Europe's increasingly complex tax reporting

Asset Management Insights

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To market their products effectively across Europe, asset managers need a deep understanding of ever-changing tax reporting requirements.

Over the last 30 years, European cross-border fund distribution has increased exponentially, through the 1985 introduction and ongoing improvement of the Undertakings for Collective Investment in Transferable Securities (UCITS) passport regime.

With the introduction of a similar harmonised approach to passporting for alternative fund ranges under the Alternative Investment Fund Managers Directive (AIFMD), it should be expected that managers of alternatives funds would increasingly seek to register their funds for distribution across borders. The ever-changing regulatory landscape has brought both opportunities and increased compliance obligations, including tax reporting obligations for asset managers.

Investor tax reporting for funds is a very demanding and constantly evolving area. In recent years, several jurisdictions including Austria, Germany, Switzerland and the United Kingdom have either introduced new tax reporting regimes or modified existing ones. In order to compete and to market their products effectively across Europe, fund managers now require a deeper understanding of country-specific investor tax reporting requirements.

The challenges

While the overall aim of most European tax reporting regimes is to ensure the most appropriate tax solution for the end investor, the actual country-specific technical reporting provisions can differ greatly. Asset managers may struggle to cope with complex legislation, and are required to interact with multiple advisers across territories where their funds are distributed, in order ensure that their products are compliant from an investor tax reporting perspective.

In both Germany and the UK, for example, advance information is required to be provided to tax authorities in order to ensure that beneficial tax treatment is afforded to investors in the fund. Often, a lack of awareness of such provisions can lead to significant issues when selling to key investor groups if these requirements have not been considered during the product structuring phase. In addition, there are ongoing daily, monthly or annual reporting compliance obligations, which require cross-border coordination between service providers. Navigating the waters of this increasingly challenging environment can be burdensome and costly.

Overview of European tax reporting regimes

The most popular markets for cross-border distribution of funds in Europe are the UK, Germany, France, Switzerland and the Netherlands. Of these, the UK, Germany, Austria and Switzerland have the most sophisticated requirements in relation to tax reporting. Italy and Belgium also have investor reporting requirements. In this article we outline some of the key considerations of each tax reporting regime.

UK

Why?

Offshore funds distributed into the UK may seek to apply for UK reporting fund status in order to secure beneficial tax treatment for their UK investors. The UK Offshore Funds (Tax) Regulations, enacted in 2009, introduced a new regime for offshore funds distributed into the UK to comply with.

HMRC, the tax authority, enforces strict deadlines for submission of applications for entry into the reporting fund regime. Funds are typically required to submit applications before the end of the accounting period for which UK reporting fund status is required for the relevant share class. As a result, close monitoring of new launches requiring reporting fund status is important.

How?

Funds have to provide details of the reportable income per unit for the share classes in the fund that have entered the reporting fund regime. This information must be reported to both HMRC and to investors within six months of the end of the fund's accounting period. To the extent that the reportable income of the fund exceeds the amount of any distributions paid, this 'excess' is treated as an additional distribution in the hands of the investors holding shares at the end of the relevant accounting period. It is deemed to have been received six months after the end of the accounting period. As investors will use this information when completing their tax returns, accurate and timely reporting of the relevant information is paramount from an investor relations perspective.

Germany

Why?

Tax reporting obligations for foreign funds are regulated by the German Investment Act (in German referred to as Investmentsteurgesetz or InvStG). Under the InvStG, a fund can be 'transparent' or 'non-transparent' for German tax purposes. For German investors only the 'transparent' fund provides the highest tax efficiency.

How?

Various reporting requirements need to be fulfilled in order for a German investor to obtain the maximum tax optimisation from offshore funds, including annual reporting and daily/NAV frequency-based tax reporting.

The InvStG also imposes a compulsory daily publication of the ADDI (Accumulated Deemed Distributed Income). To benefit from certain tax advantages in Germany, the InvStG also requires the publication of 'Zwischengewinn' ('Interim Profit'), 'Aktiengewinn I & II' ('Equity Profit I & II') and 'Immobiliengewinn' ('Real Estate Profit'). The accuracy of this information is key for German investors, not only to ensure a smooth tax declaration process but also to avoid dormant tax risks.

Austria

Why?

From an Austrian tax perspective, investment funds are considered transparent, requiring a direct allocation of funds' income to their investors. Austrian investors are, therefore, subject to annual taxation regardless of whether the income of the fund is distributed or accumulated.

How?

Accumulated income (also referred to as deemed distributed income (DDI)) has to be calculated and electronically filed by an Austrian tax representative.

Switzerland

Why?

Swiss private investors have to declare their taxable income and the value of the investment in their tax return. Therefore, it is recommended that information is made available to Swiss private investors to protect them from prohibitive income taxation. It is necessary to ascertain the taxable income in order to separate it from tax-exempt capital gains in the hands of Swiss private investors, based on Swiss calculation principles.

How?

In Switzerland, no specific deadline for calculating the income tax value applies. However, generally we recommend publishing income tax values by April/May of the year following the fiscal year end of the entities, as Swiss private investors generally start preparing their tax returns at that time.

For the purposes of income tax and personal wealth tax, the respective taxable income and net asset value per share can be provided to the Swiss Federal Tax Administration (FTA). The FTA then publishes the above values in the official rates list. Please note, the FTA will only publish share classes that have a Swiss Valoren number.

Italy

Why?

Since 1 July, 2014, profits from certain Collective Investment Funds and SICAVs (hereinafter 'funds') have been generally subject to a 26% final taxation (in lieu of the previous 12.5% tax rate).

Profits deriving from direct investment in eligible bonds (i.e., Italian government bonds and other eligible securities, including government bonds issued by countries allowing an adequate exchange of information with Italy) generally continue to be subject to the lower 12.5% tax rate. In order to prevent 'indirect' (i.e., through funds) investment in eligible bonds being subject to the 26% tax rate, Decree 13 December 2011 (ref. 11A16232) sets out a methodology to determine the portion of profits derived from funds (investing directly and/or indirectly in eligible bonds) that should be exempt from the 26% tax rate.

The benefit for investors is that only 62.5% of profits associated with 'indirect' investment in eligible bonds should be subject to the new 26% tax rate. As a result, 37.5% of these profits will be tax exempt.

All the funds listed below that invest in eligible bonds and have Italian private individual (retail) investors should consider Italian investor tax reporting requirements:

- Italian funds
- Non-Italian UCITS funds (compliant with UCITS IV Directive) established in the EU and in certain EEA Countries
- Non-Italian non-UCITS funds established in the EU and in certain European Economic Area (EEA) countries and managed by a regulated fund manager
- The fund tax reporting rules also apply to non-Italian Funds that are not authorised for distribution in Italy
- Fund tax reporting is not mandatory; however, without it Italian investors will not be able to obtain beneficial tax treatment

How?

In order to identify the portion of profits/losses associated with 'indirect' investment in eligible bonds, it is necessary to determine an average percentage. This can be calculated on the basis of the ratio between the value of the eligible bonds and the total asset value (net of any 'tax asset') over the fund's last two available financial statements (semi-annual or annual).

Belgium

Why?

Foreign funds are subject to a 0.0925% tax on the total of the net outstanding amounts invested in Belgium, as at 31 December of the previous year, to the extent that they are registered with the Belgian financial regulator. The net asset tax (NAT) return must be filed annually, before 31 March, based on a tax year corresponding with the calendar year.

How?

This tax return must provide the taxable basis of the fund, i.e. the total of the net outstanding amounts invested in Belgium as of 31 December of the previous year, including the units acquired abroad on behalf of a Belgian resident. The NAT return should specify the taxable amount on a sub-fund basis. To avoid any double taxation, funds participating in other investment institutions are allowed to offset the amounts that have already been subject to this tax at the level of other institutions.

Where the fund fails to file the necessary information, the tax is assessed on the total of the gross amounts invested in Belgium, at 31 December of the previous year. Where an incorrect or incomplete return is filed, a minimum fine of EUR 250 is due (up to a maximum of twice the tax which has not been paid, with potential relief in the case of obvious oversights or mistakes which do not influence the tax liability). Where the return is filed late, a fine of EUR 250 per week applies.

Integrated solutions needed

Multi-market tax reporting solutions are necessary in order to cope with these challenges. Asset managers distributing their funds in an ever-increasing number of countries need multi-jurisdictional tax reporting services. PwC reviews and/or calculates annual tax figures according to the local laws of many jurisdictions. Additionally, we act as an outsourced service provider for a number of high-profile clients, producing calculations under the UK tax reporting regime.

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