax paid and the right for the relief.

Thus, withholding taxes cause compliance costs to firms, including both administrative burdens and liquidity costs. Administrative burdens are the part of administrative costs that businesses sustain simply because it is a regulatory requirement. Some of the most important administrative cost drivers are the requirement to use paper forms and by the different document formats, different documents to be attached, different confirmations, certificates, etc. Since the costs of reclaim do not depend on the size of the tax claim, SMEs are particularly disadvantaged.

To quantify the size of the administrative costs the CE survey draws on the findings of DG MARKT in the European Commission[18], where the amount of occurring costs related to the reclaim procedures account on average for 2% of the refundable amount. This means that administrative costs of withholding taxes on royalty payments amounts to €26 million (2% of €1.3 billion) if full tax relief is provided. Those associated with interest payments amount to approximately €16 million (2% of €0.8 billion)[19]. In total, it is expected that the cost to EU

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16 Jensen, M. (1986), "Agency Costs of Free Cash Flow, Corporate Finance and Takeovers", American Economic Review 76, 323–329.

17 Dischinger, M. and Riedel, N. (2008), "Corporate Taxes and the Location of Intangible Assets Within Multinational Firms", Munich Discussion Paper 15.

18 DG Internal Market and Services: *Simplified Withholding Tax Relief Procedures*, Brussels 2010.

19 Source: Copenhagen Economics: *Taxation of interest and royalties – impact assessment of amendments to the present Directive,* October 2010, on the basis of *Eurostat, International Transactions in Royalties and Licence Fees* and *Eurostat, International Transactions in Interest and Dividend payments.* For

firms of reclaiming withholding tax paid on interest and royalty payments is around €42 million.

Concerning liquidity costs, the issue arises since firms are required to withhold taxes and are subsequently reimbursed if the tax administration deems that they qualify for the DTC exemption or reduction. Also, when withholding tax rates are matched by tax credits in the home country, it has to be taken into account that the withholding is levied on the payment while its reduction in the residence State is only possible later during the period to submit the tax return. It could also be the case that no corporate taxes are due in the home country, for instance because the firm is running losses; the tax credit yields no immediate tax saving. Losses may typically be carried forward for tax purposes, but even if the tax credit is used in subsequent tax years, this represents a liquidity cost to the firm.

Regarding the timing of the tax refund procedure, the CE survey refers to a time lag of at least six months (see annex 6)[20]. To estimate the opportunity costs of claiming withholding tax relief on dividends, interest and other securities income, the DG MARKT study applies the interest paid for taking out a loan. In their calculations, an investor who receives the tax relief without delay could invest their relief with at present at least a 4% return per year. Consequently, the €1.3 billion paid in withholding tax on royalty payments carry a cost for the investors due to the delay of approximately €52 million per year (4% of €1.3 billion).For interest payments, we find that the liquidity cost amounts to €32 million (4% of 0.8 billions).

2.2.4. International Double taxation

In addition to the withholding tax charged by the source State, the recipient's residence State charges corporate tax on the income derived from the cross-border payment. In order to avoid such double taxation, the residence State either exempts this international income or allows a tax credit to reduce its tax on the said income, as provided for in its national law or in the relevant DTC. This tax credit is normally limited to the residence corporate tax on the corresponding profit; as well, it is calculated on the basis of the net profit, while the withholding tax is charger on the gross payment. Thus, when withholding taxes are high compared to statutory taxes in the residence State or the royalty or interest payments are large compared to profits, there is a risk of a higher taxation in the case of an international payment than that borne by an equivalent domestic payment (excessive taxation).

According to the CE survey, the effective withholding taxes on interest payments received from other EU countries lie in the range of 4 to 9%; the average withholding tax on interest payments is 6.2% in all EU countries. The withholding taxes on royalty payments range between 3 and 8%. The average withholding tax on royalty payments in EU countries is 5.5%. These numbers tell us that the withholding tax charged on royalty payments is slightly lower than the withholding tax paid upon cross-border interest payments. In order to gain an understanding of how important the excessive taxation problem is we also need to look at statutory tax rates in EU Member States. We find that the EU27 corporate tax rates range between 35% and 10%. The average (unweighted) corporate tax rate is 23.5%. Also, we see

further details on the amount of the withholding taxes on interests and royalties, see below section 5.1, option 2 of this impact assessment.

20 The European Commission's general *Impact Assessment study on Clearing and Settlement* of 2006 concluded that in the EU, an investor pays on average between twice and six times more for a cross-border equity transaction compared to a domestic one. The report can be downloaded from http://ec.europa.eu/internal_market/financial-markets/docs/clearing/draft/draft_en.pdf.

that the old EU Member States typically have higher corporate taxes than the new Member States (see annexes 1 to 5).

The conclusion of the CE survey is that it will rarely be the case that the corporate tax rate is lower than the withholding tax. Even for the countries with the lowest corporate tax rates (Slovakia, Romania, Latvia, Ireland, Bulgaria and Cyprus) it is the case that the bilaterally negotiated withholding taxes on both interests and royalties are much lower than the corporate tax rate. Table 1 shows that those Member States in group A have higher corporate tax rates and low withholding rates in the DTCs so that the risk of excessive taxation is low. The excessive taxation problem is most pronounced in the new EU Member States in group D, where statutory tax rates are relatively low but where withholding taxes paid on royalty income from other EU countries are relatively high (the shaded area).

Table 1. Risk of excessive taxation of royalty payments within the EU

	High statutory tax in residence State	**Low statutory tax in residence State**
Low withholding tax on royalty income from DTC source State	Group A: Austria, Luxembourg, Denmark, Belgium, Finland, Netherlands, Sweden, United Kingdom, France Germany, Greece, Spain and Italy,	Group C: Bulgaria, Cyprus, Ireland and Hungary
High withholding tax on royalty income from DTC source State	Group B: Portugal and Malta	Group D: Estonia, Romania, Latvia, Lithuania, Poland, Slovenia, Czech Republic and Slovakia

Source: Copenhagen Economics: *Taxation of interest and royalties – impact assessment of amendments to the present Directive,* October 2010.

According to the CE survey, the impression of relatively modest excessive taxation of royalties is confirmed when we consider the economic variables of country size and flows of foreign direct investment (FDI) and royalty payments (see table 2). In fact, group A has the lowest potential excessive taxation problem and accounts for 95% of the total intra-EU FDI stock, more than 60% of the total EU income on royalties and licences fees, and 97% of the total intangible fixed assets recorded in the Amadeus data base. By contrast, the group of new Member States in group D, where potential excessive taxation problems are the largest, account for just a small fraction of the economic variables that reflect cross-border and intra-company royalty payments. This finding suggests that companies in the new Member States are more prone to excessive taxation whereas their governments earn net revenues from high withholding taxes.

Table 2. Indications of size of excessive taxation of royalties across groups of countries

	Group A	Group B	Group C	Group D
Share of EU intra FDI stock	95.1	1.0	3.1	0.8
Share of EU royalty income	61.4	0.5	34.6	3.4
Share of EU patent firm's intangible assets	97.2	1.1	1.4	0.2

Source: Data on the FDI stock is from Eurostat, *European Union Direct Investment*; data on royalty income is from Eurostat, *International Trade in Services. Data on intangibles fixed assets is from Amadeus.*

Again, we find that it is mainly companies in the new EU Member States that face high withholding taxes on interest income from other EU countries, cf. Table 3.

Table 3. Risk of excessive taxation of interest payments within the EU

	High statutory tax in residence State	**Low statutory tax in residence State**
Low withholding tax on royalty income from DTC source State	Group A: Sweden, Spain, Austria, Finland, United Kingdom, Germany, Netherlands and France	Group C: Bulgaria, Slovakia, Hungary, Czech Republic and Ireland
High withholding tax on royalty income from DTC source State	Group B: Belgium, Portugal, Italy, Malta, Denmark, Greece and Luxembourg	Group D: Romania, Latvia, Lithuania, Estonia, Poland, Cyprus and Slovenia

Source: Copenhagen Economics: *Taxation of interest and royalties – impact assessment of amendments to the present Directive,* October 2010.

For interest payments it also seems to be the case that the excessive taxation problem is less serious in cases where cross-border payments are expected to be the largest, cf. Table 4. Here, we see that the countries in Group A account for 70-80% of the assets that generate cross-border interest payments.

Table 4. Indications of size of double taxation of interests across groups of countries

	Group A	Group B	Group C	Group D
Share of EU intra FDI stock	81.5	14.6	3.2	0.7
Share of EU interest income	73.2	21.0	4.1	1.8
Share of EU patent firm's financial revenue	82.3	15.3	2.0	0.4

Source: Data on the FDI stock is from Eurostat, *European Union Direct Investment*; data on interest income is from Eurostat, *International Trade in Services. Data on financial revenue is from Amadeus.*

2.2.5. Specific legal requirements in the case of payments made through permanent establishments

The Directive covers the cases where the companies make the payments through their permanent establishments. These are cases where the entity does not create a subsidiary to run its activities in another country but decides to do it through a fixed place of business without own legal personality, i.e. a branch. In the case of payments made through a permanent establishment, the Directive requires that these have to be a tax deductible expense for this taxpayer in the Member State where it is situated. The "tax-deductibility" requirement ensures that the benefits of the Directive accrue only when the payments are attributable to the permanent establishment. However, on its wording the Directive would not apply to cases where deduction is denied on other grounds, such as the failure to comply with all the formal requirements. This could result in an unjustifiable difference of treatment between subsidiaries and permanent establishments.

2.2.6. Risk of tax avoidance

The Directive exempts from withholding taxes in the host country interest and royalty payments but does not guarantee that its recipient is actually subject to tax on the corresponding income in the home country. This taxpayer may be exempted from corporate tax on these payments. There is a risk of non-taxation and abusive practices cannot be excluded. This is a result beyond the purposes of the Directive, whose recitals mention expressly that such payments should be subject to tax at least once in a Member State.

Thus, there could be an important loophole in the provisions of the Directive allowing for circumvention of taxation of interest and royalty payments. This could lead to a suboptimal allocation of capital and intangibles. We should recall that resources employed with the sole aim of reducing tax liabilities generate a welfare loss equal to the productivity of these resources in the best alternative use.

2.3. How would the problem evolve, all things being equal?

The compliance costs linked to withholding charges and the risk of double or excessive taxation result mainly in a tax discriminatory treatment between cross-border activities and purely domestic ones. Their direct effect is the increase of the cross-border investment costs, requiring higher yield thresholds in order to decide entering into international activities.

There are important disparities among the tax burden borne in the different international investments and according to the type of capital flows. As well, the lack of tax coordination would ease tax evasion since firms would exploit tax differentials with the aim of reducing their tax charges. Maintaining the current scenario will lead to continuous distortions on business behaviour: firms will respond to the risk of excessive taxation by taking advantage artificially of differences in effective tax rates in EU Member States through tax planning; they may make suboptimal choices regarding their cross-border investments, concerning the intra-firm capital structure or regarding their organizational form.

In conclusion, maintaining the current costs associated with the assessment of withholding taxes will have as a consequence less cross-border capital flows, reducing capital and technology transfers. The process of cross-border allocation of resources will be altered negatively.

The CE survey concludes that the Directive adoption made a significant contribution to eliminating withholding taxes on interests and royalties payments between associated companies. This study also mentions that there has been a trend in Member States to reduce these levies at source. In fact, between 2003 and 2009 taxation of royalties has been put on a more equal footing with interest payments in most EU countries. Also, an increasing number of DTCs have been signed and have reduced or eliminated withholding taxes between country pairs. Thus, there has been a convergence of national tax policies after the adoption and implementation of the Directive. This is a positive trend since the costs and distortions linked to withholding taxes have been reduced. However, there is no guarantee that this trend will continue in the future without further EU action in this tax policy area. Efforts should be made to reinforce tax policies that contribute to the smooth functioning of the internal market.

2.4. Who is affected?

The problems addressed by this initiative affect any business entering into cross-border transactions within the EU and making or receiving interest or royalty payments.

Interest and royalty payments are neither exclusive to any specific sector nor any geographical area. The size of the company is not relevant either. Concerning SMEs, there no specific elements in the problems detected that could affect them in a specific manner requiring special action. However, it is true that compliance costs typically constitute a larger share of their total costs.

Interest covers essentially payments from all sorts of credit, loans and similar financial transactions. The problems here addressed affect mainly the financial sector. Financial groups enter daily in internal lending and borrowing. Any solution to the problems identified will benefit more frequently their activities. Still, the capital structure of corporate groups in any sector of activity is generally made up of equity and debt. This means that all sectors of activity are affected.

Concerning royalties, these should cover payments in consideration for the use of intangibles, including industrial property, know-how and other information, processes and formulas relevant for business activities, as well as the consideration for the use of intellectual rights. Thus, sectors intensive in the use of technology will also benefit more often from this initiative as they are facing the tax burdens more frequently (see annex 7 for further details on the sectors affected). The same conclusion can be extended to sectors with intense use of intellectual property rights.

Member States are also affected. They receive income from withholding charges. At the same time, they assume the cost of the tax credit applied by those companies bearing withholding levies at source.

2.5. Treaty base and the subsidiarity principle.

The Interest and Royalties Directive, adopted by the Council in 2003, was based on Article 94 of the EU Treaty, currently Article 115 of the TFUE; thus, it refers to cross-border activities of multinational groups hampered by tax obstacles affecting the smooth functioning of the internal market.

EU action must respect the subsidiarity principle. This involves assessing two aspects. Firstly, it is important to be sure that the objectives of the proposed action could not be achieved sufficiently by Member States in the framework of their national constitutional system (necessity test). Withholding rates are fixed by each Member State in its national law according to its corresponding tax policy options. These charges may be reduced or excluded according to bilateral DTCs. However, each particular DTC fixes it own rate as a result of the trade-off between the two States agreeing it. The result is that withholding taxes vary according to each bilateral relation between the Member States. These cannot even succeed on having a unique tax rate for all their bilateral relations. Less, it does not seem that exemption could be achievable so that all the problems described – economic distortions due the existing different rates, distortions caused by tax relief requirements, those deriving from the different tax regime applicable across the capital flows, compliance costs and the cases of double taxation – will be hampering crossborder activities. The result is that there will not be a spontaneous coordinated action of the Member States.

The second aspect to consider is whether and how the objectives could be better achieved by action on the part of the EU (test of European value-added). The rationale for a European action stems from the cross-border nature of the problem and the impossibility for each individual Member State to establish a unique tax policy for itself and across the EU. Clearly, action at EU level will guarantee harmonized and coordinated tax policies in this particular taxation area. Member States would be bound by the exemption of withholding taxes to the same extent. This exemption will also diminish tax compliance costs faced by firms. This will reduce the costs of doing cross-border business and assimilate taxation of foreign income to that imposed on domestic profits with gains in productivity in EU Member States. It is therefore in the interest of all EU Member States to remove these obstacles to the free movement of capital across EU borders.

Thus, the subsidiarity principle is respected, since the policy objectives cannot be sufficiently achieved by actions of the Member States, and can be better achieved at EU level.

3. OBJECTIVES

3.1. What are the general policy objectives?

The proposal aims at strengthening the objectives pursued by the Interest and Royalties Directive, i.e. the elimination of the tax obstacles to the smooth functioning of the internal market concerning cross-border interest and royalty payments, as foreseen in Article 115 of the TFEU. In particular, the goal is that the tax treatment of these payments between companies of different Member States is not less favourable than that applicable to the same transactions carried out between companies of the same Member State. These aims should be accomplished with the least costs possible in terms of distortions and efficiency in the raising of taxes by the Member States.

In sum, the policy objectives are related to the identified problems as described above, but weighted according to their importance. For this purpose, we should take into account that the reduction of distortions due to differences in withholding rates will not solve those deriving from differences in corporate tax rates charged by the State of residence so that this should not be a primary objective. On the other hand, introducing less restrictive requirements for the withholding tax exemption and making them similar to those of the Parent-Subsidiary Directive would be efficient to reduce the distortions due to the difference tax regime applicable on different crossborder payments in each EU bilateral relation.

This initiative aims also at recasting the three existing Directives in this area of tax law. Gathering existing legislation in one single act will simplify, clarify and facilitate the application of harmonised law by businesses and professionals dealing with these matters.

3.2. What are the more specific/operational objectives?

The more specific objective of the proposal is the extension of the withholding tax exemption provided for in the Directive to a wider range of cases in order to reduce the economic distortions derived from the lack of harmonization, the compliance costs faced by companies and the risk of excessive or double taxation.

In particular, it is important to eliminate or reduce the distortions derived from the different taxation of the three types of capital flows, dividends, interests and royalties., which should also contribute to reduce the effect of the other distortions: being the tax requirements for the Directives benefits the same will diminish their importance as tax driven factor; as well, it will increase the number of cases enjoying tax exemption so that distortions due to different rates will also be reduced. These should be achieved by aligning the scope of the Directive with that of the Parent-Subsidiary Directive.

The Directive should also be amended with a view to close loopholes that may be abused for tax avoidance purposes. Some types of companies may engage in tax planning strategies to enjoy non-taxation of cross-border payments. The legislation should guarantee taxation at least once in a Member State.

3.3. Are these objectives consistent with other EU policies?

The objectives pursued by this proposal will have a positive impact in other policy areas of the EU. The Communication from the Commission, "Europe 2020 - A strategy for smart, sustainable and inclusive growth" COM (2010) 2020, includes within its priorities: smart growth, developing an economy based on knowledge and innovation; sustainable growth and promoting a more resource efficient, greener and more competitive economy; concerning the financial system, this document refers to the easy availability of credit. In this context, this document refers specifically to the contribution of tax systems to achieve its priorities. In particular, it refers to the reduction of administrative burdens and removing tax obstacles.

Thus, eliminating tax obstacles to cross-border interest and royalty payments should improve economic performance in the internal market. These actions will address and improve taxation associated to financing, technology, industrial and business information as well as intellectual rights. This should promote the corresponding activities and reinforce other EU specific policies in these areas.

4. POLICY OPTIONS

When assessing tax policy options, it should be kept in mind the aims of the Directive: the abolition of taxation at source on interest and royalty payments as the most appropriate means of ensuring the equality of tax treatment between national and cross-border transactions. This review process finds its origin in its Article 8, where it refers to the Commission's report of the Directive on its operation with a view to extending its coverage.

The proposed amendments should be proportionate. On the bases of the problems detected, it should offer solutions capable to meet the objectives fixed. The conclusions from previous sections of this impact assessment report is that the main cause of compliance costs, economic distortions and the risk of excessive or double taxation is the existence of withholding taxes charge at source; as well, the disparities on the taxation of the different types of cross-border capital flows alter business behaviour. Thus, amendments to the Directive should try to achieve tax neutrality in a larger number of cases so that economic operators allocate resources more efficiently.

Below we will refer to different policy options addressing the problems found in this area of taxation. Options 1, 2 and 3 are exclusive alternatives. Options 4 and 5 can be combined either with option 2 or with option 3.

4.1. What are the options for meeting the objectives and tackling the problems described? Description of the different options

Option 1 – No action

The first option is to maintain the current state of play and disregard any possible amendments. The legal forms out of the scope of the current Directive and payments between non-associated companies as defined in its text will have to face the problems described.

Option 2 - Extending the scope of the Directive to transactions between unrelated undertakings

It could be considered extending the benefits of the Directive to interest and royalty payments between unrelated undertakings, i.e. non-associated companies. In fact, international double or excessive taxation, burdensome administrative formalities and cash-flow problems, as cross-border obstacles are also present in the case of payments between unrelated parties. The result would be the full elimination of withholding taxes on all interest and royalty payments between companies covered by the Directive.

Option 3 – Aligning the requirements of the Interests and Royalties Directive to those of the Parent- Subsidiary Directive

One of the main problems detected is the distortions in business behaviour deriving from the different scope of the two directives ruling the taxation of cross-border capital flows. The tax regime applicable to dividends included in the Parent-Subsidiary Directive has a broader scope than that applicable to interest and royalty payments.

Firstly, the Directives are only applicable to companies which have a legal type listed in their corresponding annexes. The list of entities of both Directives is made by reference to the national company laws. The one annexed to the Parent-Subsidiary Directive is broader and includes in its scope the SE and the SCE. There is no obvious justification for these differences. The Parent-Subsidiary Directive applies to profit distributions and shares the aim of the Interest and Royalties Directive, the elimination of withholding taxes and the risk of double taxation in the case of cross-border capital flows. The amendment to the Interest and Royalties Directive would consist of the extension of its list with a view to make it identical to that of the Parent-Subsidiary Directive.

The second issue to address concerns the requirements to consider that companies are associated. In the Interests and Royalties Directive association is deemed to exist when one of the companies has a direct minimum holding of 25% in the capital of the other company, or a third company has a direct minimum holding of 25% in the capital of both the payer and the recipient companies. However, the Parent-Subsidiary Directive reduces the threshold for 'holdings' to apply its benefits to 10% of capital or voting rights and indirect participations can be computed. Again, there is no obvious justification to maintain these differences. The amendment to the Interest and Royalties Directive would consist of the reduction of the minimum shareholding requirements from 25% to 10% and including indirect shareholdings to calculate if the minimum participation exists.

This tax policy option extends the scope of the withholding exemption and is useful to tackle the distortions derived from different taxation of cross-border capital flows. The cross-border capital flows often affected by these problems take place between associated companies and will therefore be closely related to FDI. EU countries' outward FDI has increased enormously during the last few decades, and the stock of total outward FDI by EU companies constitute 60% of GDP out of which the stock of intra-EU FDI is 40%[21]. These figures show the importance of such type of international activities. Limiting the amendments to transactions between associated companies would be proportionate to the goals pursued.

Option 4 – Clarifying the tax deductibility requirement applicable to payments made by permanent establishments

The amendment would consist of rewording the Directive text in order to make it more precise by replacing "tax-deductible expense for the permanent establishment" with "expense attributable to the permanent establishment". This modification is important for the sake of legal certainty. This text would contribute to avoid tax disputes over these legal references and will achieve better the aim pursued. On the other hand, it will not extend the scope of the withholding tax exemption. Both tax authorities and taxpayers would benefit from a more clear text and the reduction of juridical disputes.

Option 5 –Requiring for the exemption of withholding tax that the recipient of the payment is subject to tax on the income derived from it

At the time of the adoption of the Interest and Royalties Directive, the statements for entry in the minutes of the Council mentioned that "the Council and the Commission agree that the benefits of the Interest and Royalty Directive should not accrue to companies that are exempt from tax on income covered by this Directive". The Council invited the Commission to propose any necessary amendments. The recitals of the Directive already provide that "it is necessary to ensure that interest and royalty payments are subject to tax once in a Member State". For that purpose, the Commission adopted the 2003 proposal which was close to an agreement in the ECOFIN Council.

The Commission withdrew this proposal when adopting its Communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, Commission Work Programme 2010 - Time to act, COM (2010) 135 final. However, this is due to the fact that this new recast of the Directive was foreseen: Annex II of this Communication includes a revision of the Directive scope among the indicative list of

21 Source: Eurostat, *European Union Direct Investment*.

possible strategic and priority initiatives under consideration. Thus, the amendments proposed in 2003 are still in the Commission's agenda and are considered to be included in this recast.

This option is the most suitable one to tackle loopholes that could ease tax avoidance, since taxation is guaranteed: either the exemption of withholding tax on the payment in the host country is denied or the beneficiary of the payment is taxed in the residence State.

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

The option of repealing or reducing the scope of the Directive has never been on the table. It took around 5 years of discussions and negotiations to get the measures into place and it has been in operation for 6 years. This is the first review and clear benefits are identified from its existence. The Commission's report of the Directive concludes that the overall implementation has been satisfactory. As mentioned before, the adoption of the Directive produced a tax policy convergence but nothing guarantees that this trend will continue.

It could also be considered combining option 2 with abolishing withholding taxes on dividends between unrelated companies or combining option 2 with the extension of the coverage of the Parent-Subsidiary Directive to below the 10% minimum shareholding threshold. However, this initiative responds to the conclusions of the Commission's report on the Directive, foreseen only to extend its particular scope, issue that had been carefully dealt with. It does not pretend to very ambitious. Concerning the Parent-Subsidiary Directive, it is currently the object of a different recast proposal. Both Directives have had their own legislative process and their own path traditionally. This recast does not seem the suitable time to address more ambitious options targeting the scope of the Parent-Subsidiary Directive.

Another solution could be extending the Directive to other types of companies beyond those referred to in the Parent-Subsidiary Directive. However, such a proposal would be contrary to one of the main objectives of this recast: making the scope of this Directive similar to that of the Parent-Subsidiary Directive. The public consultation launched in pararell with this initiative shows more consensus on aligning both application scopes (89% of the responses received) that extending the Directive to a wider number of entities (47%).

On the other hand, the Directive covers payments between two different companies and does not refer to intra-company situations, for instance actual or notional payments between a head office and a permanent establishment, or between two permanent establishments of the same company. The Commission' report refers to them and to the OECD work on the attribution of profits to permanent establishments, where the question had arisen. The issue arose since during the debate in the framework of that organization some OECD countries had indicated that they would be minded to impose a withholding tax on the above payments. Taxation at source on intra-company payments would create disadvantages for crossborder investment similar or identical to those that prompted the adoption of the Directive. The report stated that if that would be the result of the work undertaken, it would seem appropriate to consider extending the scope of the latter to cover such payments. Finally, this initiative does not deal with this issue since the OECD did not conclude on the possibility to charge withholding taxes on notional payments.

5. ANALYSIS OF IMPACTS

5.1. Impacts of the different options

This section deals with the impacts of the policy options described. These impacts are largely economic by nature, as we cannot expect that any of the options would have significant environmental or social impacts, except a slight positive impact on employment through productivity increases.

The policy options proposing the extension of the current coverage of the Directive would reduce the number of companies which currently pay withholding taxes. As described in section 2, withholding taxes entail distortions and costs to the companies. Hence eliminating withholding taxes would bring forth economic benefits of the following kind. First, the gap in the rates of return between cross-border and domestic investments would be reduced, which would encourage cross-border investment and enhance in this way productivity, technological transfer and economic growth. Through this channel also employment could be enhanced. Second, the costs of doing business in the EU would be reduced. Compliance costs related to withholding taxes are a particular form of such costs and may be significant to the companies subject to withholding taxes.

These tax policy options would also entail some costs to the Member States, as eliminating withholding taxes would reduce their tax revenues. On the other hand, these revenues costs would be mitigated by the fact that the countries receiving withholding taxes would also reduce tax credits provided for in DTCs or in domestic laws.

The scope of the Directive is limited to EU companies. Thus, the tax policy options described above will not have any effect in third countries. Non-EU firms may, however, benefit from the proposed amendments to the Directive to the extent that they own EU subsidiaries. But the effects on these are computed within the general effects on EU based companies.

We will refer to the impact of the policy options on the economic distortions described, on compliance costs for companies and on the Member States' tax revenues. Concerning their measurement, approximate estimates of their magnitude are given, based on the CE study.

Option 1 – No action

The current tax regime applicable to cross-border transactions of interests and royalties creates the problems that have been described in section 2. We should recall that withholding taxes increase the cost of doing business, reduce cross-border capital flows and, as a consequence, diminish productivity. Companies facing high effective withholding taxes might engage in tax planning and restructuring processes to in order to reduce tax burdens and compliance costs. On the government side, opportunities for tax avoidance result in a lost of tax revenues. Leaving the current Directive unchanged would not solve these problems.

In particular, this situation will limit the interest in adopting the legal form of a SE or of a SCE, legal types which are not currently included in the Directive scope.

Concerning the legal context of this tax policy area, it will continue to be established in the four Directives and the annexes of the Accession Treaty of Bulgaria and Romania in the absence of a consolidated text. This situation results in legal complexity for those needing to consult the legislation in force.

Option 2 - Extending the scope of the Directive to transactions between unrelated undertakings

Economic benefits

The exemption of withholding tax will eliminate the differences found in withholding rates applicable in the different country pairs. These should reduce the distortions in the patterns of capital flows. As well, the suppression of some of the tax requirements to enjoy the Directive should contribute to reduce distortions in holding structures and organizational forms currently faced by firms. However, the differences in taxation of dividends, interests and royalties will remain and their distortive consequences regarding the capital structure of companies and their allocation of intangibles.

Social impact

The reduction of compliance costs, risks of double taxation and lower liquidity costs deriving from this option would reduce the costs of FDI-related activities and spur cross-border investments. This could have a positive impact on productivity and employment.. The gains are larger when the EU firm's activities give access to new technology and knowledge. Thus, outward FDI has a positive impact on employment in EU countries[22]. However, this impact is likely to be small and it has not been possible to quantify it in the impact assessment.

Impact from the point of view of companies

This option would eliminate withholding taxes on all cross-border payments for the companies not currently covered by the Directive, i.e. to those with holding links lying below the current 25% ownership interval. As already mentioned, in the Amadeus database used in the CE study such companies represent 12% of holding links (the share of holding links within 10-25% ownership interval is 5% and the share of those within 0-10% interval is 7%, see tables in annexes 8 and 18). These companies represent, however, a large share of employment and turnover: 32% (5% + 27%) and 28 % (4% + 24%) respectively[23]. Hence the economic benefits that could be obtained by removing withholding taxes on cross-border payments for these companies could be significant.

Moreover, it should be taken into account that the above presented shares do not cover SMEs[24], since these are not included in the Amadeus database consulted. Hence the share of companies benefiting form the removal of withholding taxes on cross-border payments could actually be larger than indicated by the numbers above, and also the economic benefits.

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22 Cuyvers, L., Dumont, M., Rayp G. and Stevens, K. (2005), "Home Employment Effects of EU Firms' Activities in Central and Eastern European Countries", Open Economies Review 16, 153–174; Falk, M. and Wolfmayr, Y. (2008), "The Impact of Outward FDI in Central and Eastern Europe on Employment in the EU-15 Countries", FIW Research Report 16; and. Konings, J. (2004), "The Employment Effects of Foreign Direct Investment", EIB Papers 9.

23 These shares are lower, however, if weighted by intangible assets (28% and 13% respectively) and also compared with the share weighted by financial assets (32% and 15% respectively) implying that cross-border payments between the companies mainly take the shape of interest payments. See annexes 13 and 19.

24 For the purposes of this impact assessment and due to the use of the Amadeus database as source of information, SMEs are: in UK, Germany, France, Italy and Spain, those companies with operating revenue below €1.5 million, or total assets below €3 million, or less than 20 employees; in all other countries, they are companies with operating revenue below €1 million, or total assets below €2 million, or less than 15 employees.

As explained in section 2, paying withholding taxes on cross-border payments and the procedures needed to avoid double taxation could entail considerable compliance costs for companies. The full elimination of withholding taxes would entail compliance cost savings in the amount estimated above: €126 million, which would constitute a direct economic benefit for the companies not currently covered by the Directive.

It should be kept in mind, however, that the above estimates are based on a number of assumptions and should therefore be taken with caution. Thus, the amount of capital flows derives from statistical data; its amount subject to tax has been determined by grouping them in large economic categories regardless of the actual qualification for tax law purposes; as well, the gross amount of tax revenues has been calculated on the bases of average withholding tax rates; concerning compliance costs of refund procedures, it has been estimated in a forfeit, 2% of the refundable amount. An additional caveat is that they do not cover SMEs. Compliance costs could constitute a larger burden on smaller firms compared to larger firms that absorb such costs more easily. Extending the coverage of the Directive to cover any cross-border interest and royalty payment is therefore likely to reduce administrative burdens laid upon SMEs and at the same time remove the financial burden of paying withholding taxes.

Impact from the point of view of the Member States

The extension of the withholding tax exemption may reduce the tax revenues of the source States as host countries; at the same time, as home countries, they will see reduced the amount of tax credits applied by their companies to relieve double taxation due to the elimination of the withholding taxes charged at source.

For interest payments, we find that the tax revenue impact of extending the scope of the Directive will be limited in more than half of the EU Member States since cross-border interest payments are generally exempted from withholding tax due to national tax law or DTC. In total, 13 countries will be affected by the amendments with respect to interest payment. By comparison, only 5 EU Member States levy no withholding taxes on cross-border royalty payments to other EU Member States (see annex 9).

As regards withholding taxes on interest, the CE survey shows that the total EU outflow of interests is more than €500 billion out of which it is expected that €334 billion go to other EU countries[25]. According to this study, the tax revenue impacts of eliminating withholding taxes on interest payments will be very limited. *First*, 74% of the interest payments are exempted from withholding tax due to national tax law in the host countries. Tax revenue in these countries will therefore not be affected. The remaining 13 EU countries that impose withholding taxes on outgoing interest payments – Belgium, Bulgaria, the Czech Republic, Greece, Hungary, Ireland, Italy, Latvia, Poland, Portugal, Romania, Slovenia and United Kingdom - account for intra-EU interest payments equal to almost €11.2 billion. These outgoing interest payments constitute 0.22% of GDP in these countries (see annex 10). Second, only a minor part of the cross-border interest payments are affected by the present Directive or even the proposed amendments. This is so because the measure of EU cross-border interest payments originates from balance sheet information and therefore captures all

[25] Source: Eurostat, *International Transactions in Interests and Dividend Payments*. The expected EU outflow to other EU countries is based on the split between intra-EU and extra EU FDI stock; the former is 2/3 of the total flows.

types of cross-border interest payments, including intra-bank payments, governmental interest payments, payments between persons and payments between (affiliated and non-affiliated) companies. However only 10% of the gross debt position in EU countries is between companies and an even smaller share is intra-firm debt[26]. Under the assumption that the interest rate paid on the different types of debt is the same, and applying the average withholding rate in the countries that impose withholding tax on cross-border interest payments, 7,1% (annex 11), the CE survey finds that gross income from withholding tax on inter-company payments amounts to €0.8 billion. The loss of tax revenues from eliminating withholding taxes on outgoing interests would, however, be offset by gains from lower credits for withholding taxes paid in host countries. According to the CE survey, it is likely that netting for this effect would amount to a loss not exceeding €200 to €300 millions (see annex 10).

Concerning royalty payments, the total EU outflow of royalties and licences fees is €46.5 billion or 0.4% of GDP[27]. By assuming that intra-EU payments constitute two thirds of these payments (using the same split as between intra-EU and extra-EU FDI stock) the intra-EU royalty payments are estimated to be around €31 billion in 2008. This amount must be further reduced by the fact that part of the cross-border payments is exempted from withholding tax due to national tax law in certain countries (Luxembourg, Malta, Netherlands, Sweden and Slovak Republic). In the remaining 22 EU countries intra-EU royalty payments are estimated to be equal to €23,3 billion (see annex 12). By applying the average EU withholding tax rate of 5,5% on this amount (annex 13), the gross income from outgoing royalty payments before considering the effect of the present Directive is estimated to be around €1.3 billion for EU as a whole. It must be further taken into account that losses on revenues on outgoing royalties will tend to be offset by gains from lower credits for withholding taxes paid in host countries for incoming royalty payments. Some countries will indeed gain on a net basis, namely those with a positive balance in royalty payments – Denmark, France and the United Kingdom (see annex 12). As well, the present Directive covers a substantial part of the revenues associated with outgoing royalty. Hence it is likely that netting for this effect leaves very limited net revenue effects: for the seven countries with the largest negative royalty balances as a share of GDP – Bulgaria, the Czech Republic, Greece, Poland, Portugal, Romania and Slovakia - , the loss should not exceed €100 to €200 million (annex 12).

Concerning the obligation to transpose the amendments into national legislation, this option would go beyond of the current scope of the harmonized corporate tax law. The Directive and the Parent-Subsidiary Directive limit their coverage to associated companies. Extending the Directive benefits to unrelated undertakings would be a new feature affecting the EU tax relations of all Member States. It is difficult to foresee how this proposal could affect national tax policy and practices and its interrelation with the DTC networks.

Option 3 – Aligning the requirements of the Interests and Royalties Directive to those of the Parent- Subsidiary Directive

Economic benefits

[26] Source: *The Quarterly External Debt Database* (QEDS), jointly developed by the World Bank and the IMF.

[27] Source: Eurostat, *International Transactions in Royalties and Licence Fees.*

Under this option the share of companies that would not need to pay withholding taxes on their cross-border payments would be larger than in the current situation, although not as large as under option 2. Hence economic benefits would be of similar nature as under option 2, but somewhat smaller in magnitude. However, the harmonization of the conditions to apply the two directives on taxation applicable to the different types of capital flows will contribute to a more neutral regime. This option offers better results that option 2 concerning the reduction in the economic distortions on capital structure of companies and on their allocation of intangibles. In the following it is examined more closely which share of companies would benefit from extending the coverage of the Directive as described in option 3.

<u>Social impact</u>

This option should also have a positive impact on employment for the reasons explained under option 2, though smaller than those derived from this latter option.

<u>Impact from the point of view of companies</u>

a. Extending the list of legal forms benefiting from the Directive

Option 3 refers to the harmonisation of the list of legal types covered by the Interest and Royalty Directive with the same list annexed to the Parent-Subsidiary Directive. We find that in 11 countries (Bulgaria, Cyprus, Estonia, Finland, Latvia, Lithuania, Malta, Poland, Portugal, Romania and the United Kingdom) the list of entities covered by the Interest and Royalty Directive is identical to the list of entities covered by the Parent-Subsidiary Directive (see annex 14). For the remaining 16 countries the impact of this option will depend on the extent to which the interest and royalty payments are concentrated in companies where the payment is already covered by the Directive.

As already mentioned, according to the CE survey, in 82% of the cases, both the parent company and the subsidiary have a legal form that falls under the scope of the Directive; nearly 95% of the tax base corresponding to royalty payments is already covered; approximately 90% of the tax base corresponding to interest payments is also under its current coverage; in fact, the main part of the economic activity (82% of total employment and 85% of total turnover) is concentrated in the subsidiaries that already fall under the Directive (see annex 15).

We are also interested in assessing to what extent the volume of interest and royalty payments are affected by the current Directive. The CE survey assumes that if all of the intangible fixed assets are located in the parent companies that do not fall under the Directive (the remaining 18%) then the Directive will continue to pose a constraint of the flow of payments between the two entities. It therefore weights the employment and turnover data by the amount of assets in the parent company. If the weighted and the unweighted numbers are the same, the parent companies hold the same amount of assets as the parent companies that do not fall under the Directive. This survey finds that the parent companies hold more assets than the average (see annex 15). This evidence indicates that the current Directive does not seem to constitute a binding constraint on cross-border interest and royalty payments between companies at the aggregate level. However, for a small number of companies the legal form could be a binding constraint and for these companies the amendment could be important. The CE survey expects that this amendment would increase up to 84% of the holding links that will be covered by the Directive, representing nearly 97% of the tax base corresponding to royalty payments and approximately 92% of the tax base corresponding to interest payments (see annex 16).

b. Extending the Directive to cover indirect holdings

In the first place, it should be mentioned that there are already two Member States (Belgium and Spain, see annex 17) that have implemented the Directive generously and have provided the computation of indirect holdings to establish that the companies are associated.

This amendment could have some impact on tax planning opportunities of companies. In most cases, where indirect holdings are above 25% whereas direct holdings fall short of this threshold, there are ways in which a tax planning company can alter the finance and holding structure in order to ensure coverage by the Directive. However, it is important to keep in mind that tax planning may be costly since it requires detailed knowledge of national tax laws across EU countries. According to the CE survey such an amendment may produce benefits in terms of increased flexibility and lower restructuring costs.

c. Reducing the shareholding requirements from 25 to 10%

According to the CE study, the holding share in EU firms is concentrated around 50% and 100%. Since the Directive offers more favourable tax treatment for associated entities if the direct ownership share is at least 25%, tax planning companies might take advantage of this by increasing their ownership share above 25% of their intra-group entities. By lowering the threshold value for the ownership share from 25 to 10%, the amendments of the Directive might allow EU firms to move closer to their preferred ownership structure and therefore reduce or eliminate the distortion caused by the limited coverage of the present Directive. In fact, the holding links that lie in this ownership interval, restricting it to companies having a legal form under the Directive as amended, accounts for a small number, only 5% of entities, i.e. 5% of the holding links. The subsidiaries that would benefit from lower holding requirements only account for a small share of employment and turnover, approximately 5% (annex 18). Hence, the economic benefits of this extension would be relatively limited.

Savings in compliance costs

To estimate the compliance cost savings that could be expected from this option, the CE survey differentiate between interest and royalty payments. Thus, most of the interest payments between non-financial institutions that fall outside the scope of the present Directive will take place between associated companies since direct loans between non-associated companies are relatively rare. This study expects 80-90% of the compliance cost savings to materialise under this option 3: that is, 80 to 90% of the 48 millions of the compliance costs accounted for interest payments, €38,4–43,2€. The opposite is the case for royalty payments. OECD[28] finds that the proportion of EU companies' patent portfolio that is being licensed to non-associated companies lies in the range 80-100%. Thus, out of the €78 millions of compliance costs associated to royalty payments, the economic gain linked to this option would amount €0-€15,6 millions. In total, out of the compliance costs of €126 million, this option 3 is estimated to offer a saving of €38,4-€58,8 millions.

28 OECD: *Who Licenses Out Patents and Why? Lessons from a Business Survey- STI Working Paper 2009/5- Statistical Analysis of Science, Technology and Industry.*

Again, it should be kept in mind that the above estimates are based on a number of assumptions and should therefore be taken with caution.

Impact from the point of view of the Member States

As we can infer from the analyses of option 2, the net revenue effects from removing withholding taxes on all cross-border payments would be relatively limited. In the case of option 3 these effects would affect the Member States in similar terms but in a more limited way, since the amendments now considered are less ambitious. Concerning the obstacles that Member States may find to transpose the new harmonized rules they should be minor. We should mention that they have already the experience gained with the obligations imposed by the Parent-Subsidiary Directive.

Concerning the tax revenue effects of this option, the CE survey considers that it is possible to make calculations on the basis of the weights of the interest and royalty transactions described above. Thus, if the total reduction of tax revenue expected from the elimination of withholding taxes in all transactions of interests amount €200-€300 millions, this particular option 3 would account for a reduction of 80 to 90%, that is €160-€270 millions. In the case of royalties, the tax revenue redaction estimated was €100-€200 millions. This option would affect to 0-20% of this type of transactions, so that the reduction of tax revenue could be estimated at a range of €0-€40 millions. In total, the tax revenue reduction could be estimated roughly at a range of €160-€310 millions.

Option 4 – Clarifying the tax deductibility requirement applicable to payments made by permanent establishments

The amendments that would derive from this tax policy option look for legal certainty and the reduction of conflicting cases in marginal circumstances. This could be concluded from the IBFD survey, which did not find cases in the surveyed Member States of relief having been denied on the grounds that the payment was a non-deductible expense. The economic impact of this tax policy option should be negligible.

As to the transposition of the new legal text, it should not cause major problems. The issue is discussed in the Commission's report of the Directive where the main elements of this amendment are considered. Any tax expert can evaluate the problem raised and the solution foreseen. The changes in national legislation should be minor and easy to implement.

Option 5 –Requiring for the exemption of withholding tax that the recipient of the payment is subject to tax on the income derived from it

The aim of this tax policy option is to tackle tax avoidance strategies. On the government side, opportunities for tax avoidance result in a loss of tax revenues. Also, tax administrations have to incur in administrative costs since they have to conduct investigation procedures related to tax avoidance practices. On the firm side, tax planning activities result in suboptimal choices, and the administrative and compliance costs of tax planning largely represent unproductive use of scarce resources. Hence, this option could potentially have a positive impact on the tax revenues in the Member States. However, it is difficult to make estimations and a proper assessment of this revenue impact and of the administrative costs associated with tax planning. We do not have statistics offering relevant information to conclude on the quantitative consequences derived from the abuse of the exemption of withholding taxes on interest and royalty payments combined with the non-taxation of the corresponding income in the home country.

Concerning the obstacles that may be found to implement this option, we should mention that in the ECOFIN Council invited the Commission to present a proposal to address this issue. In addition, if Member States want to check if taxpayers are subject to tax on the payments received in their home country, they have cross-border administrative cooperation. Council Directive 77/799/EEC of 19 December 1977 concerning mutual assistance by the competent authorities of the Member States in the field of direct taxation[29] establishes the rules for administrative cooperation and the exchange of information between Member States with the purpose, among other things, to enable Member States to carry out a correct tax assessment in the case of cross-border activities.

Table 5. Table of impacts

	Option 1 **No action**	**Option 2** **Extension of the exemption to unrelated undertakings**	**Option 3** **Aligning with Parent-Subsidiary Directive**	**Option 4** **Exemption of payments connected to PE**	**Option 5** **Subject to tax requirement on the recipient company**
Reduction of distortions due to differences in withholding rates	--	++	+	=	+
Reduction of distortions due to requirements for the exemption	--	++	+	=	=
Reduction of distortions due to different taxation of dividends, interests and royalties	--	-	+	=	=
Savings in compliance costs	None	€126 mill.	€38,4-58,8 mill.	negligible	Unknown
Changes in tax revenue	None	- €300-500 mill.	- €160-310 mill.	negligible	Unknown

Note: Positive: +; Strongly positive: ++; Negative: -; Strongly negative: --; Neutral/marginal: =

5.2. Comparison of options

The objective of this initiative is the elimination of withholding taxes in a wider range of cases with the final aim of reducing the economic distortions, the compliance costs and the risk of excessive or double taxation linked to them. As a more specific objective, it is important to highlight the need to have a more neutral tax regime applicable to dividends,

[29] DO L 336 de 27.12.1977, p. 15.

interest and royalties by aligning the scope of the Directive with that of the Parent-Subsidiary Directive.

In view of the above analysis, option 1, which represents the business as usual scenario, should be rejected. Withholding tax rates continue to affect the investment decisions and financing structures for a number of firms within the EU. It is shown in this impact assessment that the static budgetary costs of extending the Directive benefits to a wider set of firms tend to be small while providing benefits in terms of fewer distortions, reduced compliance costs for EU firms and gains in productivity following from increased cross-border investments. Hence, other policy options largely outweigh the business as usual scenario.

On the other hand, both options 2 and 3 give important advantages. They would meet the objective fixed to extend the Directive coverage. At the same time, they could be complemented with the policy options 4 and 5, which as such will surely contribute to a better functioning of the Directive and should for this reason be included in any future proposal for its amendment. Thus, we will refer to two alternatives: the alternative I would combine options 2, 4 and 5 and the alternative II would combine options 3, 4 and 5.

Concerning the reduction of economic distortions due to the differences in withholding rates, while the alternative I would have more positive effects than the alternative II since it covers all payments between companies, both solutions pose the question of their efficiency and their coherence. Alternative I implies a bigger impact on public finances. The reduction of Member State tax revenues is an important element to consider as stated in the Commission Communication on the 2020 strategy, where reference is made to the need for consolidation of public finances in the current crisis context. The alternative I would have a bigger impact in the reduction of Member States tax revenue (roughly estimated at a range of €300-€500 millions) than alternative II (€100-€240 millions), As well, the difficulties for implementation will be bigger in the case of alternative I since it would be the first case where the taxation of the relations between non-associated parties is harmonized. At the same time, the coherence of both options is also limited: since the payments will no longer suffer withholding taxes, the relative importance of the corporate tax rate charged by the home country will increase. Thus, the major distortions could now be due to the different corporate tax rates in force in the home Member States; it is not proposed to harmonize this tax element which is a general feature applicable to all the taxpayers' income. Thus, the reduction of the distortions due to different withholding tax rates should be weighed against these considerations.

As regards the distortions due to the requirements to enjoy the Directive benefits, the alternative I also have slightly more positive effects than the alternative II since it will eliminate the condition that companies are associated. However, this same effect restricts the capacity of this alternative to reduce the distortions deriving from the different tax regime applicable to the different types of capital flows (dividends, interest and royalties) as we will see below. Thus, such a proposal will not be coherent with other objectives of this initiative. Nor is it very efficient due again to its bigger budgetary costs for the Member States and the implementation costs. Concerning alternative II, the reduction of the threshold holding to be considered as associated companies should allow EU firms to move closer to their preferred ownership structure and therefore reduce the distortion caused by the limited coverage of the present Directive. As regards the computation of indirect holdings, it may produce benefits in terms of increased flexibility and lower restructuring costs. If such a proposal would be adopted, companies will not be forced to maintain holdings over a certain limit to enjoy the Directive benefits, reducing part of the financial costs linked to a particular holding structure.

It will neither have such negative consequences as those attributable to alternative I, since the tax revenue effort and the implementation costs will be lower.

On the other hand the alternative II will reduce the economic distortions due to the different scope between the Directive and the Parent-Subsidiary Directive. The exemption of withholding taxes on dividends, interest and royalties will be applicable under the same circumstances. The firms' legal form, holding structure and their allocation of intangibles will not be altered so negatively as up to present due to the different withholding tax regime across the different capital flows. The new legal context will offer a more neutral solution and reduce the influence of taxation on business decisions. It can be said that it is an effective, since it meets this particular achievement; it is efficient since there are no important costs associated to it; and coherent with the other objectives of reducing compliance costs and the other distortions. The alternative I will not have this effect and these distortions will remain since it would maintain the different treatment of different capital flows: the exemption of withholding taxes on dividends would still require a minimum holding between the payer and the recipient of 10% while the benefits on interest and royalty payments would not require so. Different types of capital flows are to some extent substitutable and the differences in tax treatment have an impact on the investment decisions of the EU investors. A reduction of the tax costs associated with interest and royalties as compared to dividends may lead to sub-optimally high levels of debt and inefficient allocation of intangibles. The financial structure of groups and the allocation of intangibles will be decisions where the tax factor will have to be weighted. This, this latter alternative is inefficient to achieve this particular goal.

As regards the reduction of compliance costs, the alternative I would have bigger effects (roughly estimated at €126 millions) than the alternative II (roughly estimated at a range of €38,4-€58,8 millions) since it would affect a larger number of transactions. Again, these results should be measured considering the negative consequences on public finances and implementation costs, larger in the case of Alternative I. This would reduce the efficiency and coherence of this proposal.

Concerning the effects on the elimination of excessive or double taxation, this impact assessment considered this as minor problem since in the current scenario it appears in a limited number of cases (see section 2.2.2). Thus, the achievement of this objective should have a minor weight at the time to value the different alternatives. For the reasons already referred to, alternative I is more effective (wider exemption) but less efficient (more tax revenue and implementation costs) and less coherent (could increase distortions due to the different tax regime applicable to capital flows).

SMEs are likely to benefit form both alternatives. In the first place, when the legal types that they normally adopt are included in the list annexed to the Directive. It should be mentioned that the economic impact of alternative I assumes that the list of entities covered by the Directive is extended to make it equal to that included in the Parent-Subsidiary Directive. In the second place, we should recall that for these, the weight of tax burden is proportionally higher.

It is possible to summarize these comparisons in the following table.

Table 6. Comparison of alternatives

Objectives/ Options	**Reduction of distortions due to differences in withholding rates**	**Reduction of distortions due to requirements for the exemption**	**Reduction of distortions due to different taxation of dividends, interests and royalties**	**Savings in compliance costs**	**Elimination of double taxation**
Option 1	Ineffective	Ineffective	Ineffective	Ineffective	Ineffective
Alternative I	More effective, but lower efficiency and coherence	More effective, but lower efficiency and coherence	Ineffective	More effective, but lower efficiency and coherence	Effective, but lower efficiency and coherence
Alternative II	Effective, higher efficiency and coherence	Effective, higher efficiency and coherence	Very effective, efficient and coherent	Effective, higher efficiency and coherence	Effective, higher efficiency and coherence

The public consultation offered also a view of stakeholders on these tax policy options[30]. The first conclusion from the responses received confirms their interest in the initiatives raised by the Commission services. There is a clear tendency to support the need to take tax policy action and amend the Directive. Only 7% of the replies do not consider necessary to update the list of entities covered by the Directive and 4% do not agree to the change of the shareholding threshold to consider entities as associated. Thus, option 1 receives hardly any support. As well, it can be concluded that the majority shows alternative II as preferred option (aligning the list of entities to that of the Parent-Subsidiary Directive is supported by 90% of the responses; the computation of indirect holdings, 91%; lowering the threshold requirement to 10%, 87% of replies). On the other hand, the main option of alternative I, extending the Directive to payments between unrelated undertakings receives very little support, 28%. Finally, the public consultation did not address questions on option 5 since this issue was brought up in the ECOFIN Council meeting that adopted the Directive in 2003. There, it was agreed to require from the Commission a proposal to deal with the issue. That same year the proposal was adopted by the Commission. The ECOFIN Council did not agree on a text due to the opposition of one Member State in successive discussions. Still, there is a need to maintain this amending proposal and included in this new initiative for a recast. In this context, it did not make much sense to include the issue in the public consultation since the decision to amend the Directive on this particular topic had been taken at that time.

Member States had also an opportunity to stress their views on these options during a meeting to discuss the Commission's report on the Directive held on 23 November 2009. The Commission services could consider which the general position on these matters was: they were more included to accept initiatives on the option 3; some of them rejected clearly any amendment on the basis of option 2. Concerning the technical modifications proposed in option 4, a majority of the Member States' delegates understood the problem and agreed the need for a solution. Concerning option 5, it has been already mentioned that the subject was brought up in the ECOFIN Council agreeing on the Directive and there has been a large majority of Member States supporting the Commission initiatives in this area. However, it

30 See annex 19 including a briefing of the responses received.

should be stressed that the said meeting had a technical purpose and delegations were not asked to take a political position on the initiatives. In fact, a number of delegates remained silent during the debate.

On the basis of this analysis, we prefer the alternative II, combining options 3, 4 and 5 since it offers a more balanced solution between benefits and costs. As already mentioned, this solution gathers more support from the public than alternative I.

As regards the distribution of alternative II impacts between the Member States, it will rely on the importance of reduction of withholding tax revenue currently obtained. Following the tables 1 to 4 of this report, it can be concluded that Member States with high withholding taxes on interest and royalty payments will be more affected. In order to measure more properly this effect, it also should be taken into account the actual capital flows affected by the initiative comprised in these options. In the case of royalty payments, the more affected Member States are the Czech Republic, Estonia, Latvia, Lithuania, Romania, Slovakia and Slovenia. In the case of interest payments, these are Cyprus, Estonia, Latvia, Lithuania, Poland, Romania and Slovenia. However, it has to be considered the reduced amount of the flows affected as shown in tables 2 and 4.

6. MONITORING AND EVALUATION

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

The main objectives of the Directive are the elimination of the risk of excessive or double taxation, the reduction of compliance costs and less tax distortions in the functioning of the internal market.

The Commission will ensure Member States' compliance with the obligations laid down in the amending Directive. Its services will offer assistance for the implementation of the legislative changes in the form of transposition workshops with tax authorities and officials from all the Member States or in the framework of its working parties for direct tax matters. Further discussion and guidance in respect of key Directive concepts may be necessary in order to achieve uniformity of interpretation and reduction in legal uncertainty.

As entrusted by the TFEU, the Commission will take the necessary and due action if any of them fails to respect its duties concerning the implementation and application of Community Law.

Concerning the performance of the internal market, it will be difficult to establish a closed and direct link between the amendments proposed and the reduction of tax distortions. Still, the increase in tax revenues or in tax bases corresponding to income from debt claims or from intangibles in the home countries could be a good approximation. However, there are other variables to consider which may have an influence on these indicators. In broad terms, the total amount of cross-border interest and royalty payments would show the evolution of these transactions after the implementation of the amendments.

Other indicators should be referred to business behaviour and analyse compliance costs, companies capital structure and organizational form, as well as the holding structure of company groups.

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

The evaluation of the consequences of the application of the legislative measure could take place three years after the entry into force of the legislative measures implementing the Directive. This period should allow the Commission services to gather sufficient and relevant data after a minimum one year period of the application of the amendments, to analyse the results and to draw up some conclusions. The Commission should submit to the European Parliament and the Council a report on the technical functioning of the Directive as amended.

The content of such a report will vary according to the scope of the Directive as finally agreed in the Council. It may be necessary to evaluate the need of further developments to fully achieve the objectives pursued.

Annex 1

Withholding taxes on interests from non-treaty countries in 2003 and 2009

Country	Tax rate 2003	Tax rate 2009	Notes
Austria	0% (25%)	0% (25%)	25% tax applies to interest paid on loans secured by mortgage on immovable property. A withholding tax of 25% is levied on bank deposit interest paid to resident individuals and, unless the company opts to be paid gross, on such interest paid to resident companies.
Belgium	15% (0%)	15% (0%)	Exemptions include interest on government bonds, registered bonds, mortgage loans on immovable property and bond interest paid by non-residents, interest on registered corporate bonds and interest on registered bonds issued by resident banks and other financial institutions as well as interest paid in relation to loans to non-profit associations and other fixed revenue loans issued by corporations and deducted from income.
Bulgaria	15%	10%	
Cyprus	20% (25%)	0% (25%)	25% on the excess amount on annual payments over £40,000.
Czech Republic	15%	15%	
Denmark	0%	0% (25%)	From 1 April, a withholding tax of 25% may apply in certain circumstances if interest paid to a foreign controlling entity (having 50% of voting power or share capital). However, the withholding tax only applies if the foreign resident company is a financial company situated in a tax haven (as defined) or (b) a jurisdiction that does not have a double taxation treaty with Denmark.
Estonia	26%	0% (21%)	There is no withholding tax on interest payments to non-residents on the condition that the interest charged does not significantly exceed the arm's length rate at the time the debt is incurred and the interest payments are made. 21% Estonian withholding tax will thus apply only to the part of the interest that significantly exceeds the arm's length amount.

Finland	0% (29%)	0% (28%)	Interest on bonds, debentures, deposits on bank accounts, foreign tax credits and other loans that are not similar to the borrower's own capital is exempt from tax if paid to a non-resident.
France	0% (15%)	0% (18%)	In practice, loan interest is exempted from French withholding tax provided specific formal conditions are fulfilled (e.g. loans with a contract).
Germany	0% (25%)	0% (25%)	Interest paid to non-residents on instruments other than convertible or profit-sharing bonds or mortgage loans is generally free of withholding tax.
Greece	37.5% (15%)	25% (10%)	Interest earned on deposits with banks operating in Greece, as well as on any kind of bonds and other interest-bearing securities issued by private enterprises, was subject to a tax withheld at the source of 15% in 2003 and 10% in 2009.
Hungary	Bilateral	30%	From 1 January 2010 30% withholding tax will be introduced on interests, royalties and certain service fee payments made to companies, which are resident in countries with which Hungary does not have a double tax treaty.
Ireland	20%	20%	
Italy	0%, 12.5%, 27%	0%, 12.5%, 27%	0% applies on loan agreements and ordinary notes; 12.5% on bonds if the term of the bond issue is more than 18 months; 27% if the above mentioned period is shorter.
Latvia	10% (5%)	10% (5%)	Interest payments to related non-resident parties are generally subject to a 10% WHT. If a bank registered in Latvia pays interest to related companies at the bank's normal interest rate level, then a 5% WHT applies.
Lithuania	0% (10%)	0% (10%)	Withholding tax is not applied on Government securities issued on international financial markets, interest accumulated and paid on deposits, and interest on subordinated loans which meet the criteria established by legal acts adopted by the Bank of Lithuania.

Luxembourg	0%	0% (15%)	Interest paid to non-residents is generally not subject to withholding tax in Luxembourg. However, interest that represents a right to profit participation on a bond may be assimilated as a dividend and subject to a withholding tax of 15%.
Malta	0%	0%	Interest and royalty income by non-residents is exempt from tax in Malta as long as certain conditions are complied with (e.g. they are not effectively connected to a permanent establishment of the recipient situated in Malta).
Netherlands	0%	0% (15%)	A nil withholding tax rate applies to payments to a resident corporation when its shareholding qualifies for the participation exemption and the shares form part of a company whose activities are carried out in the Netherlands. However, dividend withholding tax may be levied on certain profit participating loans (15%).
Poland	20%	20%	
Portugal	20%	20%	
Romania	10%	16% (0%)	Interest income obtained from Romania by EEA registered pension funds will be exempt from withholding taxes.
Slovak Republic	25%	0% (19%)	Interest paid to related EU-resident companies is generally not subject to withholding tax. Under certain conditions the tax rate is 19%. In 2002 it was 25%
Slovenia	25%	15%	
Spain	0% (18%)	0% (18%)	Spanish internal legislation provides withholding tax exemption on interest obtained by EU lenders not established in Spain. Under certain conditions the tax rate is 18%.
Sweden	0%	0%	
United Kingdom	20% (0%)	20% (0%)	Interest paid on debts not capable of exceeding one year (short interest) is not subject to withholding tax.

Note: The withholding taxes listed in the table refer to the rates applicable to non-treaty countries.

Source: IBFD (2005) and various tax tables provided by PriceWaterhouseCoopers.

Annex 2

Withholding taxes on royalties

Country	Tax rate 2003	Tax rate 2009	Notes
Austria	20%	20%	
Belgium	15%	15%	
Bulgaria	15%	10%	
Cyprus	10% (5%*)	0% (10%**)	*5% on film and TV royalties. **Where royalties are earned on rights used within Cyprus there is a 10 % withholding tax.
Czech Republic	25%	15%	
Denmark	30% (0%)	25% (0%)	Exemptions include payments for copyrights, e.g. software, manuscripts, music, movies and videos and payments for the use of industrial, commercial or scientific equipment.
Estonia	15%	10% (5%)	The lower 5% rate applies to royalties paid for the use of industrial, commercial or scientific equipment.
Finland	29%	28%	
France	33.3%	33.3%	
Germany	25%	15%	
Greece	20% (10%)	20%	Before 1.1. 2003 the withholding tax was 10% for film rentals of fixed amounts or film rentals based on a percent of

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			receipts.
Hungary	Bilateral	30%	From 1 January 2010 30% withholding tax will be introduced on interests, royalties and certain service fee payments made to companies, which are resident in countries with which Hungary does not have a double tax treaty.
Ireland	0% (20%)	0% (20%)	20% tax applies to patent royalties.
Italy	22.5% (30%)	22.5% (30%)	A 30% withholding tax must be applied to 75% of the gross income, making the effective rate 22.5% (30% x 75%). A 30% withholding tax, levied on the entire amount, applies to the payments for the use, or the right to use, industrial, commercial or scientific equipment if the property is physically situated in Italy.
Latvia	15% (5%)	5%	Rental income from property located in Latvia is subject to a 5% withholding tax in 2003.
Lithuania	10%	10%	
Luxembourg	10%	0%	
Malta	0%	0%	Interest and royalty income is exempt from tax when certain conditions are complied with (e.g. they are not effectively connected to a permanent establishment of the recipient situated in Malta).
Netherlands	0%	0%	A nil withholding tax rate applies to payments to a resident corporation when its shareholding qualifies for the participation exemption and the shares form part of a company whose activities are carried out in the Netherlands.

Poland	20%	20%	
Portugal	15%	15%	
Romania	15%	16%	
Slovak Republic	25% (1%)	19%	The lower rate applies to lease contracts under which the lessee has the right to purchase the leased asset at the end of the lease period, provide that the lease is of a certain minimum duration.
Slovenia	25%	15%	
Spain	25%	24%	
Sweden	0% (28%)	0% (28%)	Under domestic law there is no withholding tax on royalties. However, a non-resident recipient of royalties is deemed to have a permanent establishment in Sweden in respect of the royalties received. Thus, the recipient would be taxed in Sweden on the net royalty income, i.e. gross royalty less expenses related to the royalty, at the ordinary corporate income tax rate (28%).
United Kingdom	22%	20% (0%)	Under UK domestic law, withholding tax is deducted from royalties in respect of UK registered patents, copyright royalties (other than film royalties), design royalties, certain mineral royalties and royalties which are regarded as annual payments.

Note: The withholding taxes listed in the table refer to the rates applicable to non-treaty countries.

Source: IBFD (2005) and various tax tables provided by PriceWaterhouseCoopers.

Annex 3

Bilateral double taxation treaties on interest payments between EU Member States (2009)

Payed from/ Recipient	Austria	Belgium	Bulgaria	Cyprus	Czech Republic	Denmark	Estonia	Finland	France	Germany	Greece	Hungary	Ireland	Italy
Austria	x	0	0	0	0	0	0	0	0	0	0	0	0	0
Belgium	15	X	0/10	0/10	0/10	10	0/10	10	15	0/10	0/5/10	0/15	15	0/15
Bulgaria	0	10/0	x	7	10/0	0	n.a.	0	0	0	10	10/0	5/0	0
Cyprus	0	10	7	x	10	10	n.a.	n.a.	10	10	10	10	0	10
Czech Republic	0	10	0/10	0/10	x	0	0/10	0	0	0	0/10	0	0	0
Denmark	0	0	0	0	0	x	0	0	0	0	0	0	0	0
Estonia	0/21	0/21	0/21	0/21	0/21	0/21	x	0/21	0/21	0/21	0/21	0/21	0/21	0/21
Finland	0	0	0	0	0	0	0	X	0	0	0	0	0	0
France	0	0/15	0	0/10	0	0/18	0/10	0/10	x	0	0	0	0	0/10
Germany	0	0/25	0/25	0/10	0	0/25	0/25	0	0	x	0/10	0	0	0/25
Greece	10/0	5/10	10	10	10	8	10	10	10	10	x	10	5	10
Hungary	0	15	10	10	0	0	10	0	0	0	0	x	0	0
Ireland	0	0/15	0/5	0	0	0	0/10	0	0	0	0/5	0	x	10

Italy	0/10	0/15	0	0/10	0	0/10	0/10	0/15	0/10	0/10	0/10	0	0/10	x
Latvia	0/5/10	0/5/10	0/5	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10
Lithuania	0/5	0/5	0/5	0/5	0/5	0/5	0/5	0/5	0/5	0/5	0/5	0/5	0/5	0/5
Luxembourg	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]
Malta	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]
Netherlands	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Poland	20	10	10	10	10	5	10	0	0	5	10	10	10	10
Portugal	20	15	10	10	10	10	10	15	12/10	15/10	15	10	15	15
Romania	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10
Slovakia	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Slovenia	5	10	5	10	5	5	10	5	5	5	10	5	5	10
Spain	0/5	0/15	0	n.a.	0	0/10	0/10	0/10	0/10	0/10	0/8	0	0	0/12
Sweden	0	0	0	0	0	0	0	0	0	0	0	0	0	0
United Kingdom	0	15	0	10	0	0	10	0	0	0	0	0	0	10

Payed from/ Recipient	Latvia	Lithuania	Luxembourg	Malta	Netherlands	Poland	Portugal	Romania	Slovakia	Slovenia	Spain	Sweden	UK
Austria	0	0	0	0	0	0	0	0	0	0	0	0	0
Belgium	0/10	0/10	0/15	0/10	0/10	0/5	15	0/10	0/10	0/10	10	0/10	15
Bulgaria	5/0	10/0	10	0	0	10/0	10/0	15/0	10	5/0	0	0	0
Cyprus	n.a.	n.a.	n.a.	10	n.a.	10	n.a.	10	10	n.a.	n.a.	10	10
Czech Republic	0/10	0/10	0	0	0	0/10	0/10	0/7	0	0/5	0	0	0
Denmark	0	0	0	0	0	0	n.a.	0	0	n.a.	0	0	0
Estonia	0/21	0/21	0/21	0/21	0/21	0/21	0/21	0/21	0/21	0/21	0/21	0/21	0/21
Finland	0	0	0	0	0	0	0	0	0	0	0	0	0
France	0/10	0/10	0/10/12	0/10	0/10	0	0/12	0/10	0	n.a.	0/10	0	0
Germany	0/25	0/25	0	0/25	0	0/25	0/25	0/25	0	0/25	0/10	0/25	0
Greece	10	10	8	8	10/8	10	15	10	10	10	8	10	0
Hungary	10	10	0	10	0	10	10	15	0	5	0	0	0
Ireland	0/10	0/10	0	0	0	0/10	0/15	0/3	0	0/5	0	0	0
Italy	0/10	0/10	0/10	0/10	0/10	0/10	0/15	0/10	0	0/10	0/12	0/15	0/10

Latvia	x	0	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10	0/5/10
Lithuania	0/5	x	0/5	0/5	0/5	0/5	0/5	0/5	0/5	0/5	0/5	0/5	0/5
Luxembourg	0[1]	0[1]	x	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]
Malta	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]	0[1]
Netherlands	0	0	0	0	x	0	0	0	0	0	0	0	0
Poland	10	10	10	10	5	x	10	10	10	10	0	0	5
Portugal	10	10	15/10	10	10	10	x	10	10	10	15	10	10
Romania	0/10	0/10	0/10	0/10	0/10	0/10	0/10	x	0/10	0/10	0/10	0/10	0/10
Slovakia	0	0	0	0	0	0	0	0	x	0	0	0	0
Slovenia	10	10	5	5	5	10	10	5	10	x	5	0	5
Spain	0/10	0/10	0/10	0	0/10	0	0/15	0/10	0/5	0/5	x	0/15	0/12
Sweden	0	0	0	0	0	0	0	0	0	0	0	x	0
United Kingdom	10	10	0	10	0	5	10	10	0	5	12	0	X

Note: Individual notes are prevalent in most bilateral double taxation treaties.

Source: PriceWaterhouseCoopers (2009).

Annex 4

Bilateral double taxation treaties on royalty payments between EU Member States (2009)

Payed from/Recipient	Austria	Belgium	Bulgaria	Cyprus	Czech Republic	Denmark	Estonia	Finland	France	Germany	Greece	Hungary	Ireland	Italy
Austria	x	0/10	0	0	5	0	10/5	5	0	0	7	0	0/10	0/10
Belgium	10	x	5	0	5/10	0	5/10	5	0	0	5	0	0	5
Bulgaria	0	5	x	10	10	0	n.a.	0/5	5	5	10	10	10	5
Cyprus	0	0	0/10	x	0/5	0	n.a.	n.a.	0	0	0	0	0	0
Czech Republic	0/5	0/10	10	0/5	x	0/5	10	0/1/5/10	0/5	5	0/10	10	10	0/5
Denmark	10/0	0	0	0	0	x	10/5	0	0	0	5	0	0	5
Estonia	0/10	0/10	0/10	0/10	0/10	0/10	x	0/10	0/10	0/10	0/10	0/10	0/10	0/10
Finland	5	5	5	28	10	0	10	x	0	5	10	5	0	5
France	0	0	5/0	0	0/5/10	33,33/0	5/10/0	0	x	0	5/0	0	0	5/0
Germany	0	0	5	0/5	5	0	10	0/5	0	x	0	0	0	0/5
Greece	10/0	5	10	5/0	10	5	5/10	10	5	0	x	10	5	5
Hungary	0	0	10	0	10	0	5/10	5	0	0	10	x	0	0
Ireland	0	0	0/10	0	0/10	0	0/10	0	0	0	0/5	0	X	0

Italy	0/10	5	5	0	0/5	0/5	5/10	0/5	0/5	0/5	0/5	0	0	x
Latvia	5/10	5/10	0/5	5/10	5/10	5/10	5/10	5/10	5/10	5/10	5/10	5/10	5/10	5/10
Lithuania	10/0	10/0	10/0	10/0	10/0	10/0	10/0	10/0	10/0	10/0	10/0	10/0	10/0	10/0
Luxembourg	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Malta	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Netherlands	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Poland	20	10	5	5	5	5	10	0	10	5	10	10	10	10
Portugal	10/5	10	10	n.a.	10	10	10	10	5	10	10	10	10	12
Romania	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10
Slovakia	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Slovenia	5	5	5/10	10	10	5	10	5	5	5	10	5	5	10
Spain	5	5	0	n.a.	5	6	10	5	5	5	6	0	10	8
Sweden	0/10	0	5	0	0/5	0	5/10	0	0	0	0/5	0	0/5	0/5
United Kingdom*	0	0	0	0	10	0	10	0	0	0	0	0	0	8

Payed from/Recipient	Latvia	Lithuania	Luxembourg	Malta	Netherlands	Poland	Portugal	Romania	Slovakia	Slovenia	Spain	Sweden	UK
Austria	10/5	10/5	0/10	0/10	0/10	5	5/10	3	5	5	5	0/10	0/10
Belgium	5/10	5/10	0	0/10	0	5	10	5	5	5	5	0	0
Bulgaria	7/5	10	5	10	0/5	5	10	15	10	5/10	0	5	0
Cyprus	n.a.	n.a.	n.a.	0/10	n.a.	5	n.a.	0/5	0/5	n.a.	n.a.	0	0
Czech Republic	10	10	0/10	5	5	5	10	10	0/10	10	0/5	0/5	0/10
Denmark	5/10	5/10	0	0	0	5	n.a.	10	5	n.a.	6	0	0
Estonia	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10	0/10
Finland	10	10	5	0	0	10	10	5	10	5	5	0	0
France	5/10/0	5/10/0	0	10/0	0	10/0	5/0	10/0	5/0	n.a.	5/0	0	0
Germany	10	10	5	0	0	5	10	3	5	5	5	0	0
Greece	5/10	5/10	5/7	8	5/7	10	10	5/7	10	10	6	5	0
Hungary	5/10	5/10	0	10	0	10	10	10	10	5	0	0	0
Ireland	0/10	0/10	0	0/5	0	0/10	0/10	0/3	0/10	0/5	0/10	0	0
Italy	5/10	5/10	10	0/10	5	10	12	10	0/5	10	4/8	5	8
Latvia	x	0	5/10	5/10	5/10	5/10	5/10	5/10	5/10	5/10	5/10	5/10	5/10

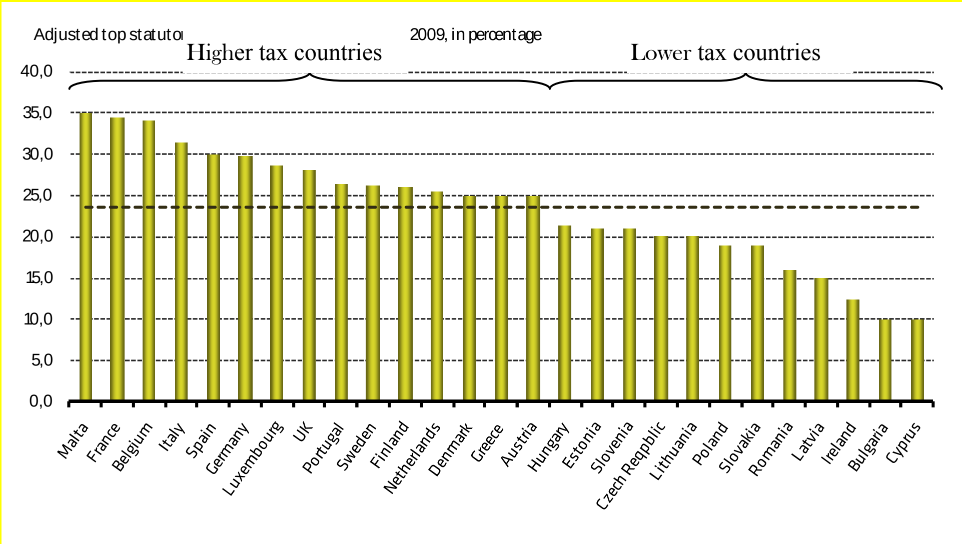
Lithuania	10/0	x	10/0	10/0	10/0	10/0	10/0	10/0	10/0	10/0	10/0	10/0	10/0
Luxembourg	0	0	x	0	0	0	0	0	0	0	0	0	0
Malta	0	0	0	x	0	0	0	0	0	0	0	0	0
Netherlands	0	0	0	0	x	0	0	0	0	0	0	0	0
Poland	10	10	10	10	5	x	10	10	5	10	10	5	5
Portugal	10	10	10	10	10	10	x	10	10	5	5	10	5
Romania	0/10	0/10	0/10	0/10	0/10	0/10	0/10	x	0/10	0/10	0/10	0/10	0/10
Slovakia	0	0	0	0	0	0	0	0	0	0	0	0	0
Slovenia	10	10	5	5	5	10	5	5	10	x	5	0	5
Spain	10	10	10	0	6	10	5	10	5	5	x	10	10
Sweden	5/10	5/10	0	0	0	0/5	0/10	0/10	0/5	n.a.	0/10	X	0
United Kingdom*	10	10	5	10	0	5	5	15	10	5	10	0	x

Note: Individual notes are prevalent in most bilateral double taxation treaties.

Source: PriceWaterhouseCoopers (2009).

Annex 5

Statutory corporate tax rates in EU countries



Annex 6

Duration of the tax refund procedure

Duration of tax relief	Countries
Less than 6 months	Austria (6 months), Ireland (6 months) and Norway (3-6 months)
Between 6 and 9 months	Denmark (6-9 months), Finland (6-9 months), Sweden (6-9 months) and Switzerland (6-8 months)
Between 9 and 24 months	Belgium (18 months), France (8-14 months), Portugal (12-24 months) and Spain (12-24 months)
More than 24 months	Italy (60-84 months)

Note: The numbers show the average run time from point of dispatching to custodian/foreign tax office. The table lists information for 12 EU host countries and no data is available for the remaining EU countries.

Source: *Simplified Withholding Tax Relief Procedures*, DG Internal Market and Services, European Commission, Brussels 2010.

Annex 7

Sectors with large intangible fixed assets, 2008 data

	Mean intangible fixed assets as a share of operating revenue	Share of intangible fixed assets	Share of value added
Patent-intensive sectors	6.0	56.4	41.3
Chemicals and chemical products	28.6	6.4	3.3
Machinery and equipment n.e.c.	0.1	1.5	3.6
Electrical and optical equipment	0.5	2.1	2.1
Manufacture of other transport equipment	2.7	1.5	1.0
Wholesale trade and retail trade	0.1	5.9	17.5
Research and development	8.9	0.7	n.a
Other business activities	1.2	38.2	13.8
Other royalty-intensive sectors	0.4	29.1	16.7
Total credit institutions	1.0	4.9	n.a.
Recreational, cultural and sporting activities	0.8	1.9	n.a.
Food products and beverages	0.6	3.5	3.4

Post and telecommunications	0.5	13.7	4.3
Computer and related activities	0.2	1.9	3.4
Rubber and plastic products	0.1	0.6	1.4
Motor vehicles, trailers and semi-trailers	0.0	1.8	2.7
Other non-metallic mineral products	0.0	0.8	1.5

Note: We exclude the resource-intensive sectors such as mining and oil extraction since such exploitation rights enter as intangible fixed assets in the companies' balance sheet information but do not all under the Directive. The definition of patent intensive industries follows Norden (2009).

Source: Own calculations based on Amadeus data.

Annex 8

The impact of lowering the holding requirements from 10% to 0%

	Share of holding links lying in the 0-10% ownership interval		
	Total	Weighted by intangible fixed assets of parent	Weighted by financial revenue of parent
Holding links	7%	.	.
Subsidiary employment	27%	12%	25%
Subsidiary turnover	24%	10%	12%

Note: The calculations are for 2008 and show the proportion of the holding links where the ownership share lies between 0 percent and 10 percent.

Source: Copenhagen Economics, *Taxation of interest and royalties – impact assessment of amendments to the present Directive,* October 2010.

Annex 9

Impacts on tax base of reducing withholding taxes on interests and royalties

No impact on tax revenues in host country		Reduced tax revenues in host countries	
Interest	Royalties	Interest	Royalties
Austria*	Luxembourg	Belgium	Austria
Cyprus*	Malta*	Bulgaria	Belgium
Denmark*	Netherlands*	Czech Republic	Bulgaria
Estonia*	Sweden	Greece	Cyprus
Finland	Slovak Republic*	Hungary	Czech Republic
France*		Ireland	Denmark
Germany*		Italy	Estonia
Lithuania*		Latvia	Finland
Luxembourg*		Poland	France
Malta		Portugal	Germany
Netherlands*		Romania	Greece
Slovak Republic*		Slovenia	Hungary
Spain*		United Kingdom	Ireland

Sweden	Italy Latvia Lithuania Poland Portugal Romania Slovenia Spain United Kingdom

Note: * Indicates that there is generally no withholding tax on cross-border payments to other EU Member States but that there might be few exemptions.

Annex 10

Indicators of interest payments for different groups of countries

	Group 1 Italy and United Kingdom	Group 2 Portugal, Poland, Greece, Hungary and Ireland	Group 3 Romania, Latvia, Slovenia, Bulgaria, Czech Rep.	Group 4 Belgium	Total
Outgoing interest payments (billion €)	79.4	13.0	3.1	16.0	111.5
Outgoing inter-company interest payments (billion €)	7.9	1.3	0.3	1.6	11.2
Outgoing inter-company interest payments as share of GDP	0.23%	0.12%	0.08%	0.46%	0.22%
Loss of gross income from withholding tax on inter-company payments(billion €)	0.5	0.1	0.0	0.2	0.8
Net balance (billions €)	6.8	0.8	0.1	-0.1	0.8
Net balance as share of GDP	0.20%	0.08%	0.03%	-0.02%	0.01%
Net revenue effects after netting for:					
Gains from reduced tax credits	0.5*	0.05*	0.0*	-0.2*	0.35*

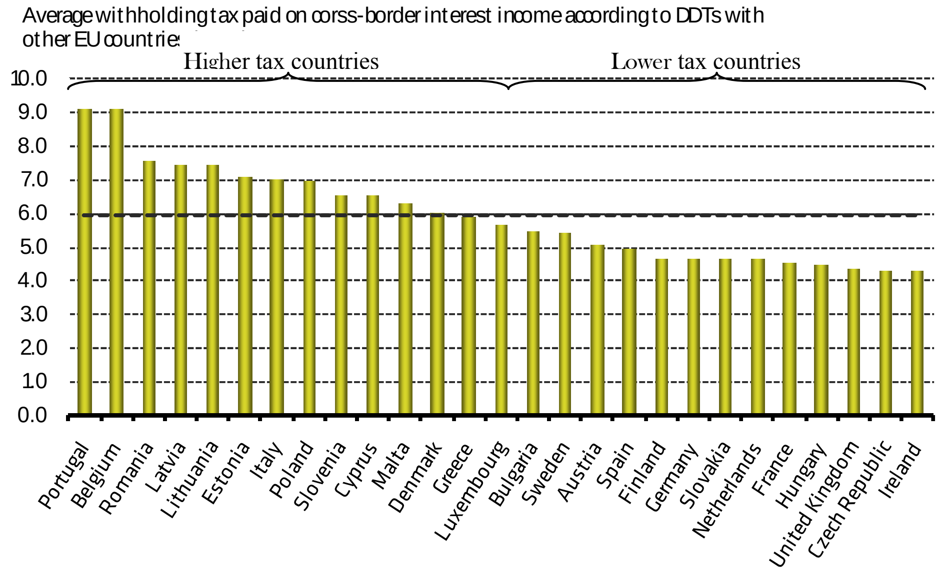
Effectives from existing Directive	0.3	0.03	0.0	-0.1	0.23

Note: All the data is from 2008 except data from Poland, Greece, Slovenia, Bulgaria with are from 2007 and Romania with are from 2006. Group 1 includes countries with net interest payments above €10.000 billion; Group 2 includes countries with net interest payments between €1000 and €10.000; Group 3 includes countries with positive net interest payments below €1000; and group 4 includes countries with negative net interest payments. The four groups represent 23 percent of the total interest paid. * These numbers should be interpreted with caution since average unweighted withholding taxes have been used in the calculations.

Source: Eurostat, *International Transactions in Interest and Dividend Payments*.

Annex 11

Average withholding taxes on interest payments to other EU countries



Note: The withholding tax in the individual home country is calculated as the unweighted average of the withholding tax paid in other EU (host) countries.

Source: PriceWaterhouseCoopers.

Annex 12

Indicators of royalty payments for different groups of countries

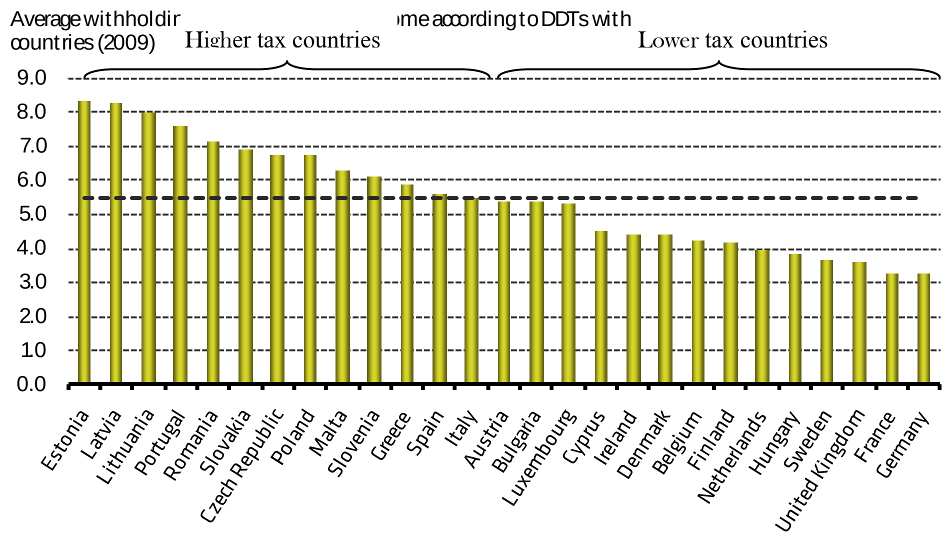
	Group 1 Denmark, France and the United Kingdom	Group 2 Austria, Belgium, Finland, Hungary, Italy and Spain	Group 3 Greece, Portugal and Romania	Group 4 Bulgaria, Czech Rep., Poland and Slovenia	Total
Outgoing royalty payments (billion €)	11,5	8,8	1	2	23.3
Outgoing royalty payments as share of GDP	0.29%	0.25%	0.18%	0.34%	0.27%
Loss of gross income from withholding tax (billion €)	0.5	0.5	0.1	0.2	1.3
Net balance (billions €)	6.6	-4.8	-0.9	-1.7	-0.8
Net balance as share of GDP	0.16%	-0.13%	-0.17%	-0.29%	-0.01%
Net revenue effects after netting from gains from reduced tax credits	0.2	-0.2	-0.1	-0.2	-0.3
Effectives from existing directive	0.1	-0.1	-0.05	-0.1	-0.15

Note: Cyprus, Estonia, Germany, Latvia, Ireland and Lithuania have been excluded due to lack of data. Group 1 consists of countries with a positive net balance; Group 2 consists of countries with a negative net balance of less than 0.25% of GDP and outgoing royalty payments greater than 0.4 billion; Group 3 consists of countries with negative net balance less than 0.25% of GDP and outgoing royalty payment less than 0.4 billion; and Group 4 consists of countries with net balance negative and greater than 0.25% of GDP. The four groups represent 49% of total EU royalty payments.

Source: Eurostat, International Transactions in Royalties and Licence Fees.

Annex 13

Average withholding taxes on royalty payments to other EU countries



Note: The withholding tax in the individual home country is calculated as the (unweighted) average of the withholding tax paid in other EU (host) countries.

Source: PriceWaterhouseCoopers.

Annex 14

Legal entities covered by the two directives

Country	Legal entities covered by the Interest and Royalty Directive as listed	Legal entities covered by the Parent-Subsidiary Directive as listed	Legal entities covered by the Interest and Royalty Directive as listed in Amadeus	Legal entities covered by the Parent-Subsidiary Directive as listed in Amadeus	Is the list of entities covered by the Parent-Subsidiary Directive less restrictive than the Interest and Royalty Directive?
Austria	Aktiengesellschaft (AG), Gesellschaft mit beschränkter Haftung (GmbH)	Aktiengesellschaft (AG), Gesellschaft mit beschränkter Haftung (GmbH), Versicherungsvereine auf Gegenseitigkeit, Erwerbs- und Wirtschaftsgenossenschaften, Betriebe gewerblicher Art von Körperschaften des öffentlichen Rechts, Sparkassen and other companies constituted under Austrian law subject to Austrian corporate tax	AG GmbH GmbH & Co KG	All companies in Amadeus	Yes

Belgium	Société anonyme (SA), Société en commandite par actions (SCA), Société privée à responsabilité limitée (SPRL) and Public law bodies that operate under private law	Société anonyme (SA), Société en commandite par actions (SCA), Société privée à responsabilité limitée (SPRL), Société coopérative à responsabilité limitée (SCRL), Société coopérative à responsabilité illimitée (SCRI), Société en nom collectif (SNC), Société en commandite simple (SCS). public undertakings which have adopted one of the above mentioned legal forms and other companies constituted under Belgian law subject to Belgian corporate tax	Private company limited by shares Private company with limited liability Company limited by shares Public company limited by shares	All companies in Amadeus	Yes

Bulgaria	Акционерно дружество (p.l.c), Командитно дружество с акции (ltd.) and Дружество с ограничена отговорност (ltd.)	Акционерно дружество (p.l.c), Командитно дружество с акции (ltd.) and Дружество с ограничена отговорност (ltd.)	Public limited company One-person public limited company One-person private limited company Private limited company	Public limited company One-person public limited company One-person private limited company Private limited company	No
Czech Republic	Akciová společnost (p.l.c), Společnost s ručením omezeným (ltd.), Veřejná obchodní společnost (general partnership), Komanditní společnost Družstvo	Akciová společnost (p.l.c), Společnost s ručením omezeným (ltd)	Joint stock company Limited liability company	Joint stock company Limited liability company	Yes/No
Cyprus	Companies in accordance with the Company's Law, Public Corporate Bodies as well as any other Body which is considered as a company in accordance with the Income tax Laws	εταιρείες" as defined in the Income Tax laws	Limited company Public limited company	Limited company Public limited company	No

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Denmark	Aktieselskab (ltd.) and Anpartsselskab (p.l.c)	Aktieselskab (ltd.), Anpartsselskab (p.l.c) and other companies subject to tax under the Corporation Tax Act, insofar as their taxable income is calculated and taxed in accordance with the general tax legislation rules applicable to "aktieselskaber"	Limited company Company with limited liability Limited company (Faroe Islands) Private limited company Private limited company (Faroe Islands)	Limited company Company with limited liability Limited company (Faroe Islands) Private limited company Private limited company (Faroe Islands) Cooperative with limited liability General partnership Limited partnership by shares Limited partnership Profit foundation	Yes

Estonia	Täisühing (general partnership), Usaldusühing (limited partnership), Osaühing (Ltd.), Aktsiaselts (p.l.c.), Tulundusühistu limited liability cooperative)	Täisühing (general partnership), Usaldusühing (limited partnership), Osaühing (Ltd.), Aktsiaselts (p.l.c.), Tulundusühistu limited liability cooperative)	Limited liability company Share company Profit oriented cooperatives	Limited liability company Share company Profit oriented cooperatives	No
Finland	Osakeyhtiö (ltd.), Osuuskunta (cooperative), Säästöpankki) and Vakuutusyhtiö (försäkringsbolag)	Osakeyhtiö (ltd.), Osuuskunta (cooperative), Säästöpankki) and Vakuutusyhtiö (försäkringsbolag)	Private limited company Public limited company Association/cooperatives	Private limited company Public limited company	No

France	Société anonyme (SA), Société en commandite par actions (SCA), Société à responsabilité limitée (SARL) and industrial and commercial public establishments and undertakings	Société anonyme (SA), Société en commandite par actions (SCA), Société à responsabilité limitée (SARL), Sociétés par actions simplifiées (SAS), Sociétés d'assurances mutuelles, Caisses d'épargne et de prévoyance and Sociétés civiles which are automatically subject to corporation tax, Coopératives , Unions de coopératives, industrial and commercial public establishments and undertakings, and other companies constituted under French law subject to French corporate tax	SA SA Directoire SARL SCA	All companies in Amadeus	Yes

Germany	Aktiengesellschaft (AG.), Kommanditgesellschaft auf Aktien (KGaA), Gesellschaft mit beschränkter Haftung (GmbH) and bergrechtliche Gewerkschaft	Aktiengesellschaft (AG), Kommanditgesellschaft auf Aktien (KGaA), Gesellschaft mit beschränkter Haftung (GmbH), Versicherungsverein auf Gegenseitigkeit, Erwerbs- und Wirtschaftsgenossenschaft, Betriebe gewerblicher Art von juristischen Personen des öffentlichen Rechts, and other companies constituted under German law subject to German corporate tax	AG KG GmbH GmbH & Co KG	All companies in Amadeus	Yes
Greece	ανώνυμη εταιρ (SA)	ανώνυμη εταιρεία (SA), εταιρεία περιωρισμένης ευθύνης (ltd.) and other companies constituted under Greek law subject to Greek corporate tax	SA	All companies in Amadeus	Yes/No

Hungary	Közkereseti társaság (community interest ltd.), Betéti társaság (partnership), Közös vállalat (joint venture), Korlátolt felelősségű társaság (ltd.), Részvénytársaság (limited company with shares), Egyesülés, Közhasznú társaság (general partnership) and Szövetkezet	Közkereseti társaság (community interest ltd.), Betéti társaság (partnership), Közös vállalat (joint venture), Korlátolt felelősségű társaság (ltd.), Részvénytársaság (limited company with shares), Egyesülés and Szövetkezet	Company limited by shares Cooperative company Limited liability company Limited partnership	Company limited by shares Cooperative company Limited liability company Limited partnership	Yes /No
Ireland	Public companies limited by shares or by guarantee (Public), private companies limited by shares or by guarantee (Private), bodies registered under the Industrial and Provident Societies Acts or building societies registered under the Building Societies Acts	Companies incorporated or existing under Irish law, bodies registered under the Industrial and Provident Societies Act, building societies incorporated under the Building Societies Acts and trustee savings banks within the meaning of the Trustee Savings Banks Act, 1989	Private Public, A.I.M. Public, quoted Public, not quoted	Private Public, A.I.M. Public, quoted Public, not quoted	Yes/No

Italy	Società per azioni (SPA), società in accomandita per azioni (SAPA), società a responsabilità limitata (SRL) and public and private entities carrying on industrial and commercial activities	Società per azioni (SPA), Società in accomandita per azioni (SAPA), Società a responsibilità limitata (SRL), Società cooperative, Società di mutua assicurazione, and private and public entities whose activity is wholly or principally commercial	Joint stock company - SPA Limited liability company - SRL Limited liability consortium Limited partnership with shares - SAPA One-person company with limited liability One-person joint stock company - SPA	All companies in Amadeus	Yes
Latvia	Akciju sabiedrība (AS), Sabiedrība ar ierobežotu atbildību (SIA)	Akciju sabiedrība (AS), Sabiedrība ar ierobežotu atbildību (SIA)	Joint stock company - AS Limited liability company - SIA	Joint stock company - AS Limited liability company - SIA	No
Lithuania	Companies incorporated under the law of Lithuania	Companies incorporated under the law of Lithuania	All companies in Amadeus	All companies in Amadeus	No

Luxembourg	Société anonyme (p.l.c), Société en commandite par actions (Limited partnership with shares) and société à responsabilité limitée (Ltd)	Société anonyme (p.l.c), Société en commandite par actions (Limited partnership with shares), Société à responsabilité limitée (Ltd), Société coopérative, Société coopérative organisée comme une société anonyme, Association d'assurances mutuelles, Association d'épargne-pension, Entreprise de nature commerciale, Industrielle ou minière de l'Etat, Des communes, des syndicats de communes, Des établissements publics et des autres personnes morales de droit public, and other companies constituted under Luxembourg law subject to Luxembourg corporate tax	Company limited by shares Limited partnership Private company with limited liability	All companies in Amadeus	Yes
Malta	Kumpaniji ta' Responsabilita' Limitata, Soċjetajiet in akkomandita li l-kapital tagħhom maqsum f'azzjonijiet	Kumpaniji ta' Responsabilita' Limitata, Soċjetajiet en commandite li l-kapital tagħhom maqsum f'azzjonijiet	International Trading Co. – Private non-Exempt Limited Liability Co. - Public Non-Exempt	International Trading Co. – Private non-Exempt Limited Liability Co. - Public Non-Exempt	No

Netherlands	Naamloze vennootschap (NV) and Besloten vennootschap met beperkte aansprakelijkheid (BV)	Naamloze vennnootschap (NV), Besloten vennootschap met beperkte aansprakelijkheid (BV), Open commanditaire vennootschap (CV), Coöperatie (C)), Onderlinge waarborgmaatschappij (Mutual insurance company), Fonds voor gemene rekening, Vereniging op coöperatieve grondslag, Vereniging welke op onderlinge grondslag als verzekeraar of kredietinstelling optreedt, and other companies constituted under Dutch law subject to Dutch corporate tax	Private limited liability company (BV) Public limited liability company (NV)	All companies in Amadeus	Yes
Poland	Spółka akcyjna (SA), Spółka z ograniczoną odpowiedzialnością (Sp. z.o.o)	Spółka akcyjna (SA), Spółka z ograniczoną odpowiedzialnością (Sp. z.o.o)	Joint stock company - SA Limited liability company - Sp. z.o.o.	Joint stock company - SA Limited liability company - Sp. z.o.o.	No

Portugal	Commercial companies or civil law companies having a commercial form, cooperatives and public undertakings incorporated in accordance with Portuguese law	Commercial companies or civil law companies having a commercial form and cooperatives and public undertakings incorporated in accordance with Portuguese law	All companies in Amadeus	All companies in Amadeus	No
Romania	Societăţi în nume colectiv (SNC), Societăţi în comandită simplă (SCS), Societăţi pe acţiuni (SA), Societăţi în comandită pe acţiuni (SCA) and Societăţi cu răspundere limitată (SRL)	Societăţi în nume colectiv (SNC), Societăţi în comandită simplă (SCS), Societăţi pe acţiuni (SA), Societăţi în comandită pe acţiuni (SCA) and Societăţi cu răspundere limitată (SRL)			
Slovak Republic	Aakciová spoločnos (Limited liability company), Spoločnosť s ručením obmedzeným (Limited company), Komanditná spoločnos (Limited liability partnership), Verejná obchodná spoločnos (general partnership or unlimited partnership), Družstvo (Cooperative)	Akciová spoločnosť (Limited liability company), Spoločnosť s ručením obmedzeným (Limited company), Komanditná spoločnosť (Limited liability partnership)	Cooperative Joint stock company Limited liability company	Joint stock company Limited liability company	Yes

Slovenia	Delniška družba (p.l.c.), Komanditna delniška družba, Komanditna družba, Družba z omejeno odgovornostjo (Ltd.), Družba z neomejeno odgovornostjo	Delniška družba (p.l.c.), Komanditna družba, Družba z omejeno odgovornostjo (Ltd.)	Cooperative with limited liability Joint-stock company Limited liability company	Cooperative with limited liability Joint-stock company Limited liability company	Yes/No
Spain	Sociedad anónima (SA), Sociedad comanditaria por acciones (SCA), Sociedad de responsabilidad limitada (SPRL) and those public law bodies which operate under private law	Sociedad anónima (SA), Sociedad comanditaria por acciones (SCA), Sociedad de responsabilidad limitada (SPRL) and public law bodies which operate under private law. Other entities constituted under Spanish law subject to Spanish corporate tax ("Impuesto sobre Sociedades")	Sociedad anonima (SA) Sociedad limitada	All companies in Amadeus	Yes
Sweden	Aktiebolag (Ltd.) and Försäkringsaktiebolag	Aktiebolag (Ltd.), Försäkringsaktiebolag, Ekonomiska föreningar (economic association), Sparbanker and Ömsesidiga försäkringsbolag	Private limited company Public limited company	Private limited company Public limited company	Yes/No

United Kingdom	Companies incorporated under the law of the United Kingdom	Companies incorporated under the law of the United Kingdom	All companies in Amadeus	All companies in Amadeus	No

Note: Yes/No means that the two lists are different but that we are not able to detect the differences in the legal forms used in Amadeus.

Source: Council Directive 2003/49/EC and Council Directive 2003/123/EC.

Annex 15

The coverage of legal forms in the Directive

	Share of holding links with a legal form is covered by the present Directive in 2008		
	Total	Weighted by intangible fixed assets of parent	Weighted by financial revenue of parent
Holding links	82%		
Subsidiary employment	82%	95%	90%
Subsidiary turnover	85%	95%	90%

Note: The calculations are for 2008 and include all cases where both the parent and the subsidiary entity have a legal form that is already covered by the Interest and Royalty Directive. The sample includes only the entities for which we have information on employment and turnover.

Source: Copenhagen Economics *Taxation of interest and royalties – impact assessment of amendments to the present Directive,* October 2010.

Annex 16

The coverage of legal forms in the amended Directive

	Share of holding links with a legal form is covered by the amended Directive (legal form as in the parent-Subsidiary Directive)		
	Total	Weighted by intangible fixed assets of parent	Weighted by financial revenue of parent
Holding links	84%	.	.
Subsidiary employment	83%	97%	92%
Subsidiary turnover	87%	96%	91%

Note: The calculations are for 2008 and include all cases where both the parent and the subsidiary entity have a legal form that is already covered by the Interest and Royalty Directive. The sample includes only the entities for which we have information on employment and turnover.

Source: Copenhagen Economics. *Taxation of interest and royalties – impact assessment of amendments to the present Directive,* October 2010.

Annex 17

Transposition of criteria applicable to “associated companies”

Country	Application to more types of entities	Association threshold	Indirect holdings	Notes
Austria	No1	25%	No	1 Austrian law limits the benefits of the Directive to entities listed in the Directive with respect to the recipients of income; with respect to the payer of income the list of the types of benefiting entities is broader than that in the Annex.
Belgium	Yes	25%	Yes	
Cyprus	No	25%	No	
Czech Republic	Yes2	25%	No	2 Czech law limits the benefits of the Directive to entities listed in the Directive with respect to the recipients of income; no limitation applies as to the payer of income resident in the Czech Republic. Czech entities subject to tax at the level of its members are listed in the Annex to the Directive.
Denmark	No	25%	No	
Estonia	Yes	25%	No	
Finland	No	25%	No	
France	No	25%	No	
Germany	No	25%	No	
Hungary	-	-	-	
Ireland	No	25%	No	
Italy	No	25%	No	
Luxembourg	-	-	-	
Malta	-	-	-	
Netherlands	Yes3	-	-	3 The Netherlands limits the benefits of the Directive to entities listed in the Directive with respect to the recipients of income; the payer of income resident in the Netherlands may be an NV (public limited liability company), a

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				BV (private limited liability company), a mutual fund or a cooperative.
Slovak Republic4	Yes	25%	No	4 The Slovak law requires the recipient company to be a legal entity, which is a taxpayer in another EU Member State; no limitation applies as to the payer of income resident in the Slovak Republic. Slovak entities subject to tax at the level of its members are listed in the Annex to the Directive.
Slovenia	No	25%	No	
Spain	Yes5	No/25%6	Yes/ No6	5 No restrictions on the type of entity for interest payments; for royalties, only entities listed in the Annex to the Directive. 6 Exemption from tax on interest payments applies to interest paid to companies resident in EU Member States irrespective of affiliation.
Sweden	No	25%	No	
United Kingdom	No	25%	No	

Source: IBFD (2005) and PriceWaterhouseCoopers (2009).

Annex 18

The impact of lowering the holding requirements from 25% to 10%

	Share of holding links lying in the 10-25% ownership interval		
	Total	Weighted by intangible fixed assets of parent	Weighted by financial revenue of parent
Holding links	5%	.	.
Subsidiary employment	5%	6%	7%
Subsidiary turnover	4%	3%	3%

Note: The calculations are for 2008 and show the proportion of the holding links where the ownership share lies between 10 percent and 25 percent.

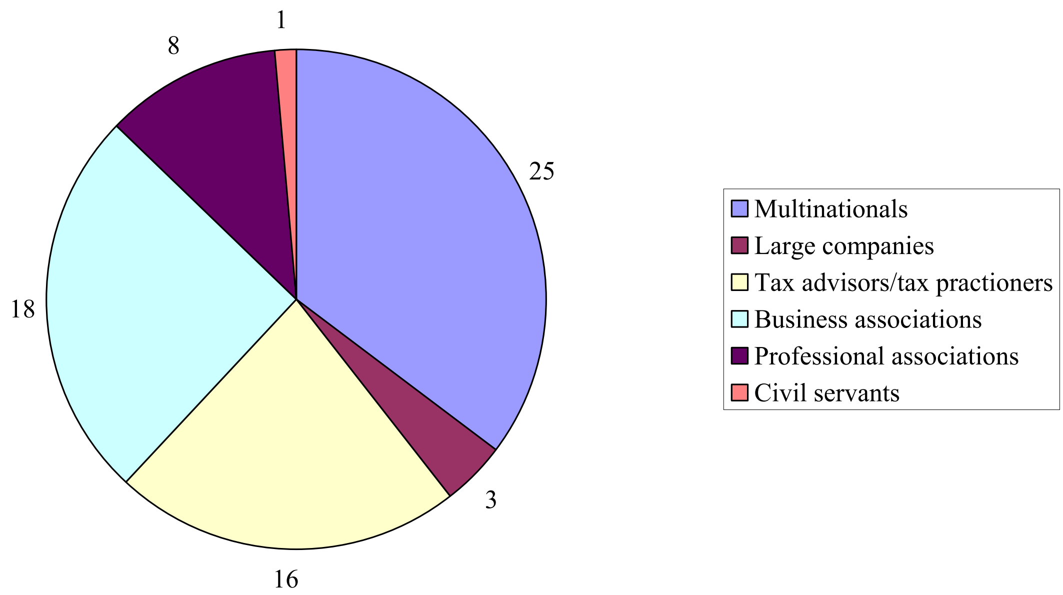
Source: Copenhagen Economics *Taxation of interest and royalties – impact assessment of amendments to the present Directive,* October 2010.

Annex 19

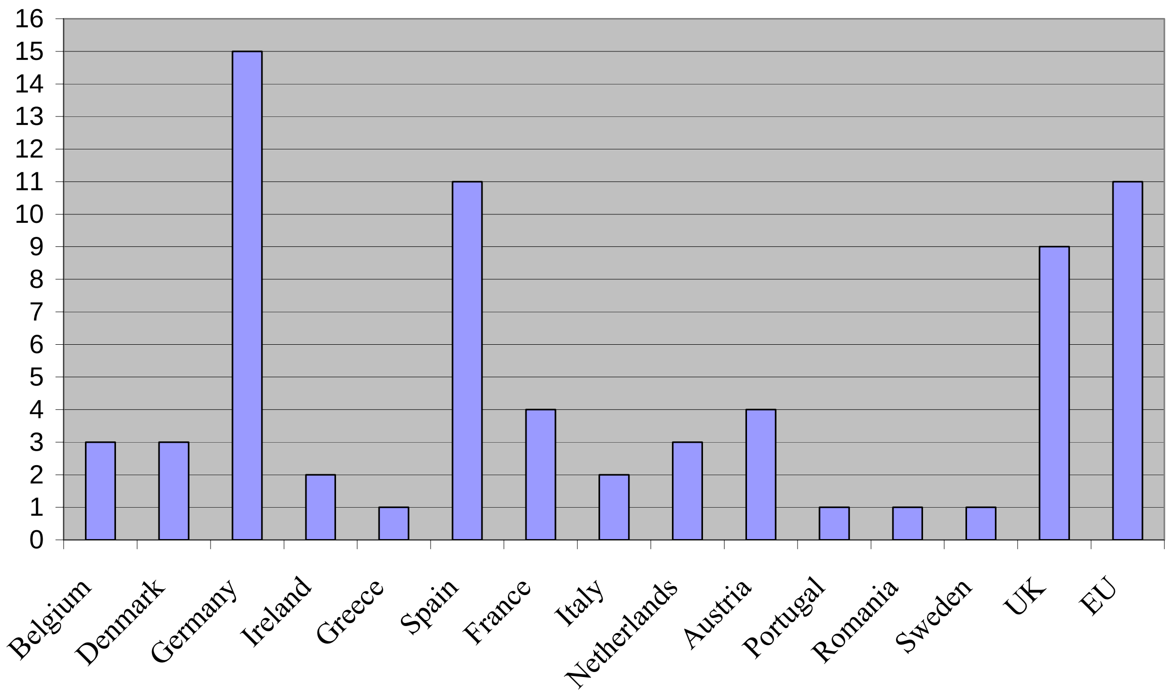
Briefing on the Public consultation on the taxation of cross-border interest and royalty payments between associated companies

On August 24, TAXUD launched a public consultation on the possible amendments to the Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States (hereinafter "the Directive"), which has been closed on 31 October. The questions referred to the policy options currently under analyses by TAXUD Directorate D. The main purpose of the amendments would be the extension of the Directive coverage, which is currently limited to payments between associated companies (25% shareholding); in addition, companies must have a legal forma as listed in the Directive annex. The results of the replies received can be summarised as follows.

71 contributors have sent their responses. They can be grouped in the following categories:

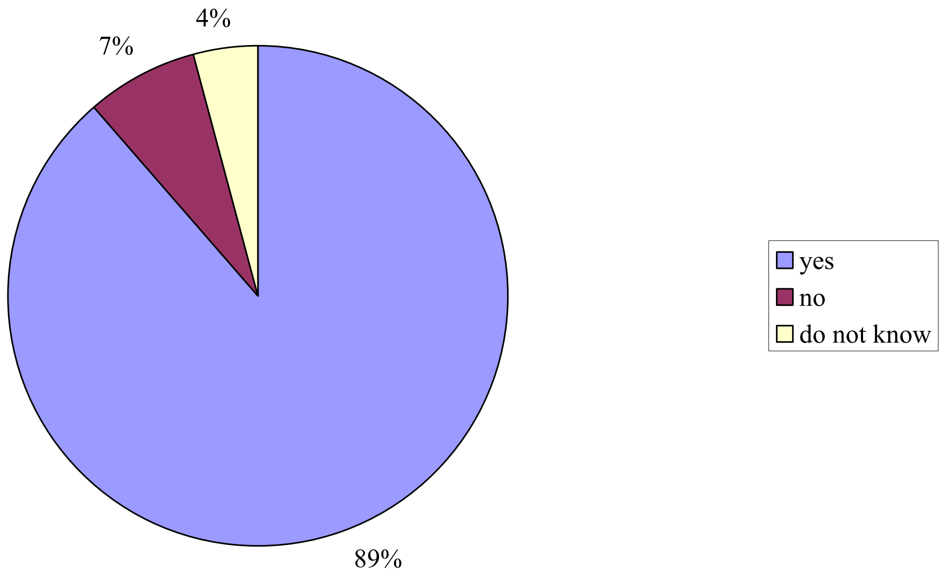


The contributors can be grouped according to their place of establishment:

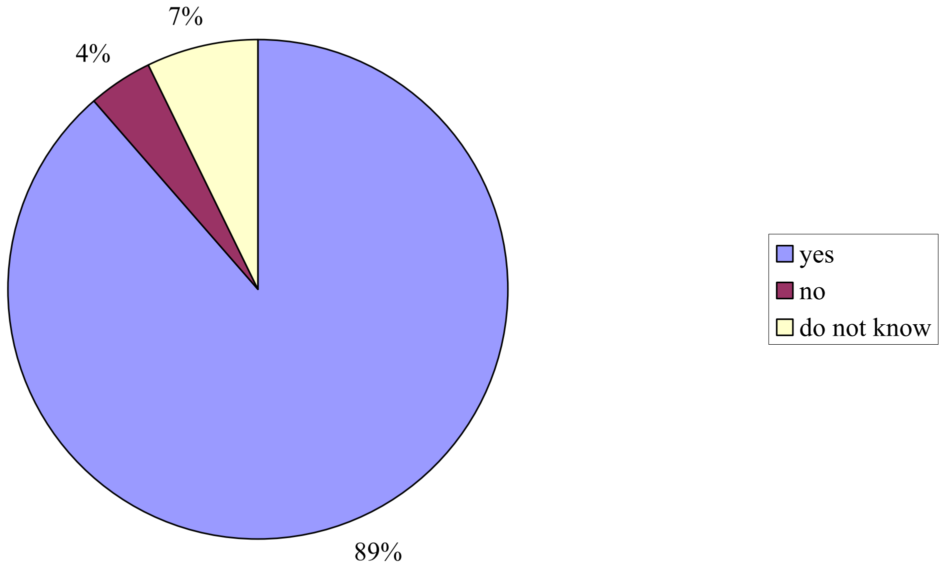


There are replies from 14 Member States. They correspond to the EU-15 (until 2004) with the exception of Finland and Luxembourg, while one response was received from Romania. We should bring the attention to the difference level of participation. It could be expected a larger share of French and Italian stakeholders. On the other hand, it is important to mention that there are 11 replies from organizations with an European dimension (6 business organizations, 3 professional associations and 2 tax advisors – law firms).

The questionnaire asked if there is a need to update the list of companies covered by the Directive. A large majority consider that the list should be updated. Only 7% of the answers do not consider necessary to update the scope of entities covered by the Directive. The responses can be seen in the following figure:

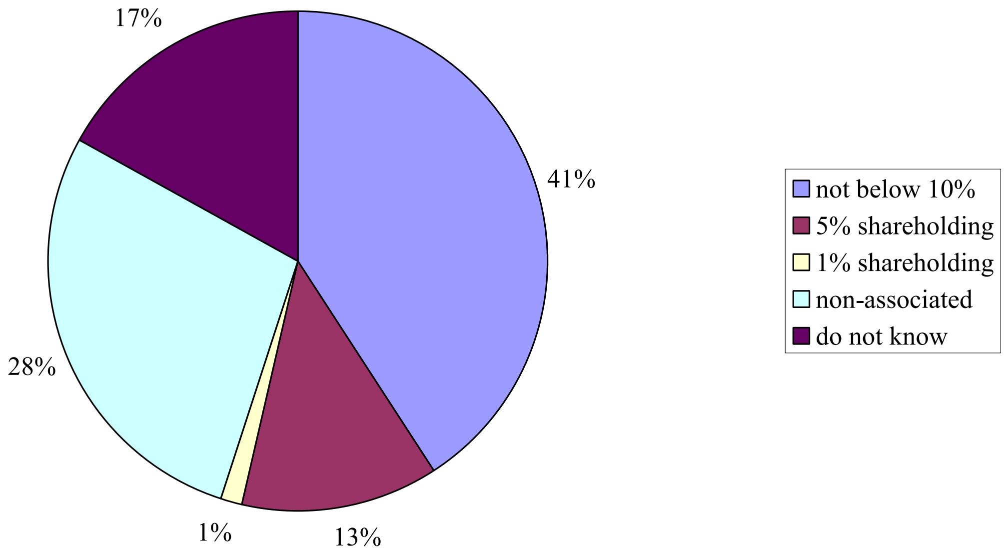


In addition, it was required if there is a need to change the minimum shareholding requirements. The results are the same as in the previous question.

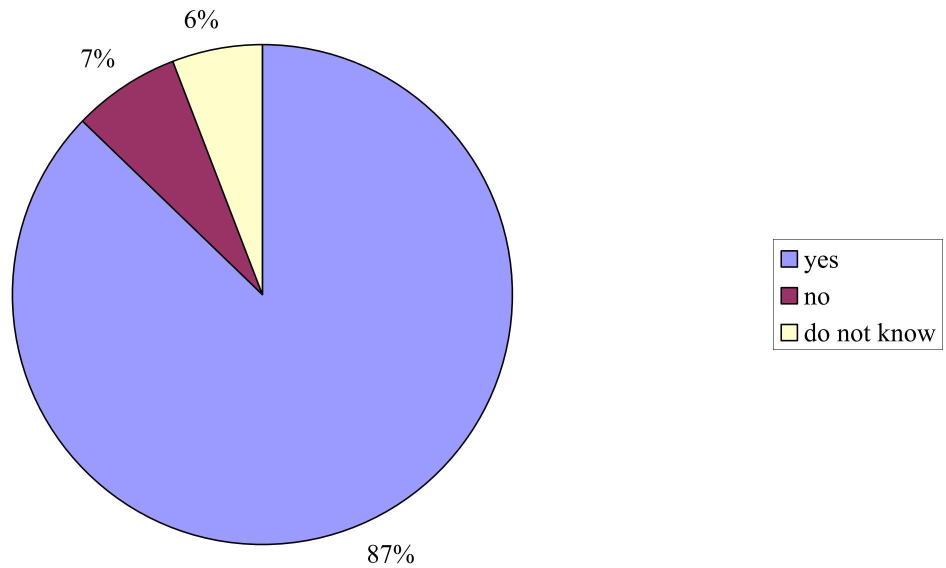


In the responses to the other policy options we can confirm that a large majority of contributors are of the opinion that the Directive needs an update.

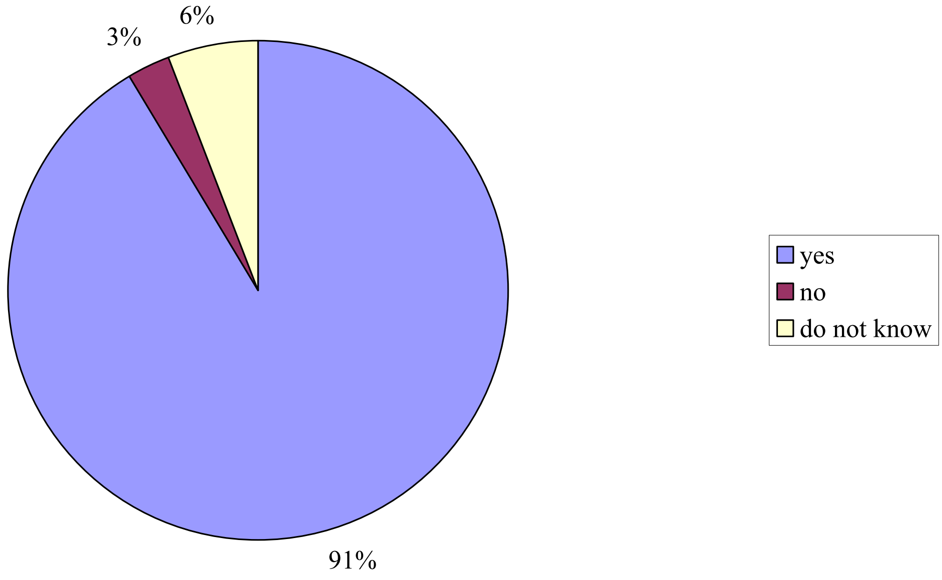
The questionnaire asked if the shareholding requirements of the Directive should be reduced below 10%. The majority prefer the option of not reducing the shareholding requirement below 10%. The second preferred alternative is the extension of the Directive scope to non-associated undertakings, but is limited to 29% of the responses.



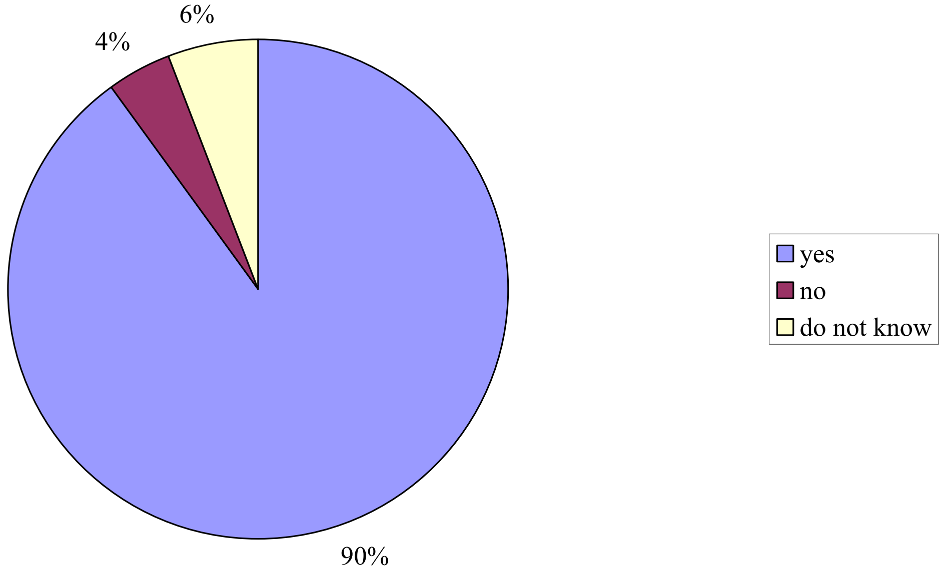
The questionnaire asked if the shareholding requirements of the Directive should be reduced to 10%. An important majority supported this initiative, 87%.



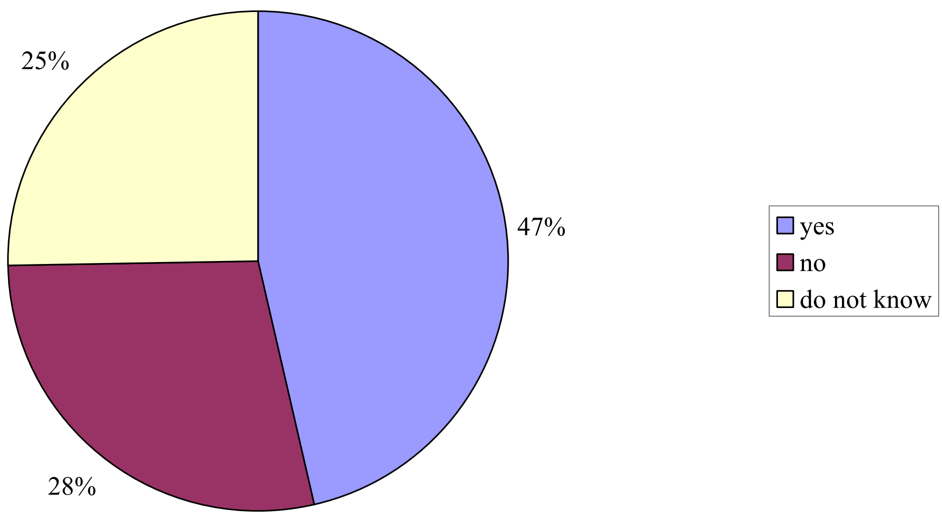
The questionnaire asked if indirect shareholdings should be taken into account when the minimum shareholding is being determined. Almost all contributors (91%) support this initiative. We can see the results in the following figure:



The questionnaire asked if the list annexed to the Directive should cover the same legal types as are included in the list of the Parent-Subsidiary Directive. Almost all contributors (89%) support this initiative. We can see the results in the following figure:



The questionnaire asked if the list should be extended so as to include other types of companies not referred to in the Parent-Subsidiary Directive. The most common answer was affirmative, but it does not reach half of the contributors. On the other hand, only 21,4% of the answers proposed the extension of the Directive to all types of entity. We can see the results in the following figure:



The questionnaire asked if the text of the Directive should be clarified in order to guarantee that its benefits apply to interest or royalty payments constituting an expense attributable to permanent establishments. Almost all contributors agree to this proposal. We can see the results in the following figure: