Austria and Ireland may face EU challenge over ATAD

Businesses in Austria and Ireland enter 2020 with uncertainty on corporate borrowing because both countries will likely miss the January 27 deadline to introduce interest limitation rules.

The European Commission (EC) has said the Austrian and Irish domestic tax rules on interest limitations are not as effective as Article 4 of EU Anti-Tax Avoidance Directive (ATAD 1). Article 4 states that countries need to implement an earnings-based interest limitation clause to allow tax deductible interest of just up to 30% of earnings before interest, tax, and amortisation (EBITDA). In its November 2019 reasoned opinion, the EC said the two countries must implement the interest barrier rules by January 27.

One Austria-based head of tax at a banking association told *ITR*: "It is not clear which options under the interest limitation rules set out in the ATAD will be adopted by Austria. So far nothing has been communicated."

Tax professionals do not expect any action to be taken in Austria or Ireland before the January 27 deadline because of political delays. For instance, Austria was left without a parliament-backed government at the end of 2019.

"Due to the still on-going coalition negotiations after the early general election in fall 2019, any reaction on recent actions taken by the EU Commission will take some time," explained Kornelia Wittmann, tax partner at bpv Hügel in Austria.

"The Austrian and Irish tax administrations were quite confident that the regimes should be considered similar to the French regime, which the EC accepted as being equally effective and allowed France to rely on the grandfathering regime," added Kornelia. Countries relying on the grandfathering regime have until January 2024 to implement changes.

The introduction of an EC appropriate interest barrier moves multinational groups from principle-based approaches under the arms-length principle to more mechanical-based approaches, which could put pressure on a corporate group's leveraging and borrowing operations.

The interest barrier limits a group's leveraging operations across a variety of subsidiaries, especially those in Ireland with larger operations than in Austria. Tax professionals said that this can hit large multinationals with complex group structures harder because they take longer to react.

"Big corporates were expecting that they would have more time to comply," said one Ireland-based tax director at a digital company. "The general market expectation was that any reaction by the Commission would take longer," he added.

While an earnings based interest limitation clause has a *de minimus* threshold of 30%, the multi-layered, mechanical ATAD rules on interest deductibility leave multinational groups with complex structures that are slow to react to any domestic changes. Countries implementing Article 4 of the ATAD domestically have the option to offer a group equity escape, allowing taxpayers to deduct borrowing costs exceeding the 30% threshold, which may help large multinational groups.

However, there is no clarity on whether the group equity escape option will be adopted by either Austria or Ireland. Other EU-based taxpayers with the option have so far faced difficulties in utilising the clause.

"Our experience with group equity escape is that it is not widely used because it is relatively complex and has some obstacles, especially for companies that have more complex international structures," said Bernd-Peter Bier, head of group finance at Bayer.

Large corporates know that Ireland and Austria will have to introduce the interest barrier, but did not realise the timeline would be sooner rather than later.

"Our clients know how the interest barrier rules will work in general and this gives them a chance to see if they have any issues with these rules given their corporate structure," said Nicolas Wolski, tax partner at bpv Hügel.

"The German interest barrier regime was used as a model for the interest barrier set out in Article 4 in the ATAD. Given Austria's strong economic link to Germany it is feasible that Austria mirrors the German rules, especially given a tight deadline from the EU Commission," added Wolski.

As taxpayers continue to analyse their structural challenges ahead of the introduction of interest barrier rules in Ireland and Austria, there are fears of long-term uncertainty because of pressing political concerns. There are limited expectations for any changes being implemented ahead of the January 27 deadline, which means the issue could lead to the EC filing a case before the EU General Court as the next step in the EC infringement process.