

TAXATION WHITE PAPER

Taxation in Europe

Investors' perspective on getting it right

Executive summary

The EU's investment gap

Europe faces a persistent competitiveness and investment gap driven by regulatory fragmentation, tax uncertainty, and the absence of a coherent cross border framework for private capital. As recently stated by the Directorate-General for Budgetary Affairs of EU Parliament, *'closing it requires action on both public and private financing fronts: public finance can provide strategic direction and risk-sharing, but around 80 per cent of the required investment must ultimately come from private capital. [...] Together, these public and private gaps undermine Europe's ability to mobilise the investment required to meet its decarbonisation, digital and defence objectives. Addressing only one side of the equation will be insufficient; public financing reforms can strengthen the foundation, but the overall investment gap cannot be closed without overcoming the structural weaknesses that impede private capital formation'* (see, *Financing competitiveness in the EU One year on from the Draghi Report*, January 2026, hereinafter the "Report")¹.

The role of private equity industry

In this respect, private equity and venture capital are essential to Europe's industrial transformation - powering innovation, scale up financing, technological transition and long term value creation - but current tax barriers significantly hinder their effectiveness. Invest Europe's White Paper on tax harmonisation for EU investments and investors prepared by members of Invest Europe's Tax Innovation Working Group positions **long-term private investment as a European public good of systemic relevance** and calls for a modernised, harmonised, future proof tax environment that unlocks the full potential of private capital across the EU.

The core problem: fragmented tax systems suppress investment

The Report highlights how *'the persistent fragmentation of EU capital markets prevents the efficient allocation of capital across borders. The lack of a single securities supervisor, the absence of a fully unified rulebook, and divergent post-trade infrastructures hinder the emergence of a truly integrated financial market. In addition, disparities in insolvency and tax regimes continue to discourage cross-border investment'*.

With respect to tax matters, investors across the EU face inconsistent tax rules, divergent administrative practices, and unpredictable cross border outcomes, creating legal uncertainty, double taxation risks, and high compliance burdens.

These issues affect all dimensions of the investment cycle - from structuring to management of the investment, to exit of the investors. Fragmentation reduces the EU's ability to compete globally, steering companies and capital toward more predictable jurisdictions.

Vision: a cohesive EU tax architecture rooted in neutrality and legal certainty

The White Paper does not intend to seek preferential tax treatment, regulatory relief or financial incentives for the private equity sector, but proposes an integrated framework aimed at removing fiscal barriers that hinder cross-border investment within the EU based on four principles:

- **Harmonisation:** This principle aims at aligning core tax concepts to reduce distortions, hybrid mismatches, and administrative duplication;
- **Neutrality:** It ensures tax rules do not drive investment decisions or vehicle selection;
- **Legal Certainty:** It provides predictable treatment across Member States, essential for cross border capital flows;
- **Cooperation:** This principle's goal is strengthening coordination between EU tax authorities and align EU rules with OECD standards.

This model preserves Member States' sovereignty while enabling a more functional single market.

Structural priorities across the investment cycle

In the structuring phase key obstacles include inconsistent residence definitions, PE risk from management/advisory activity, divergent beneficial owner rules, opaque classifications under PSD / I&R Directives and tax treaties, mismatches for partnerships and disparities in the tax treatment of debt and equity.

Against this background the White Paper calls for:

- residence based strictly on place of establishment;
- an EU Investment Management Exemption (IME) to prevent unintended PEs;
- automatic beneficial owner recognition for regulated EU funds;
- extension of PSD and I&R Directive and tax treaties benefits to funds;
- harmonised classification of limited partnerships;
- equality of equity contributions compared to third-party financing.

Building on these structural solutions in the structuring phase, the White Paper further emphasizes the importance of streamlining cross-border administrative processes and facilitating efficient fund passporting to reduce friction for investors and fund managers. It advocates for the adoption of common reporting standards and integrated digital platforms, enabling seamless information exchange and compliance monitoring across Member States. Such measures are intended to support a more predictable and transparent tax environment, bolstering investor confidence and reinforcing the EU's position as an attractive destination for capital.

As the investment cycle advances to the management phase, attention turns to the operational complexities and risks that arise, including transfer pricing challenges, VAT inconsistencies, and the evolving tax treatment of carried interest, all of which the White Paper addresses with targeted policy recommendations designed to foster consistency and legal certainty throughout the EU investment landscape.

To address challenges arising during the management phase, the White Paper calls for following solutions:

- applying IME to MC/AC structures;
- adopting the EU Transfer Pricing Directive or TP Platform;
- harmonizing VAT definitions for fund management;
- allowing optional VAT taxation to remedy input VAT leakage.

In addition, the White Paper underscores the necessity of clear guidance and consistent application of tax rules to minimise uncertainty for fund managers operating across multiple jurisdictions. Enhancing cooperation among tax authorities and fostering an environment of mutual trust are highlighted as key factors in ensuring smooth cross-border fund operations. These initiatives aim to further align regulatory and operational frameworks, ultimately contributing to a more unified and competitive European investment market.

The following point of attention is the treatment of carried interest, which suffers inconsistent tax classification and timing rules across Member States, discouraged by digitalisation driven ambiguity. White Paper's recommendation includes an EU wide regime treating carried interest as capital income, based on risk alignment, holding periods, and subordinated waterfalls.

To complement these measures, the White Paper also addresses the mischaracterisation of SPVs as shell companies, which frequently results in the loss of directive or treaty benefits and creates challenges for VAT recovery. By proposing a safe harbour that specifically excludes fund-owned SPVs from *shell* definitions and advocating for the VAT recognition of acquisition-related activities, the aim is to safeguard legitimate investment structures and facilitate more predictable tax outcomes for cross-border funds. This approach dovetails with broader recommendations to mitigate debt-equity bias, streamline equity repayment, and establish neutral regulatory standards for digital financial instruments, all geared toward fostering an efficient, transparent and competitive investment environment throughout the EU.

Furthermore, the White Paper draws attention to the ongoing need for rationalising administrative obligations by advocating targeted reforms to DAC6, proposing clearer and harmonised definitions, streamlined procedures for routine fund transactions, robust safeguards for legal professional privilege, and standardized penalty frameworks across Member States. These steps are intended to alleviate unnecessary compliance costs and regulatory uncertainty, thereby enabling fund managers to focus resources on value-creating activities and support a competitive cross-border investment environment.

Building on these efforts to foster administrative efficiency, the discussion turns to the persistent challenges of double taxation during the exit phase and the imperative of achieving full tax neutrality for funds and SPVs, as well as adapting the tax framework to technological advancements and a forward-looking European investment strategy.

Technology as a structural catalyst

Building on the imperative for technology-neutral tax frameworks, the White Paper emphasises that embracing digital transformation is critical for ensuring the European investment landscape remains agile and future-proof. As the market pivots toward novel structures and digital assets, regulatory and tax policies must evolve in tandem to facilitate seamless cross-border investment activity, reduce administrative burden, and foster innovation. By modernising the tax treatment of dematerialised assets and decentralised entities, the EU can address the unique challenges posed by rapidly advancing technologies, while enhancing industrial competitiveness and unlocking greater flows of private capital to strategic priorities such as the green and digital transitions. This forward-looking approach ensures that taxation keeps pace with the realities of the digital economy, supporting a resilient and attractive environment for long-term investment across the Union.

A forward looking European strategy

By prioritising pragmatic convergence over sweeping uniformity, the White Paper recognises the value of flexible, responsive tax frameworks that accommodate diverse national systems while eliminating the most disruptive barriers to cross-border investment. It urges policymakers to focus on harmonising key definitions, reporting standards, and procedural rules, thus promoting predictability for investors without stifling Member State innovation. This nuanced approach aims to strike a balance between regulatory certainty and fiscal sovereignty, enabling Europe to attract and nurture high-potential enterprises, accelerate capital market integration, and advance strategic goals in sustainability and technological leadership. In doing so, the White Paper sets a clear agenda for future reforms that empower the European investment ecosystem to thrive amid global competition and ongoing transformation.

In summary, the White Paper calls for a **holistic EU investment tax model** that:

- treats long term investment as a *public good*;
- modernises outdated tax concepts;
- reduces fragmentation;
- enhances EU industrial competitiveness;
- unlocks private capital for green, digital, and innovation priorities.

This is not a call for full harmonisation, but for **targeted, pragmatic alignment** that removes the most damaging frictions undermining Europe's competitiveness and ability to retain and scale high growth companies.

1. The Draghi Report highlights that closing Europe's investment gap—estimated at EUR 750-800 billion per year, or around 4.4-4.7 per cent of EU GDP—will require a dual effort. Historically, approximately four-fifths of investment across the Union has been financed privately, with only one-fifth funded through public sources. This distribution implies that the EU must address two sets of obstacles: those stemming from the EU's public financing architecture, and those that hinder the mobilisation of private capital at scale. Both dimensions are essential, and neither can compensate for the other.