Guernsey and ATAD III

Briefing Summary: Due to the potential negative impact of ATAD III, fund managers and institutional investors may wish to consider replacing existing EU asset-holding companies with Guernsey holding structures. The avoidance of such ATAD III implications, combined with a flexible corporate regime and certainty on substance, make Guernsey a highly attractive domicile.

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What is ATAD III?

In December 2021, the European Commission ("EC") published its proposed Anti-Tax Avoidance Directive (known as "ATAD III"). ATAD III is intended to discourage the misuse of shell companies within the European Union ("EU"). The Directive is aimed at EU-resident entities which claim benefits under double taxation treaties and other EU Directives, but which lack a minimum level of economic substance.

ATAD III determines an entity's substance by a prescribed series of "gateway" tests, intended to establish whether an entity has a genuine economic link with its country of residence.

If the company passes any of these "gateways", it must (subject to certain exemptions) report specified information on its activities and economic substance in its tax return.

Any reporting entity which fails to provide sufficient evidence that it is not a shell entity may be unable to obtain tax residency certificates, and may thereby be denied the benefits of double tax treaties and other EU Directives. Turnover-based financial penalties may also be applied to such entities. Further, payments to third countries may not be treated as flowing through the entity and may be subject to withholding tax at the level of the payor. Payments to the entity will be taxed in the state of the entity's shareholder.

Entities established solely for the purpose of accessing double taxation treaties available in certain EU jurisdictions, and which have minimal substance in such jurisdictions, are therefore at risk.

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The EC has also announced its intention to follow ATAD III with a directive which is aimed at non-EU shell companies.

What does this have to do with Guernsey?

Guernsey is not (and has never been) part of the EU, and Guernsey vehicles do not typically seek to benefit from EU-facing double taxation treaties.

Accordingly:

- ATAD III does not apply to Guernsey vehicles; and
- even if ATAD III equivalent provisions were extended to cover Guernsey vehicles, and EU double-tax treaty benefits were denied, this is unlikely to have any detrimental impact on Guernsey vehicles.

Also, Guernsey has previously implemented economic substance regulations, which came into force on 1 January 2019. As a result, Guernsey continues to be considered by the EU Council to be a cooperative jurisdiction for tax purposes.

What should you do next?

We would advise any firms with EU holding companies to consider now whether they may be adversely affected by ATAD III.

The draft ATAD III text has a look-back period to determine undertakings that may be considered to lack economic substance. It is therefore important that consideration is given now as to whether the gateways apply in order to ensure that there is sufficient time for action to be taken to mitigate any potentially adverse tax implications.

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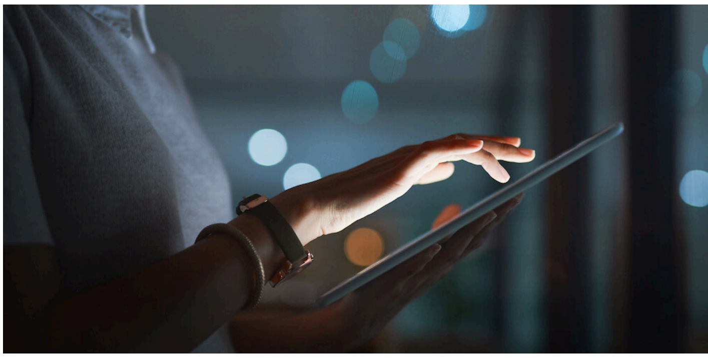

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