ATOZ ALERT

The Council reached an agreement (general approach) on new rules for withholding tax procedures (FASTER)

21 May 2024

Introduction

On 14 May 2024, the European and Financial Affairs Council ("**ECOFIN**") met to discuss the proposal for a Council Directive on Faster and Safer Relief of Excess Withholding Taxes (hereafter "**FASTER**" or "**the Proposal**") through a compromise text which presents substantial differences compared to the original text of the proposal published in June 2023. The Council reached an agreement (general approach) on the compromise text providing for new rules for withholding tax ("**WHT**") procedures.

FASTER aims at creating:

- A common EU digital tax residence certificate; and
- A standardised WHT relief procedure implying:
  - ✓ Standardised reporting obligations for financial intermediaries to provide national tax administrations with the necessary tools to check eligibility for the reduced rate and to detect potential abuse; and
  - ✓ A two fast-track procedure, assorted with new due diligence obligations, complementing the existing standard refund procedure to relieve excess WHT withheld by a Member State on dividend or interest income paid on publicly traded shares or bonds to non-resident investors.

With this initiative, the Commission aims to tackle the current particularly burdensome WHT refund procedures - which differ amongst Member States - for cross-border investors in the EU and, at the same time, the risks of tax abuse related to refund procedures revealed notably by the Cum/Ex and Cum/Cum scandals.

We describe hereafter the implications of the Proposal.

EU digital tax residence certificate

Member States will be required to issue an EU digital tax residence certificate within one working day from the submission of a request. The certificate will notably be used by investors, as adequate proof of residence, to reclaim WHT refunds and will replace the paper-based procedures currently applicable.

According to FASTER, a common EU digital tax residence certificate ("**eTRC**") is to be introduced by all Member States mainly in order to streamline WHT procedures. It will identify the recipient of a payment subject to WHT (dividend or interest) and confirm its tax residency according to the relevant Member State's national rules. Tax paying investors would be able to use this eTRC in order to benefit from the fast-track procedures set up by the Proposal to obtain relief from withholding taxes.

Based on the information known by the issuing authority on the date of issuance, Member States will be required to issue eTRCs to natural persons and entities deemed resident for tax purposes in their jurisdiction within, in principle, fourteen calendar days from the submission of a request. To meet this requirement, a fully automated system to issue the eTRC should be implemented by the Member States.

According to the Proposal, Member States shall recognise the eTRC as adequate proof of residence of the recipient of an income in another Member State. In order for the eTRC to be recognised by the source Member State as valid proof of residence, when the relief of WHT is claimed under the provisions of a double tax treaty, it is, however, essential that the applicable double tax treaty(ies) is(/are) mentioned on the eTRC.

An eTRC shall: (a) cover a period not exceeding the calendar year or the period of a fiscal year for which it is issued, as applicable in the issuing Member State; and (b) be valid for certifying the residence of such covered period unless the Member State issuing the eTRC has evidence that the relevant person is not resident for tax purposes in its jurisdiction for the entire period and the Member State therefore completely or partially invalidates the eTRC. The eTRC is intended to be issued once during the calendar year or once during the fiscal year.

Withholding tax relief procedures

The WHT relief procedures under FASTER are only relevant for Member States that apply WHT on cash or stock dividends at different rates depending on the specific investor's tax residence and Member States that do not have a comprehensive relief at source system and have a market capitalisation ratio equal or above 1.5%.

The Proposal aims at introducing more efficient (and harmonised) procedures across the EU concerning cross-border cases of relief from withholding taxes that Member States levy on income from publicly traded securities. However, Member States that provide relief of excess WHT on interest paid on publicly traded bonds issued by a resident in their jurisdiction may also apply FASTER.

The provisions of the Proposal described in this section in relation to the FASTER WHT relief procedures should thus be relevant only in the Member States that apply WHT on cash or stock dividends at different rates depending on the specific investor's tax residence. Member States that do not need relief procedures in relation to excess withholding taxes on dividends and interest, as the case may be, are not concerned by the procedures referred to in this section.

Similarly, the provisions of the Proposal related to the WHT relief procedures should not be binding to the Member States that have a comprehensive relief at source system and a market capitalisation ratio below 1.5% for each of the four consecutive years, as set out in the four latest publications by the European Securities and Markets Authority ("**ESMA**"). The market capitalisation ratio threshold is applied because Member States with smaller capital markets are considered as often having a lower number of requests for WHT relief. These Member States may, however, also apply these provisions.

In order to be considered as comprehensive, the national relief at source system should contain a number of specific key features similar to the FASTER WHT relief procedures and, with regards to the condition of the market capitalisation ratio, ESMA should provide the required data according to regulatory technical standards. The 'market capitalisation ratio' means the ratio expressed as a percentage of the market capitalisation of a Member State on 31 December to the overall market capitalisation of the European Union on 31 December in a given year.

According to a note prepared in anticipation to the ECOFIN meeting of 14 May 2024, only ten Member States have a market capitalisation ratio above 1.5% and the Luxembourg ratio is currently set as 0.61%. In case the Luxembourg relief at source system is considered as comprehensive, Luxembourg would thus not have to mandatorily apply the FASTER WHT relief procedures described in the Proposal.

Nevertheless, once a Member State no longer fulfils at least one of the two conditions (concerning the comprehensive relief at source system and the market capitalisation ratio threshold), it must transpose into national legislation and irrevocably apply the FASTER WHT relief procedures.

NATIONAL REGISTERS

National registers of certified financial intermediaries which are large institutions that handle payments of dividends from publicly traded shares (and bonds), as well as central securities depositories that provide WHT agent services for the same payments, will have to be established by Member States.

Member States will have to establish a national register ("**National Register**") of Certified Financial Intermediaries ("**CFI**"). All large institutions that handle payments of dividends under the relevant EU regulations and, where relevant, interest on securities issued by a resident in their jurisdiction, as well as central securities depositories that are WHT agents for such payments, will have to register with their National Register. Financial intermediaries that are not under the obligation to register as CFIs can still opt to be registered as such. National Registers shall be made publicly accessible on a dedicated portal via a website of the EU Commission.

Registration should be requested by the financial intermediary itself by submitting an application through the European Certified Financial Intermediary Portal that should serve as a single entry point. These applications should then be forwarded to the relevant Member States.

Financial intermediaries that do not comply with registration requirements may be subject to penalties. In addition, only Registered Owners (as defined below) engaged with financial intermediaries that are certified to provide these services will benefit from the systems of relief described in the Proposal.

OBLIGATIONS OF CFIS

The Proposal also aims at tracing payment flows until the final investors through the chain of financial intermediaries, and therefore defines certain reporting and due diligence obligations regarding Registered Owners. "Registered Owner" means any natural person or entity that is entitled to receive dividend or interest income from listed securities subject to WHT in a Member State, as the holder of the securities on the record date, and that is not a financial intermediary acting for the account of others with respect to the dividend or interest income. Member States may also consider, in accordance with their national legislation, the holder of depositary receipts as the Registered Owner, instead of the holder of the underlying securities, as if this holder had directly invested in such securities.

- **Standardised reporting obligation of CFIs**

Through the standardised reporting obligation of CFIs, tax authorities will receive, within specific timelines, a relevant set of information allowing them to assess the eligibility of Registered Owners applying for a reduced WHT rate and to trace potential tax abuse situations.

CFIs will have to report a relevant common set of information laid down in Annex II of the Proposal to the competent authority, within the second month following the month of the payment date. This information provides national tax administrations with the necessary tools to check eligibility for a potential reduced rate of WHT and to detect potential abuse. The reported data should include information on the eligibility of the investor concerned but should be limited to the information that is available to the reporting CFI.

Two reporting options should be provided: direct and indirect reporting. Where the reporting is direct, a CFI should report directly to the competent authority of the source Member State. Where the reporting is indirect, the information should be provided by the CFIs along the securities payment chain in a sequential order, and in respect of the position of the CFIs in the securities payment chain in which they are part of. The outcome should be that this information reaches the WHT agent or a designated CFI, who ultimately reports the information to the competent authority of the source Member State.
Financial intermediaries that are not under an obligation to register as CFIs and have not opted to register as such do not have reporting obligations under this Proposal. Nevertheless, information on the payments handled by such intermediaries that are not CFIs remains relevant and may be considered necessary by a Member State, at its discretion. To ensure there are no information gaps in the payment chain and to enable investors to access the relief procedures, the Proposal should allow a CFI, who may not be directly involved in a specific payment chain, to step into the role of another financial intermediary within the chain that is not a CFI.

A CFI should also be permitted to rely on a third party to fulfil the relevant obligations on WHT procedures. In any case, these obligations should remain under the responsibility of the CFI that outsourced their responsibilities.
CFIs that do not comply with registration requirements may be subject to penalties.

- **Request of systems of relief by CFIs**

Complementing the existing standard refund procedure, two fast-track procedures, assorted with conditions and new due diligence obligations, will make the relief process faster and more harmonised across the EU. Member States will be able to choose which one to use – including a combination of both.

This Proposal harmonises the access to systems of relief for investors in all Member States by providing a regulation on the relief at source system and the quick refund system, still leaving the possibility for Member States to maintain their national regulation of relief at source systems, under certain conditions and taking into account the differences in development of Member States' economies, while ensuring the access to systems of relief in Member States.

The Proposal allows Member States to choose between (or to combine) two fast-track procedures complementing the existing standard refund procedure: a relief at source system (Option 1) and/or a quick refund system (Option 2).

No matter the option chosen, a CFI maintaining the investment account of a Registered Owner will request the benefit of the system of relief, on behalf of such Registered Owner, if:

- the Registered Owner has authorised the CFI to request relief on its behalf; and
- the CFI has performed due diligence duties to verify and establish the Registered Owner's eligibility to the system of relief. Such verification may also include a risk assessment that considers the credit risk and fraud risk.

Due diligence obligations

When requesting tax relief at source or a quick refund on behalf of Registered Owners, CFIs will have to verify that the Registered Owners are eligible for the reduced WHT rate and the absence of certain financial arrangements linked to the securities which could create a risk of Cum/Cum or Cum/eEx scheme.

According to the Proposal, when requesting tax reliefs on behalf of Registered Owners, CFIs will have to put in place adequate procedures to ensure the Registered Owners are eligible for such reliefs.

CFIs will need to collect certain information from Registered Owners, including a declaration that the registered owner:

- is the one entitled to the relief of the WHT with respect to the dividend or interest in accordance with the national legislation of the source Member State or a double tax treaty, where applicable, including the legal basis and the applicable WHT rate; and
- is the beneficial owner, when required by the source Member State, with respect to the dividend or interest in accordance with the national legislation of the source Member State or a double tax treaty, where applicable; and
- has engaged or not in a financial arrangement linked to the underlying publicly traded share that has not been settled, expired or otherwise terminated before the ex-dividend date; and
- undertakes to inform the CFI of any change in their circumstances without undue delay.

One particularly interesting aspect of the Proposal is that CFIs will also have to verify, in principle on an annual basis:

- the eTRC of the Registered Owner or a proof of tax residence in a third country deemed appropriate by the source Member State;
- the documentation deemed appropriate by the source Member State, in cases where a Registered Owner is an entity for which an eTRC cannot be issued or that cannot obtain a proof of tax residence in a third country because it is disregarded for tax purposes and its income (or part thereof) is taxed at the level of the persons who have an interest in the entity, but it is entitled to the relief of the WHT with respect to the dividend or interest in accordance with the national legislation of the source Member State or a double tax treaty, where applicable;
- the Registered Owner's declaration and tax residence, against the information that the CFI has obtained or has an obligation to obtain;
- the Registered Owner's entitlement to a specific reduced WHT rate in accordance with a double tax treaty;
- in case of a dividend payment, the possible existence of any financial arrangement that has not been settled, expired or otherwise terminated at the ex-dividend date;
- in case of a dividend payment, that the underlying share has been acquired by the Registered Owner in a transaction carried out earlier or within a period of five days before the ex-dividend date.

In this context, this obligation should be understood in the sense that the closest CFI to the investor (i.e. its client) should take reasonable measures to perform such checks in good faith.

According to the Proposal, such verification should be made by CFIs based on the information available to them. This means that CFIs should check whether the information in the eTRC or its equivalent, or the information in the investor's declaration, contradicts the information collected by the CFIs on their clients in their normal course of business (such as the investor's account information and other information that they may have collected applying KYC rules). Consequently, also according to the Proposal, CFIs should not be required to perform further examinations or to request and collect further information from their customers. However, it is difficult to imagine how a CFI can verify the Registered Owner's entitlement to a specific reduced WHT rate in accordance with a double tax treaty without carrying out an analysis for that purpose, especially taking into account the financial responsibility of CFIs established by the Proposal.

Indeed, according to the Proposal, CFIs can be held liable for full or part of WHT revenue loss incurred due to their full or partial non-compliance with the key obligations of the Proposal. Member States may thus establish in their national legislation several strict and joint liabilities for CFIs requesting the relief.

Option 1: Relief at source system

Under this option, CFIs maintaining a Registered Owner's investment account will be required to request relief at source on behalf of such Registered Owner by providing the WHT agent with the tax residence of the Registered Owner and the applicable WHT rate on the payment in accordance with a double tax treaty or specific national legislation.

Under this option, the correct amount of taxes is applied at the time of the dividend or interest payment directly without any further action required. CFIs are supposed to have verified the eligibility for a reduced WHT rate in advance.

Option 2: Quick refund system

Under this option, CFIs maintaining a Registered Owner's investment account will be required to request a quick refund of the excess WHT on behalf of such Registered Owner, if some information is provided by the CFIs within the second month following the month of the payment date of the dividend or interest.

In such situation, the initial payment is made considering the WHT rate of the source Member State, but the refund for any overpaid taxes is made within 60 calendar days after the end of the period to request the quick refund. Member States shall apply interest on the amount of such refund for each day of delay after the 60th day. Under certain conditions, Member States may reject a refund request.

Special provisions for indirect investments

When the Registered Owner is a collective investment undertaking or a designated legal person within the fund regulations, instruments of incorporation or prospectus of a collective investment undertaking that holds securities in an investment account and maintains internal records enabling the individual allocation of these securities to the collective investment undertaking or to the investors in the collective investment undertaking as applicable, Member States shall allow a CFI maintaining the investment account of such Registered Owner to request a relief at source or a quick refund on behalf of the Registered Owner, provided that some requirements have been met.

NON-APPLICATION OR LIMITATIONS TO THE APPLICATION OF THE SYSTEMS OF RELIEF

Each Member State is allowed to limit the benefit of the systems of relief to low-risk taxpayers and exclude the benefit of such systems to specific situations.

Each Member State needs to ensure that at least one of the two systems is available to all investors when the conditions set out by the Proposal are met. Nevertheless, within these two systems, Member States have the discretion, for instance, to only allow low risk taxpayers to request relief at source whilst other taxpayers can only request a quick refund.

For this purpose, the Proposal foresees a non-mandatory list of cases where Member States have a possibility to exclude requests for relief and conduct further checks. Member States have the discretion to determine which of such cases should be covered by the standard refund procedure.

As a result, Member States may completely or partially exclude requests for relief under the Proposal where:

- at least one of the financial intermediaries in the securities payment chain is not a CFI and no CFI has assumed the position of the financial intermediary;
- an exemption of the WHT is claimed;
- a reduced WHT rate not deriving from double tax treaties is claimed;
- the dividend has been paid on a publicly traded share that the Registered Owner acquired within a period of five days before the ex-dividend date;
- the dividend payment exceeds a gross amount of at least 100,000 EUR, per Registered Owner and per payment date. This amount shall be determined by the gross dividend amount per investor holding equity in a collective investment undertaking when this underlying investor is entitled to the relief pursuant to the Proposal;
    - This 100,000 EUR threshold should not apply when a concerned collective investment undertaking established and regulated in the EU (UCITS, AIFs or AIFMs), a statutory pension scheme of a Member State or an institution for occupational retirement provision registered or authorised in a Member State in accordance with Article 9(1) of Directive (EU) 2016/2341 is

entitled to the relief because these undertakings, schemes and institutions are highly regulated and subject to supervision by the national competent authorities and robust internal controls.

- the dividend payment on the underlying security for which relief is requested is linked to a financial arrangement that has not been settled, expired or otherwise terminated before the ex-dividend date.
    - Arrangements such as future contracts, repurchase transactions, securities lending and securities borrowing, buy-sell back transactions or sell-buy back transactions, derivatives, margin lending transactions and contracts for difference ("CFDs") may be considered as financial arrangements if they imply a temporarily or permanent split between the natural person or entity bearing the economic risks of the investment and the legal owner of the share or underlying rights. These examples are not exhaustive.
    - Any arrangement under which the dividend is compensated between the parties concerned may be considered as a financial arrangement.

Where the relief at source and quick refund systems set out in the Proposal do not apply, the standard refund procedure will apply, where the taxpayer or its appointed representative, which does not necessarily have to be a financial institution, is able to directly request a refund to the tax authority.

Implications

The Proposal should simplify WHT relief procedures but creates new heavy reporting and due diligence duties for CFIs with a potentially high degree of liability.

We welcome the Proposal since it has the potential to simplify WHT relief procedures and to improve WHT procedures for non-resident investors to the extent it should facilitate cross-border investments within the EU.

We especially welcome the introduction of the eTRC, its board scope of application and the short deadline in which tax authorities will have to provide it.

Nevertheless, this Proposal creates new heavy reporting and due diligence duties for CFIs with a potentially high degree of liability. At this stage we can, however, already note that, as the systems of relief apply only at the request of the recipient of the dividend (or interest) payment and as the due diligence duties must be performed when the systems of relief are requested, if the recipient of the dividend (or interest) payment does not authorise the CFI to request a relief on its behalf, such CFI does not have to perform due diligence duties to verify and establish the recipient's eligibility.

The Proposal guarantees that all investors can benefit from at least one of the two standardised systems, as long as they meet the conditions set out in the Proposal. As a consequence, if a CFI concludes that investors do not meet the eligibility conditions, it should be allowed to refuse to request the benefit of a system of relief on behalf of a Registered Owner. However, it is still not clear at this stage whether CFIs could refuse, for any other reasons, to apply the systems of relief, notably when the verification required is not possible or just because their liability could be engaged. In the latter case, the CFI could also be exempted from the due diligence duties to verify and establish the recipient's eligibility.

In any case, notwithstanding the fact that CFIs must perform due diligence verifications to request the benefit of the relief at source system or the quick refund system on behalf of the Registered Owner of a security, it appears nowhere that the due diligence conclusions of the CFIs on the non-eligibility of a Registered Owner for a reduced WHT rate should be communicated to the tax authorities. In such case, the systems of relief would not be applied and the Registered Owner or its authorised representative could still request a refund of the excess WHT via the standard refund system, under the condition that he provides, if required, at least the information required under Annex II, heading E (i.e. information about the holding period of underlying securities and information about financial arrangements linked to the securities for which the taxpayer is requesting relief) to the competent authorities.

Next steps

The European Parliament was consulted and delivered its opinion on the initial text of the Proposal on 28 February 2024. However, due to the changes the Council made to the Proposal during the negotiations, the European Parliament will be consulted again on the agreed text.

Following this re-consultation with the European Parliament, the Proposal will need to be formally adopted by the Council (unanimity required) before being published in the EU's Official Journal and entering into force. In this respect, the Council is currently expected to adopt the Proposal in early 2025.

Member states will then have to transpose the directive into national legislation by 31 December 2028, but the national rules will, in principle, become applicable only as from 1 January 2030.

We will keep you informed of any further developments in the legislative process.

Do you have further questions?

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