

THE
EU SAVINGS TAX
DIRECTIVE
AMENDMENTS



A
*practical
Guideline*

This guideline endeavours to illustrate the key extensions of the revised EU Savings Tax Directive with practical examples of what will be in or out of scope.

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1. INTRODUCTION

1.1 Summary

There are basically five important changes to the EU Savings Tax Directive (EUSD):-

a) Extend scope to untaxed entities and legal arrangements i.e. companies, trusts, foundations and partnerships:

✎ If effectively managed inside the EUSD territorial scope then the entity / arrangement itself becomes a “Paying Agent Upon Receipt” regarding the payments secured in its bank accounts anywhere in the world.

✎ If effectively managed outside EUSD territorial scope then bank remains the Paying Agent but must 'look through' the entity / arrangement to the beneficiary.

b) Banks which route payments to another bank outside the EUSD territory remains Paying Agent if it is aware of the Beneficial Owner.

c) Interest includes an expanded definition of funds from UCITS to all types of collective investments.

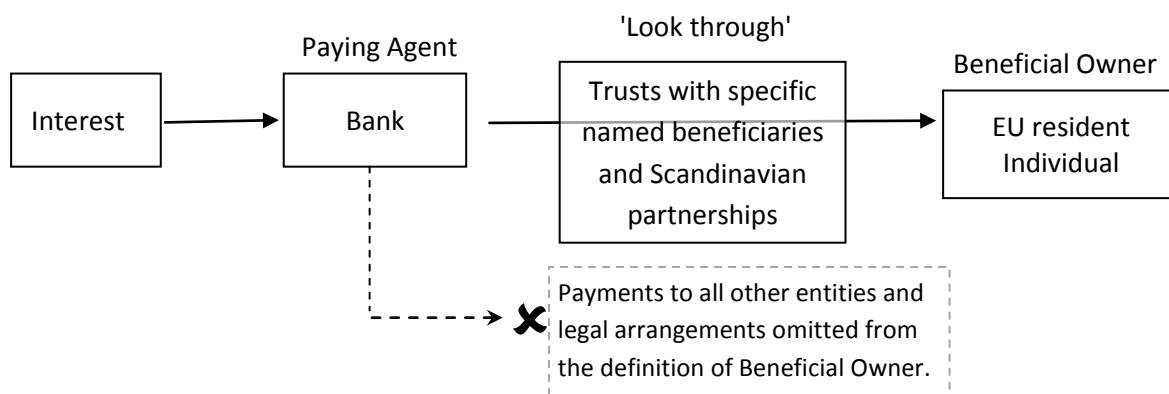
d) Interest includes capital guaranteed structured products and other minimal risk securities, including derivatives.

e) Interest includes benefits of life insurance policies whose performance is linked to investments, irrespective of the mortality risk or longevity risk.

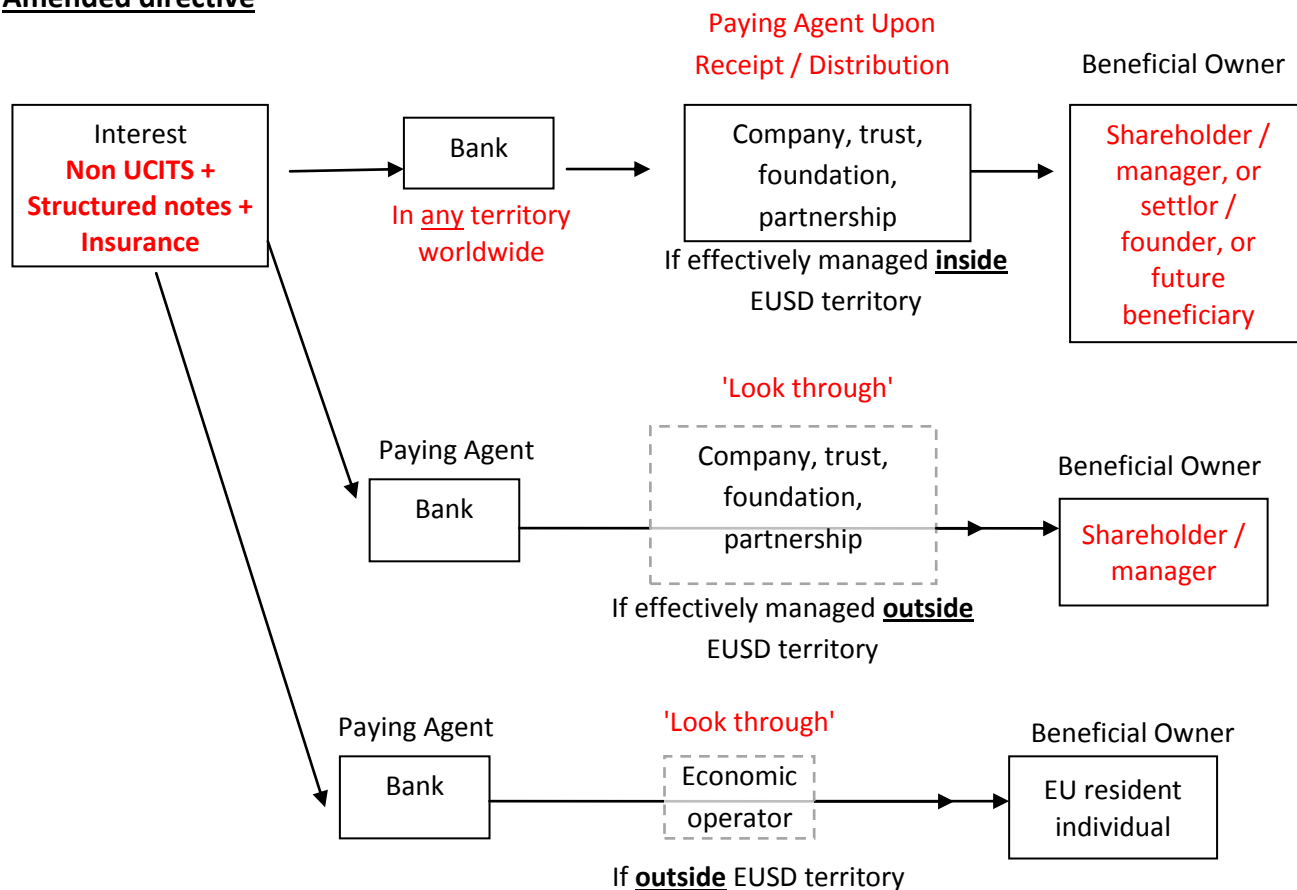
1.2 Revision of Paying Agent, Beneficial Owner and Interest

The amendment provides updated definitions of a) Interest b) Paying Agent, and c) Beneficial Owner. The expanded definition of interest is straightforward and concerns collective investments, derivatives and unit-linked insurance. The changes to the definition of Beneficial Owner and Paying Agent responsibilities mostly relate to the extension of the scope of the directive to entities and legal arrangements:



Current directive - limited scope regarding entities and legal arrangements:



Amended directive



1.3 EU Savings Tax Amendment - Paying Agent, Beneficial Owner and Interest

PAYING AGENT  (Who applies the directive)	BENEFICIAL OWNER  (Who is taxed)	INTEREST  (What is taxed)
<p>“Upon Receipt” - Untaxed entities and arrangements which are effectively managed <u>within</u> the territorial scope will be “Paying Agents Upon Receipt”.</p> <ul style="list-style-type: none">  E.g. Liechtenstein Stiftung, Guernsey trust, BVI company, Spanish deceased estate, UK investment club, etc.  Nominee shareholders or nominee settlers / founders according to the EU money laundering directive, categorised as “<i>Trusts and Service providers</i>” and hence are also “Paying Agents upon receipt” who must identify the beneficiary for whom they are acting for.  A bank within the EUSD territory is a “paying agent upon receipt” if it has a discretionary mandate over accounts located out of EUSD territory as this is a legal arrangement, e.g. Panama subsidiary / Singapore branch. <p>Option : Untaxed entities and arrangements similar to a fund can opt out of being a Paying Agent upon receipt and be elect to be treated as a collective investment.</p>	<p>For untaxed entities and arrangements effectively managed <u>inside</u> the territorial scope the Beneficial Owner is :</p> <ul style="list-style-type: none">  Anyone entitled to immediately receive income, or alternatively, it is the natural person who exercises control over the management of a legal entity  If no immediate beneficiary is identifiable, the Beneficial Owner is the individual who contributed the assets to establish the entity / arrangement i.e. settlors / founders.  If no immediate beneficiary or contributor of assets is identifiable, the Beneficial Owner is the person who within 10 years, later becomes entitled to payment. In this case the entity / arrangement is a “Paying Agent Upon Distribution”. 	<p>For untaxed entities / arrangements inside the territorial scope, interest received in its bank account held <u>anywhere</u> in the world, even outside EUSD territory.</p> <ul style="list-style-type: none">  E.g. Isle of Man company with bank account in Seychelles
<p>Banks which route payments via non-territory network</p> <ul style="list-style-type: none">  E.g. Bank in Jersey routing fund interest via accounts in their Hong Kong branch. 	<p>For untaxed entities and arrangements established <u>outside</u> the territorial scope the Beneficial Owner is the beneficiary according to the EU directive on money laundering.</p> <ul style="list-style-type: none">  E.g. Panama foundation, Hong Kong private company, Bahamas foreign trust, Aruba Stichting, etc.  If all beneficiaries have 25% or less ownership, the Beneficial Owner is the individual who has control over the management.  Discretionary trusts / foundations effectively managed outside the EUSD territory.  Non-EU nominee shareholders. 	<p>All collective investments</p> <ul style="list-style-type: none">  E.g. UCITS III, OEICs, etc. <p>Life insurance policies</p> <ul style="list-style-type: none">  E.g. Portfolio Bonds.  Short term pensions and fixed annuities.  Issued before July 2010  Unit linked policies with no mortality cover, such as health, annuity certain, etc.
		<p>Structured products with at least a 95% capital guarantee.</p> <ul style="list-style-type: none">  Capital gains on the note will be deemed as interest  Within scope even if the capital guarantee not provided by fixed income.  Issued before July 2010 <p>Securities of any kind containing or emulating fixed income returns.</p> <ul style="list-style-type: none">  E.g. Derivative contracts, interest swap funds, CDOs, repos, baskets / certificates of bonds, etc.  Issued before July 2010

Legend

 In scope	 Out of scope	 Surprise
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2. Paying Agent

2.1 Routing payments via international network

If a bank remits interest to other bank outside the territorial scope, knowing that the recipient is a Beneficial Owner, then the sending bank remains a Paying Agent.


 Jersey bank distributing payments to client accounts in Hong Kong.

2.2 Paying Agent Upon Receipt

2.2.1 Untaxed entities and legal arrangements within territory: The revision contains an indicative list of untaxed entities / arrangements which are effectively managed* within the directive's territory as "Paying Agent upon receipt". The logic for allocating responsibility of Paying Agent to an entity / arrangement is that it knows the ultimate individual beneficiary, even when there is no requirement to publically file ownership.


Important




 The Paying Agent upon receipt applies the savings tax provisions (reporting or withholding) on its accounts located anywhere in the world. This means that automatic reporting could occur even if the bank account is located in a jurisdiction with banking secrecy, such as Switzerland or Singapore

Important



 A bank within the directive's territory which controls a customer's account located out of jurisdiction is a Paying Agent Upon Receipt because this is a legal arrangement, e.g. a bank in Andorra is the Paying Agent if it manages a customer's account in their Panama subsidiary, or if a bank in Switzerland has discretionary mandate agreement over a portfolio account in their Singapore branch.


 Nominee shareholders of companies - the EU directive on money laundering and terrorist financing categorises nominees as '*trust and company service providers*' and hence are Paying Agents and thus must identify the Beneficial Owners for whom they are acting for.

* **Place of effective management** of an entity / arrangement, with or without legal personality, shall mean the address where key management decisions are taken that are necessary for the conduct of the entity's activity as a whole. Where key management decisions are taken in more than one country or jurisdiction, the place of effective management shall be considered to be at the address where most of the key management decisions are taken relating to the assets producing interest payments within the meaning of this Directive;

Legend






2.2.2 Becoming a “Paying Agent Upon Distribution”: If the management of an entity / arrangement cannot identify an immediate beneficiary nor identify the individuals(s) who initially directly or indirectly contributed the assets, then the “Paying Agent Upon Receipt” becomes a “Paying Agent Upon Distribution”. The Beneficial owner will be the person who within 10 years becomes entitled to payment.

 This will be most likely for a discretionary trust or foundation where the settler / founder is deceased or claim they do not know the source of the assets which were used to establish the trust / foundation.

2.2.3 Option to be treated as a collective investment: The entity / arrangement has the option of not being a 'Paying Agent Upon Receipt' or a 'Paying Agent Upon distribution' if it is *similar* to a collective investment by electing to be treated as a collective investment. This means the bank making or securing interest payments for the entity / arrangement reverts to be the Paying Agent.

 E.g. a private investment club

Legend

 In scope	 Out of scope	 Surprise
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3 Beneficial Owner



3.1 Untaxed Entities and Arrangements within territorial jurisdiction

An entity or arrangement established or effectively managed within the EUSD territory is a Paying Agent Upon Receipt and must determine the Beneficial Owner according to EU money laundering directive, depending on the following three scenarios:-

3.1.1 Immediate beneficiary identifiable: Beneficial Owners are deemed to be the individuals who are immediately entitled to receive the income arising from the assets producing such payment, when the entity or legal arrangement receives the payment or when the payment is secured on its behalf;

☞ The Beneficial Owner of a company is:-

- 💰 any shareholder who owns more than 25% equity of a company, or
- ⊗ alternatively, it is the natural person who exercises control over the management of a legal entity;

☞ The Beneficial Owner of a trust or foundation is:-

- 💰 where the future beneficiaries have already been determined, the natural person(s) who is the beneficiary of 25% or more of the property; or
- ⊗ the natural person(s) who exercises control over 25% or more of the property of a legal arrangement or entity;

3.1.2 No identifiable immediate beneficiary: If at the time of receipt of payment it is not possible to identify a beneficiary who is immediately entitled to the interest payment, the Beneficial Owner is then deemed to be the individual who directly or indirectly contributed the assets to establish the entity / arrangement. (similar to a U.S. grantor trust)

💰 If a discretionary trust claims at the time of receipt of income it does not yet know the beneficiary then the settler will be deemed the Beneficial Owner.

💰 This will also similarly affect foundation councils who know the founder, even if it is not publically registered.

⊗ Nominees are commonly used, for example a founder of a Liechtenstein foundation or shareholder of a BVI company. According to the EU directive on money laundering and terrorist Art 3.7(e), nominees are categorised as '*trust and company service providers*' and hence will be Paying Agents Upon Receipt themselves, and must thus identify the true beneficiary for whom they are acting.

Legend

💰 In scope	🍷 Out of scope	⊗ Surprise
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Beneficial Owner continued...



3.1.3 Paying Agent Upon Distribution: If there is no immediate beneficiary identifiable nor identifiable contributors, then the Paying Agent upon receipt must keep track of interest and later apply the savings tax provisions with the Beneficial Owner being the person who at a within 10 years becomes entitled to payment.

⊗ This will be the standard for a discretionary trust / foundation where the settlor / founder is deceased.

Legend

 In scope	 Out of scope	 Surprise
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3.2 Untaxed Entities and Arrangements outside EUSD territorial jurisdiction

For an entity / arrangement established or effectively managed in a jurisdiction **outside** the EUSD territory the Paying Agent is the bank (economic operator) who makes or secures an interest payment which is not subject to effective taxation.

Looked through: The Paying Agent must look through the entity / arrangement to the Beneficial Owner according to the EU money laundering directive.

☞ The Beneficial Owner of a company is:-

- 💰 any shareholder who owns more than 25% equity of a company, or
- ⊗ alternatively, it is the natural person who exercises control over the management of a legal entity;

☞ The Beneficial Owner of a trust or foundation is:-

- 💰 where the future beneficiaries have already been determined, the natural person(s) who is the beneficiary of 25% or more of the property; or
- ⊗ the natural person(s) who exercises control over 25% or more of the property of a legal arrangement or entity;

⚡ If an immediate beneficiary or manager is not identifiable then there is no Beneficial Owner. The EU money laundering directive defines a beneficiary in this case as the class of persons in whose main interest the legal arrangement or entity is set up or operates. This does not help identify a Beneficial Owner individual for savings tax purposes.

⚡ Also the settlor / founder is not deemed a Beneficial Owner because banks in several EU Member States do not identify the individuals who initially contributes the entity / arrangement's assets.

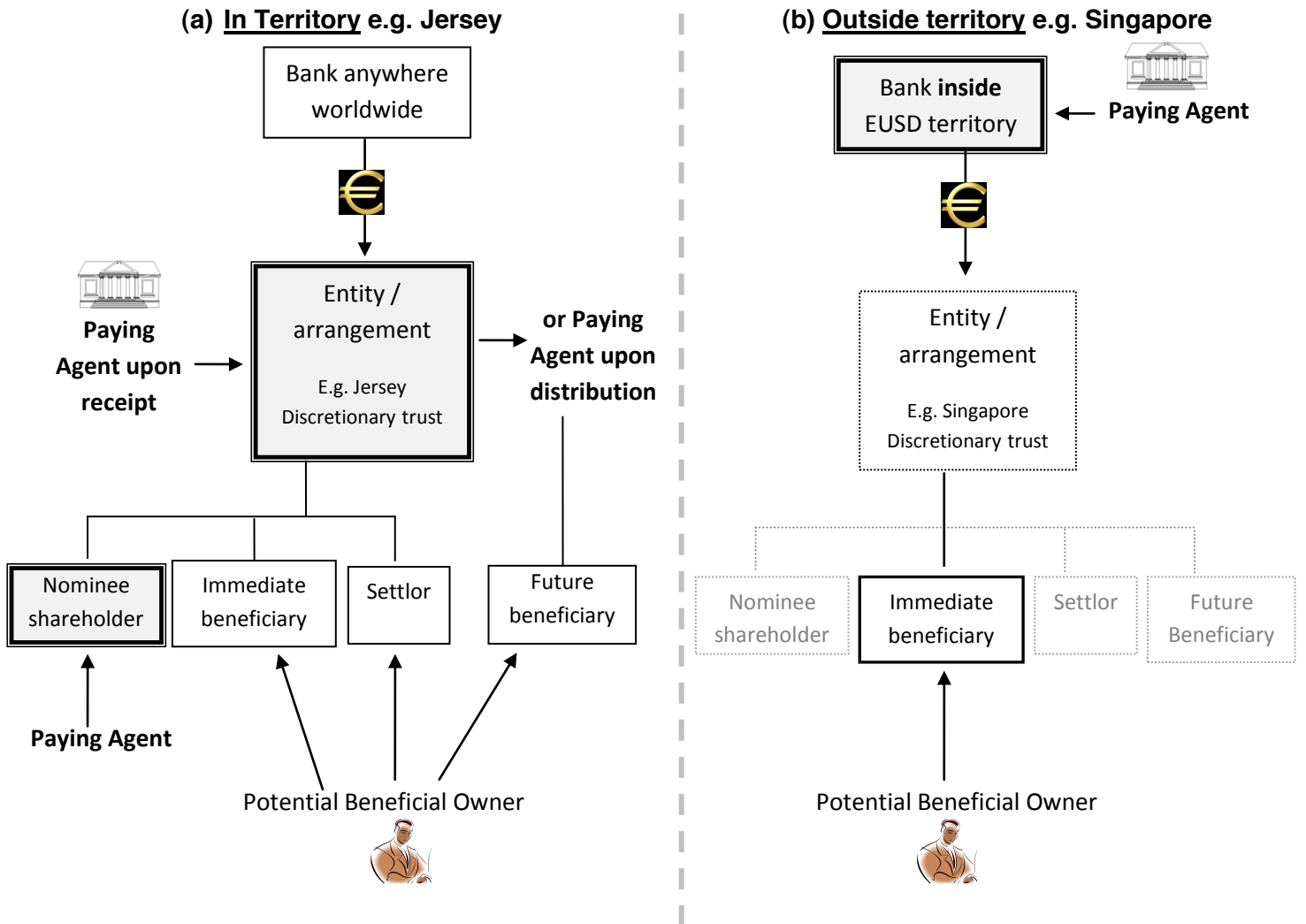
⚡ There is no Paying Agent Upon Distribution when a Beneficial Owner later becomes entitled to the income.

Legend

💰 In scope	⚡ Out of scope	⊗ Surprise
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3.3 Beneficial Owners of entities / arrangements within versus outside the EUSD territory



4 Interest



The amendment extends the definition of interest to all securities of any kind that either contain interest or emulate the risk free nature of fixed income returns:-

4.1 Collective Investments

The current scope for collective investments is narrowly restricted to funds classified as UCITS. The amendments now include all funds irrespective of the legal form or scheme setup and irrespective of any restriction to a limited group of investors.

<ul style="list-style-type: none"> 💰 Luxembourg SICAV II, SICAR, SIF-SICAV 💰 Ireland UCITS-III collective investments 💰 Investment Company with Variable Capital / OEICs 💰 Professional investors funds 💰 Qualifying investors funds 	<ul style="list-style-type: none"> 💰 Caribbean <i>non-UCITS equivalent</i> funds 💰 Hedge funds 💰 Private equity funds 💰 Income trusts 💰 Managed Futures Accounts which act like a mutual fund for more than one investor 💰 Micro finance funds 💰 Pooled private investment clubs 	<ul style="list-style-type: none"> 💰 Closed end funds 💰 Unit trusts 💰 Fonds commun de placement 💰 Beleggingsvennootschap met vast kapitaal / PRIVAK 💰 Exchange Traded Funds (ETF) 💰 Real Estate Investment Trusts (REIT) 💰 Listed investment company
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⊗ A member State has the option to set any lower threshold on the percentage of debt assets in a collective investment to be included in scope. The exercise of the option shall be binding on the other Member States.

Legend

💰 In scope	🍷 Out of scope	😞 Surprise
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4.2 Capital Guaranteed Structured Products

The amendment states interest also includes any income paid or realised, or credited to an account, relating to **securities of any kind**, and where:

- the conditions of a return of capital defined at the issuing date include a commitment towards the investor that he receives, at the end of the term, at least 95% of the capital invested, or
- the conditions defined at the issuing date provide for a link of at least 95% of the income from the security to interest or income.

⊗ This effectively means **all** gains for capital guaranteed notes will be deemed as interest, including the derivative capital gains in addition to the zero coupon bond gains.

⚡ Structured products with less than 95% guarantee or less than 95% promised debt income are out of scope;

4.3 Derivatives

Any income paid or realised, or credited to an account, relating to securities of any kind. “Securities”, are defined as:

- ✍ fungible - *one unit easily exchanged for another unit of the same commodity*
- ✍ negotiable instrument - *A transferable contract that promises to pay the bearer a sum of money at a future date or on demand*
- ✍ representing financial value.

Included in scope will be derivatives such as:-

- 💰 Baskets and certificates which are either static or active in nature.
- 💰 Derivative contracts, such as forwards, futures, options and swaps.
- 💰 Derivative which are sold openly on the market such as credit default swaps, synthetic securitization contracts, credit default swaps, Collateralized Debt Obligations (CDOs), sale and repurchase agreements (Repos), LEPOS on bonds, etc., are securities and thus are within scope.
- ⚡ Derivatives which are exclusively contracts between two parties and are not sold to others such as total return swaps are defined as non security contracts and are out of scope.

Legend

💰 In scope	⚡ Out of scope	⊗ Surprise
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4.4 Life Insurance Benefits

All life insurance policies, irrespective of the level of mortality cover will be within scope if more than 25% of the benefit is linked to debt claims.

⊗ Life insurance policies for the purpose of pensions or fixed annuities are within scope if benefits are paid within five years.

⊗ A member State has the option to include within scope all life insurance policy benefits “regardless of the composition of performance obtained from a life insurer established within that State”, i.e. less than 25% debt link. The exercise of the option shall be binding on the other Member States.

⚗ The amendment states that life insurance policies for the purpose of pensions are considered as pensions only if the benefits are paid after 5 years and are thus out of scope. *It remains unclear what determines that the purpose of life insurance policy as a pension, i.e. merely a marketing term for a international portfolio bond?*

⚗ Besides life insurance, other insurance benefits such as health unit-linked policies, long term fixed annuities and annuity certain are out of scope because insurance is excluded from the definition of *securities*.

☞ **Note:** The Administrative Co-operation and Mutual Assistance Directive of 2011 covers income from employment, directors' fees, dividends, capital gains, royalties, ownership of and income from immovable property. And importantly, **life insurance products** and pensions not included in the EU savings tax amendments.

===== END OF REPORT =====

Legend

In scope	Out of scope	Surprise
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