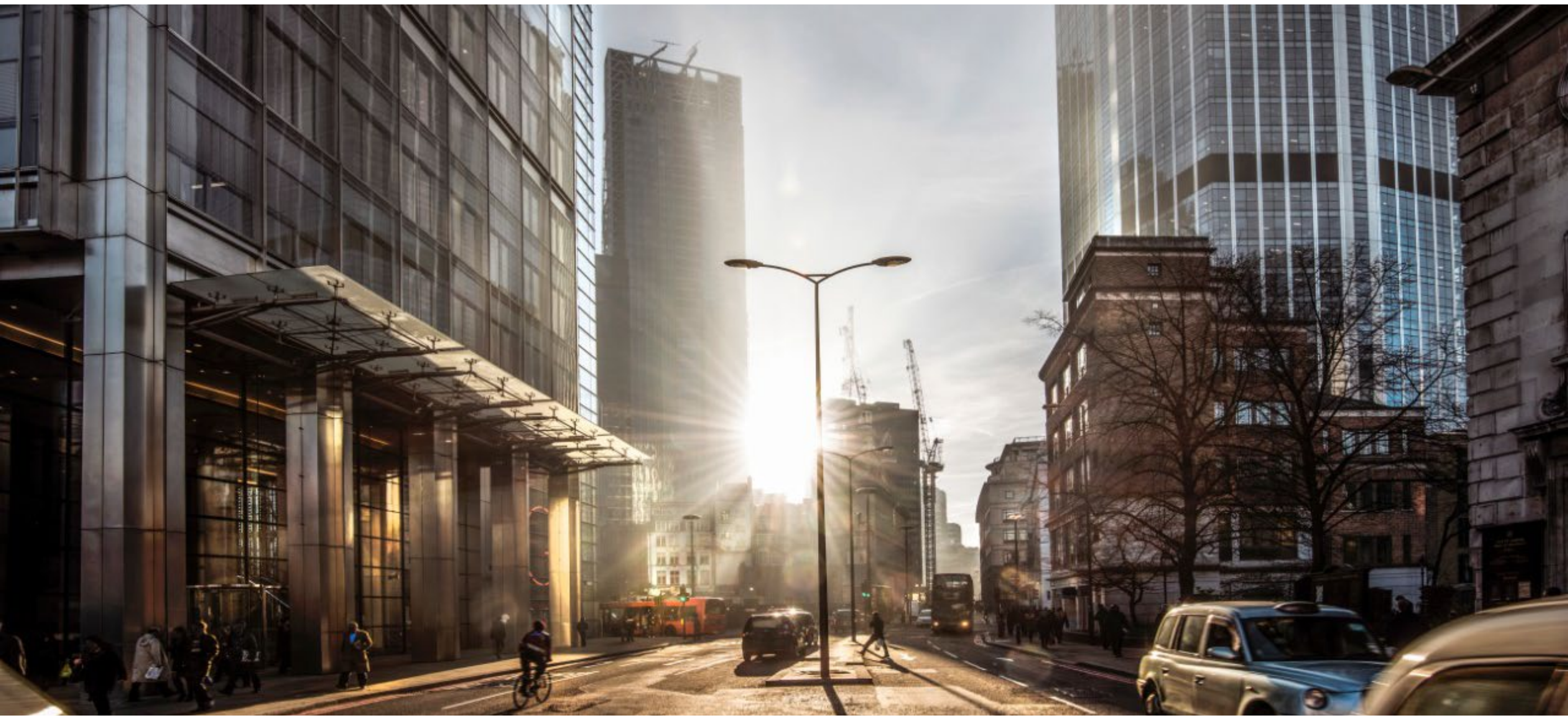
ATAD 3: The European Parliament provides initial thoughts

In May 2022's edition of PwC UK's Keeping up with Alternative Investment Funds ("KUWAIF") , our colleagues Gareth Hughes and John Holt penned an insightful article 'Corporate Substance - time to get it right'. If you haven't read it, we would recommend doing so for a broad summary on implications of having or being unable to demonstrate sufficient substance in jurisdictions in the international tax landscape, the article from The Suite can be found here. This is particularly important considering the mooted third instalment of the EU's Anti-Tax Avoidance Directives, the unsurprisingly named "ATAD 3" (or "ATAD III" if you like Roman numerals and extra keystrokes).

At the time when Gareth and John had written their article, ATAD 3 had been drafted by the European Commission and was sent down to the European Parliament. May's KUWAIF article summarised this Directive and identified a few features that may cause concern for investment managers, such as the apparent restriction on the outsourcing of operations by entities within a fund structure or having another EU Directive (remember DAC 6?) which requires them to look back at their arrangements since 1 January 2022 and apply "gateway" tests which are yet to be finalised in the legislation.

Gareth and John's article did feature a warning to the reader that by the time of reading some of these features may have been resolved; this was prophetic as the European Parliament's Committee on Economic and Monetary Affairs ("ECON") released a draft report setting out their proposed amendments to ATAD 3. A link to the draft report can be found here. Please note, however, that this is a draft report and further amendments can be made by ECON until 6 September 2022. A vote isn't due to be taken until 17 November 2022 and even then, the European Commission can then decide to reject the amendments. Once the Directive is ratified by the European Council, there still may be some derogations when Member States implement ATAD 3 into their domestic laws, so there is some way to go.

Please find a table below setting out a selection of ECON's amendments, but for those who cannot contain their excitement about the big announcements, there are key relaxations for outsourcing to associated enterprises in the same jurisdiction and a deferral of the implementation of ATAD 3 to 1 January 2025 and whilst the two year "look back" period remains, at least this new date isn't in the past (at the time of publishing). The relaxation on outsourcing would be particularly welcomed by the alternative investment management industry as whilst many fund structures may have ample substance and activities "in-country", ATAD 3 would seemingly only permit those of a company's in-country parent to be considered.



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ATAD 3: The European Parliament provides initial thoughts (continued)

Item	**Per Draft ATAD 3**	**ECON's draft amendment**	**Relaxation or tightening?**
Outsourcing of administration of day-to-day operations and the decision making on significant functions	See previous article for more information, but broadly only to parent companies in same jurisdiction	Can be outsourced in jurisdiction to associated enterprises	Relaxation
Exclusions for regulated financial undertakings	None	Yes	Relaxation
Gateway conditions:			
Revenue of "shell" being "relevant income"company	More than 75%	More than 80%	Relaxation
Relevant income of shell company being outside its jurisdiction	At least 60%	More than 65%	Relaxation
Headcount generating relevant income	At least five full time workers carrying on activities for company	Same as draft but the workers need to work in the state of residence of the entity	Tightening
Assets of shell company being outside its jurisdiction	More than 60%	More than 55%	Relaxation

Assuming the proposed and welcome amendments by the European Parliament are accepted by the European Commission and European Council as the draft Directive makes its way through the EU legislative machinery, please note that businesses are still going to have to assess their structures against the gateway tests and document their analysis, so this adds another compliance and governance process to be built out and implemented.

We will keep you posted as and when further developments happen in relation to ATAD 3, but if you have any queries in the meantime, please do reach out to your PwC contact or to Rob Mellor and Dan Jones, whose contact details are below.

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