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The EU listing act & tax discrimination of equity

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What is the Capital Markets Union about?

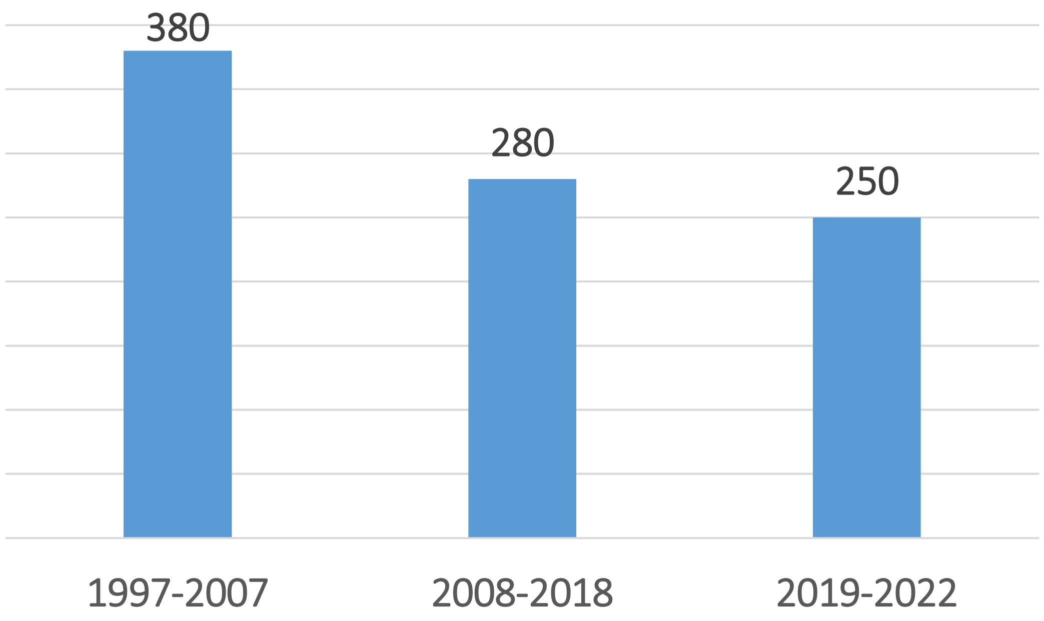
Fostering green transition and digital transformation

“The CMU is the EU’s plan to create a truly single market for capital across the EU. It aims to get investment and savings flowing across all Member States, benefitting citizens, investors and companies, regardless of where they are located. A fully functioning and integrated market for capital will allow the EU’s economy to grow in a sustainable way and be more competitive. An economically stronger Europe will better serve its citizens and help the EU play a stronger role on the global stage.”

Why does Europe needs a Capital Markets Union?

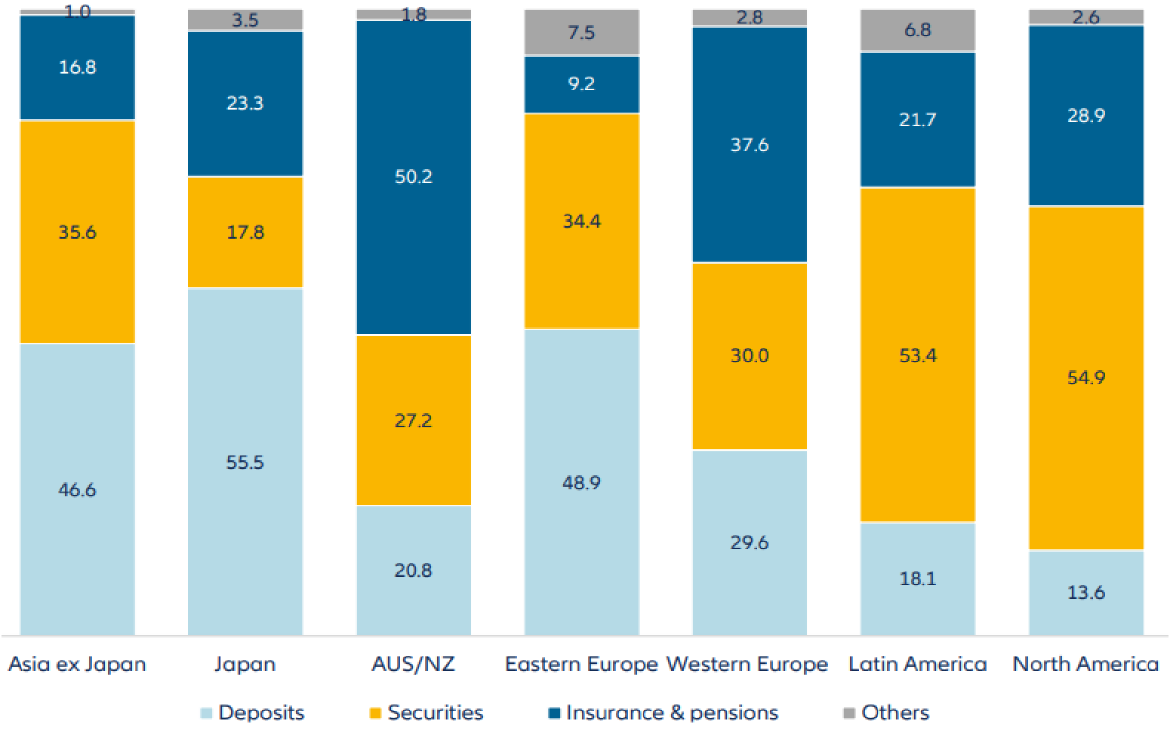
Potential of capital markets for companies and investors is not exploited – so far

Number of European IPOs p.a. decreases



Source: European IPO Report 2020, FESE

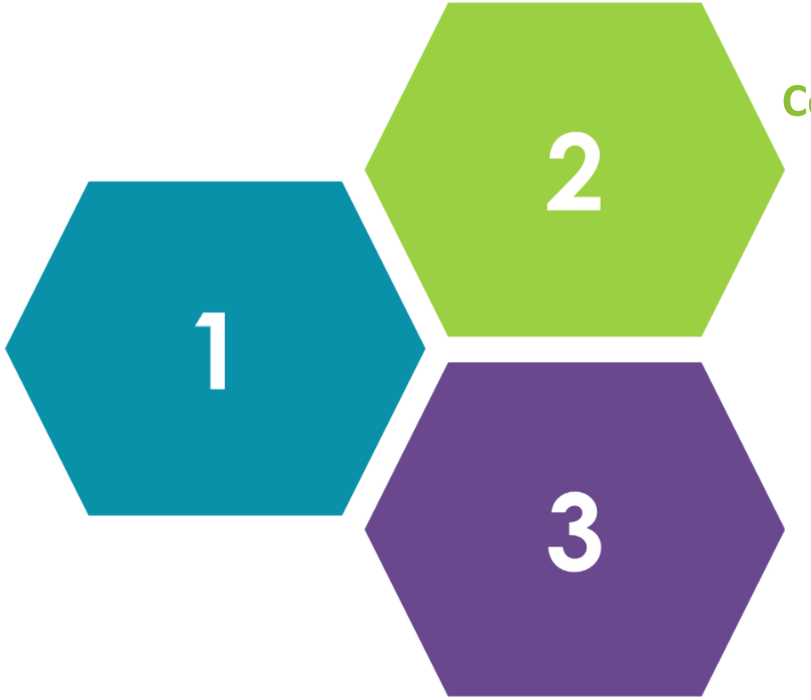
Retail investor participation: Equity – or not?



Source: Allianz Research (2022), asset classes in % of total gross financial assets

What has to be done?

Measures which needs to be taken



Market regulation that protects investors without overburdening companies (EU Listing Act I: Research, Market Abuse, Prospectus)

Corporate law, that meets the needs of growth companies (EU Listing Act II: Multiple-Vote Share Structures)

Equity/investment culture among (retail) investors in Europe (Debt-Equity Bias Reduction)

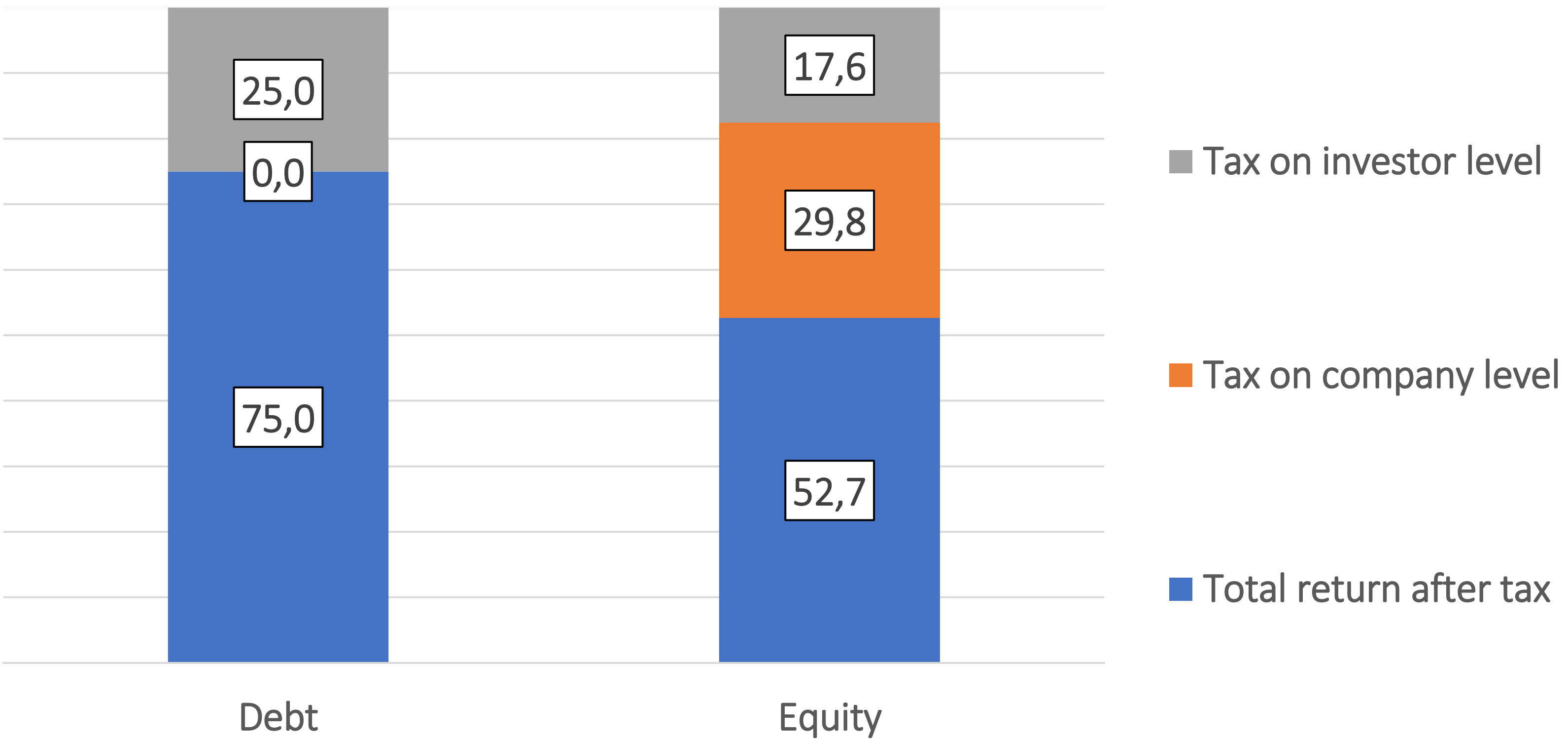
EU Listing Act: Key issues

Make capital markets in Europe more attractive again

- Research: Re-bundling of trading execution fees and research fees would be possible for companies with a market capitalization up to EUR 10 billion.
- Multiple-Vote Share Structures
    - Over-come the fear of company founders to lose control after the IPO
    - So far, no common EU rules regarding multiple-vote are in place
        - Allowed e.g. in Sweden, Netherlands, UK (since 2021 in the „Premium Listing Regime“)
        - Not allowed e.g. in Germany, Austria, Portugal
    - Commission‘s proposal on multiple-vote shares: Minimum harmonisation
        - Adoption of multiple-vote share structures for companies seeking a listing on a SME Growth Markets
        - Safeguards: Sunset Clauses?

Debt-Equity Bias: Example Germany

Tax on debt amounts up to 25 percent, on equity nearly 50 percent



Discrimination of Equity: Consequences

What could be possible solutions of the problem?

- Corporates: Incentives for debt financing
  - The leverage ratio of non-financial companies in the EU is about 30 percentage points higher than that in the US. This means that US companies have a higher risk buffer.
  - Shares and venture capital = more IPOs = more financing of innovation
- Investors: Tax framework for equity/share ownership is unattractive
- Possible solutions
  - Relief at company level (debt-equity bias reduction allowance - DEBRA)
  - Relief at investor level (investment savings account)

DEBRA: Proposal to solve the debt-equity bias problem

Treatment of tax issues on European level is difficult due to national specifics

- EU Commission proposal for a debt-equity bias reduction allowance from 11 May 2022
- Tax allowance on capital increases (per year)
- Like interest expenses, a fictional equity "interest“ expense is allowed to be deducted
- Fictional interest rate on equity is calculated as risk-free interest…
    - …plus a premium of 1 percent for larger companies
    - …plus a premium of 1.5 percent for SMEs
- Drawback, which is crucial: Limitation of the deductibility of interest expenses to 85 percent

Investment saving account: Fair taxation at investor level

EU Commission discusses investment saving accounts within the Capital Markets Union

What are investment saving accounts? Some key features

- Tax incentiviced savings in equity and other capital market instruments like funds, bonds etc.
- Tax exemption/lower tax rate (up to a maximum yearly or total limit)
- Deferred taxation/tax decuction
- Withdrawals of funds are possible at any time/are restricted

European landscape of investment saving accounts

So far, investment saving accounts are offered in 11 EU Member States

Examples

- France (Plan d'Epargne en Actions, 1992): Up to EUR 150,000 in shares or funds (illiquid instruments of SMEs: EUR 225,000), tax-free after 5 years
- UK (Individual Saving Accounts, 1991): Up to 20,000 £ annually in securities (shares, funds, bonds), without any mandatory holding period
- Italy (PIR, 2017): Up to EUR 200,000 in securities, especially from Italian issuers (max. EUR 40,000 annually; SMEs: EUR 300,000 or EUR 1.5 million), tax-free after 5 years
- Sweden (Investeringssparkonto, 2012): Investment in financial instruments admitted to a regulated market and MTF, as well as units of fund with no maximum limit. No tax exemption, but flat-rate income taxation calculated by a risk-free interest rate

Investment savings accounts are a success story in UK and Sweden

Some figures

UK (2019/2020)

- 20 million savers
- £ 620 billion (on average £31,000 per saver), of which around 50 per cent in shares/funds/bonds
- Nearly half of savers invest up to £ 2,499 per year

Sweden

- Every fifth person in Sweden has an investment savings account (2016)
- Volume: SEK 576 billion (EUR 50 billion), of which 90 percent are invested in equity or mixed funds (2023)
- As the volume in Swedish investment savings accounts grew, so did the number of Swedish IPOs, especially in the SME segment (2014-2016)

Unleash the forces of capital markets in Europe

Recommandations for action

EU legislator

- Find the right regulation balance between transparency needs of investors and cost-burden for companies
- Push Member States to offer incentives for share or capital market instruments investments

National legislator

- Mobilise domestic capital in order to (also) provide financing for growth companies
- Overcome the debt-equity bias by introducing investment saving account
- Other measures with great impact: More shares in the pension system, employee share ownership etc.