

# The future repeal of the EU Savings directive and its consequences

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By the law of 21 June 2005, as amended ("Savings Law")<sup>(1)</sup>, Luxembourg has implemented the European Savings directive (or "EUSD")<sup>(2)</sup> and several agreements concluded between Luxembourg and certain dependent or associated territories of the European Union ("EU"). The Savings Law is in effect as of 1 July 2005. By reason of the development of a global standard for automatic exchange of information ("AEOI"), the EUSD and thus the Savings Law are now destined to be repealed. Indeed, the European Council Conclusions of 21 March 2014 and the Economic and Financial Affairs Council Statement of 9 December 2014 demonstrate Member States clear preference for having only one standard for the AEOI on financial income.

## Abolishment of withholding tax and move towards automatic exchange of information

The general principle on which relies the EUSD the automatic exchange of information. However, in 2005, Luxembourg, Austria and Belgium<sup>(3)</sup> benefited from a derogation to such general principle and were authorized to apply during a transitory period a withholding tax, the rate of which increased over time up to 35%, on interest payments made to individuals being resident for tax purposes of another EU Member State.

More precisely, based on article 7 of Savings Law such withholding tax was applicable on payments of interest or other similar income made in Luxembourg by an economic operator (paying agent within the meaning of the EUSD) to (or under certain circumstances, to the benefit of) an individual or certain so-called "residual entities" resident or established in another EU Member State or in certain dependent or associated territories. As an exception, the beneficiary of the interest payments could formally agree for an automatic exchange of information with the tax authorities of its Member State of residence and give a specific mandate to his paying agent (e.g. the bank holding his account) to do so based on article 9 of the Savings Law.

With the adoption of the law of 25 November 2014, Luxembourg has abolished the above described withholding tax system and decided to apply the automatic exchange of information in all cases previously concerned by the withholding tax (articles 7 and 9 of the Savings Law were entirely redrafted). Such reform has entered into force with effect from 1 January 2015 (i.e. the updated law applies to interest income payments made after 31 December 2014). As a result, the first full scope communication of information between the Luxembourg tax authorities and their foreign counterparts in other EU Member States should take place in 2016 with regard to interest income derived in 2015.

On 19 January 2015, the Luxembourg Tax Authorities released an administrative circular (RIUE – n°4) on automatic exchange of information between EU Member States in the context of the taxation of savings of individuals (the "Circular").

The Circular aims at clarifying some aspects of the law of 25 November 2014.

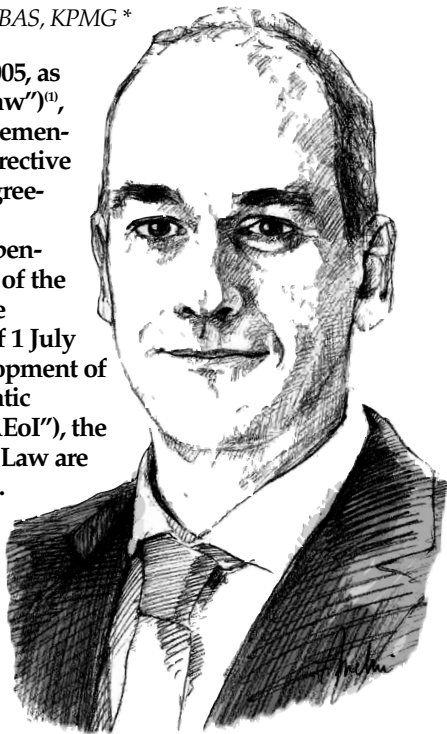
The Circular confirms that the automatic exchange of information on interest income is not applicable to legal persons (*personnes morales*), to Luxembourg residents and to residents of a non-EU country.

As a result of the abolishment of the withholding tax system, some clarifications were needed when it comes to the definition of the notion of paying agent upon receipt of an interest payment (so-called "residual entities"). The Circular also aims at providing these clarifications.

The deadline for the first communication to the Luxembourg Tax Authorities will be 20 March 2016 with respect to information of 2015. In case of missing, late, incomplete or false reporting, the economic operator risks a maximum penalty of 0.5% of the amounts that should have been reported.

## Towards a global norm for automatic exchange of information

In March 2014, the Council of the European Union adopted a directive amending the EUSD (Directive 2014/48/EU amending directive



2003/48/EC on taxation of savings income in the form of interest payments, "revised EUSD")<sup>(4)</sup>. The revised EUSD aims at enlarging the scope of the EUSD in its current version and applying the automatic exchange of information as a global standard. The revised EUSD must in principle be transposed by Member States before 1 January 2016 and applied as from 1 January 2017 (see however our comments below in this respect).

The ongoing process towards more transparency did however not stop with the adoption of the revised EUSD but rather took two additional and important steps as far as the "European FATCA" and "OECD FATCA" projects are concerned.

At EU level, one of the milestones in the movement for more transparency was the adoption of the directive on administrative cooperation in the field of taxation ("DAC")<sup>(5)</sup>. This directive is fully transposed in Luxembourg. What has been nicknamed the "European FATCA" is the project to extend the scope of the DAC in a FATCA-like manner. After a first political agreement found on 14 October 2014, the revision of the DAC has been formally approved on the 9 December 2014 (the "revised DAC")<sup>(6)</sup>.

In parallel, the OECD pushed forward its own initiative on AEOI and released on 13 February 2014 its global standard for automatic exchange of financial account information (the "Global Standard"). The Global Standard consists of two components, i.e. the Common Reporting Standard ("CRS"), which contains the reporting and due diligence rules to be imposed on financial institutions, and the Model Competent Authority Agreement ("CAA"), pursuant to which governments would agree to exchange the information reported. To become binding, the CRS needs to be implemented via bilateral or multilateral agreements such as the revised DAC. On 29 October 2014, Finance Ministers more than 50 countries and jurisdictions have signed a Multilateral CAA on the implementation of the Global Standard.

Under both the Global Standard of the OECD (for the so-called "early adopters") and the revised DAC, information related to fiscal years as from 1st of January 2016 will be exchanged between parties/ Member States as from 1st of January 2017 on an automatic basis. The two initiative have in common a very broad scope (dividends, sales, interest, all other forms of financial income and account balance) built on the FATCA model and more particularly the model 1 IGA.

## Relationship between EUSD and revised DAC

The adoption of the revised DAC necessarily raised the question on the future of the EUSD.

The last subparagraph of the new article 8(3a) introduced in the revised DAC states clearly that the provisions contained in this paragraph (paragraph 3a) will take precedence over the revised EUSD. In the explanatory memorandum (the "Explanatory Memorandum") related to the proposal for a Council directive repealing the EUSD published on 18 March 2015 (the "Proposal of repealing directive")<sup>(7)</sup>, the EU Commission confirms that "Since there is significant overlap between the two directives, there would thus be only a few cases where the revised Savings Directive would still apply."

These residual cases exist as a result of slight differences in the approaches taken by the EUSD and revised DAC, and specific exemptions included in the two directives.

The three cases identified by the EU Commission as currently covered by the EUSD (or in principle by the revised EUSD) and that should not fall within the scope of the revised DAC are as follows:

- Firstly, the revised DAC sets reporting obligations on Financial Institutions that are entities as defined therein. Therefore, unlike the EUSD, it does not set reporting obligations on individuals (e.g. brokers) that may pay financial income.
- Secondly, there are some exemptions in the revised DAC with regard to certain pension/retirement funds, credit card issuers, regulated tax-favoured accounts and similar financial institutions and products that pose a low risk for tax evasion.
- Thirdly, the paying agent on receipt approach in article 4(2) of the EUSD covers also interest paid by a non-participating jurisdiction through a Member State's paying agent on receipt; in addition, the look-through approach under article 2(3) and enhanced paying agent on receipt approach under article 4(2) of the revised EUSD cover also income paid through "Active" non-financial entities, as long as they are tax-exempt.

However, the EU Commission states that "The effect of these residual cases being covered or not by the EU legislation under discussion here is marginal in the context of the overall scope of the Amending Directive on Administrative Cooperation. The international application of the global standard and the close supervision of its implementation by the Global Forum on Transparency and Exchange of Information will minimise any risks associated with these residual cases."

Keeping the two legal systems (revised EUSD and revised DAC) operating in parallel would have meant having two sets of similar, but not fully aligned, customer due diligence rules, procedures and reporting systems — both in respect of financial institutions reporting to competent authorities, and of competent authorities exchanging information between themselves. Fortunately, the EU Commission admitted that "The cost of this would greatly outweigh the benefits of the additional coverage given by the Savings Directive." therefore opening the door to the repeal of the EUSD via the publication of the Proposal of repealing directive.

## Consequences on tax reporting

As a result of the repeal of the EUSD<sup>(8)</sup>, AEOI related to interest income earned by individuals within the EU should take place as follows<sup>(9)</sup>:

- Interest income earned in 2015 should be reported in 2016 based on the Savings Law (current scope of the EUSD), and
- Interest income earned in 2016 should be reported in 2017 based on the revised DAC as it will have been transposed into Luxembourg domestic law in the meantime.

In the context of the revised DAC, Austria received a derogation under article 2(2), on the grounds of structural differences, and is allowed to start applying the revised DAC up to one year later than other Member States. At the time of adopting the revised DAC, Austria announced that it would not make full use of the derogation. It was particularly difficult to know what this announcement would mean in practice.

It is therefore interesting to note that the EU Commission mentions in the Explanatory Memorandum that Austria "would start exchanging information by September 2017 on a limited set of accounts (only new accounts opened during the period 1 October 2016 - 31 December 2016), while making use of the derogation for other accounts".

To take the specific situation of Austria into account and in order not to leave any gaps in the reporting, article 1 (2) of the Proposal of repealing directive provides with specific rules for Austria.

## Conclusion

The future repeal of the EUSD is for sure good news for the actors of the financial sector in the widest meaning of the terms since the risk of having two legal systems (revised EUSD and revised DAC) operating in parallel with the adverse consequences mentioned above disappear.

However, the publication of the Proposal of repealing directive represents also another step towards the implementation of a global standard on AEOI confirming that current deadline of 1 January 2016 for the starting of the AEOI remains the target and that at this point of the year it would be very risky to bet on a deferment of the application of the CRS/ revised DAC.

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- 1) Law of 21 June 2005 Loi du 21 juin 2005 transposing the Council directive 2003/48/CE of 3 June 2003 on taxation of savings income in the form of interest payments, Memorial, as modified by the laws of 17 July 2008 and 19 December 2008.
- 2) Council directive 2003/48/CE of 3 June 2003 on taxation of savings income in the form of interest payments.
- 3) Belgium switched to automatic exchange of information as from 1 January 2010.
- 4) Council directive 2014/48/EU of 24 March 2014 amending directive 2003/48/EC on taxation of savings income in the form of interest payments, OJ L111, 15.4.2014.
- 5) Council directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and repealing directive 77/799/EEC, OJ L64, 11.3.2011.
- 6) Council directive 2014/107/EU of 9 December 2014 amending directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation, OJ L359, 16.12.2014.
- 7) Proposal for a Council directive repealing the Council directive 2003/48/EC published on 18 March 2015 (2015/0065 (CNS)).
- 8) Article 1 of the Proposal of repealing directive reads "Directive 2003/48/EC is repealed with effect from 1 January 2016".
- 9) With the exception of (in particular) the paying agents upon receipt for whom the obligations imposed by the EUSD will continue to apply until 5 October 2016 or until those obligations have been fulfilled.

## La table ronde de FARAD, à nouveau un grand succès

**FARAD International SA a tenu ce 2 avril 2015 la 9<sup>ème</sup> édition de sa «Table ronde sur l'intermédiation internationale». Le thème majeur développé au cours de cette journée était «Private Life Insurance Intermédiation Luxembourg ; Le point de rencontre des leaders de l'assurance sur la Place financière ; Opportunités 2015 – Les solutions Tailor Made».**

Organisée en collaboration avec les autorités du secteur de l'assurance, cette rencontre professionnelle a remporté une nouvelle fois un grand succès de participation avec une audience de plus de 150 participants. La journée a débuté par une intervention de l'invité d'honneur, Claude Wirion, Directeur du Commissariat aux Assurances, au sujet des nouvelles règles d'investissement pour les contrats d'assurances en unités de compte.

Ensuite, sous la présidence de Fernand Grulms, Managing Director de Pecoma Actuarial et Risk SA, se sont succédées les interventions de plusieurs acteurs spécialisés – du métier du conseil, du droit et de l'assurance – tous actifs dans le domaine du Private Life Insurance.

La matinée de la Table ronde s'est terminée sur deux panels de discussion, l'un au sujet de la loi sur le PSA et de ses opportunités, l'autre sur « une prise de pouls » du domaine du Private Life Insurance au Luxembourg. Deux Key-Note

Speakers étaient également invités. Tout d'abord, Matt Moran de PWC qui a présenté sa vision 2015 – 2020 concernant les modèles de distribution dans le domaine du Wealth Management et, ensuite, Anice Chlagou de Lombard Odier qui a partagé son expérience dans l'utilisation pratique de l'assurance en matière de structuration patrimoniale.

L'après-midi, les participants ont pu assister à 7 différentes masterclasses présentées sous l'égide des compagnies d'assurances ING Life, Vitis Life, IWI et Baloise Assurances. Y était traité, respectivement, du potentiel et de la réglementation de marchés spécifiques tels que la France, le UK, le Luxembourg, Israël et le Portugal.

Sous égide de FARAD, une masterclass était dédiée spécialement au thème de la Voluntary Disclosure, propre marché italien, et deux autres traitaient des thématiques «Passion & Insurance – Art – Ecologie – Philanthropie» et «Islamic Finance & Insurance - Takaful».

Forte de ce succès renouvelé, FARAD International SA vous donne, d'ores et déjà, rendez-vous le jeudi 17 septembre 2015 pour la 10<sup>ème</sup> édition de sa Table Ronde.

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