

ATOZ ALERT

European Commission releases FASTER Directive Proposal

21 June 2023

On 19 June 2023, the European Commission published the Proposal for a Council Directive on Faster and Safer Relief of Excess Withholding Taxes (hereafter “**FASTER**” or “the **Proposal**”). With this new initiative, the Commission aims to tackle the current particularly burdensome withholding tax (“**WHT**”) refund procedures - which differ between 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.

This Proposal aims at creating:

- Common EU digital tax residence certificates;
- 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
- Two fast-track procedures, assorted with new due diligence obligations, complementing the existing standard refund procedure to relieve any excess WHT that can be withheld by a Member State on dividend or interest income paid on shares or bonds traded publicly to non-resident investors.

Hereafter, we briefly describe 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 submission of a request. The certificate will notably be used by investors, as adequate proof of residence, to reclaim multiple WHT refunds and will replace the paper-based procedures currently applicable.

A common EU digital tax residence certificate (“**eTRC**”) is to be introduced by all Member States in order to, mainly, 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 rules¹.

¹ The following information shall be included : (a) the first and last name of the taxpayer and the date and place of birth, if the taxpayer is an individual, or its name and its European Unique Identifier number (EUID), if the taxpayer is an entity (b) tax identification number; (c) address of the taxpayer; (d) date of issuance; (e) the covered period; (f) identification of the tax authority issuing the certificate; (g) any additional information that may be relevant where the certificate is issued to serve purposes other than relief of withholding tax under this Directive or information required to be included in a tax residence certificate under EU law.

Provided that no exceptional circumstances occur justifying a delay, Member States will be required to issue an eTRC within one working day from submission of a request. To meet this requirement, a fully automated system to issue the eTRC should be implemented by Member States which allows for requests via an online portal accessible to taxpayers and parties authorised thereby (e.g., financial intermediaries requesting the eTRC on behalf of their clients).

Member States shall recognise the eTRC as adequate proof of residence of the recipient of an income in another Member State.

Member States' 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 Intermediary (“**CFI**”). A CFI is a financial intermediary which meets the requirements of relevant EU regulations and is supervised for compliance therewith.

All large institutions as defined in the Capital Requirements Regulation (i.e., credit institutions and investment firms) that perform custodial activities and, in this context, handle payments of dividends from publicly traded shares originating in their jurisdictions to registered owners who are resident for tax purposes outside that Member State, as well as central securities depositories that provide WHT agent services for the same payments, will have to register, as CFI, with their National Register. However, Member States can also opt to use the National Register in relation to payments of interest from publicly traded bonds. Financial intermediaries that are not under the obligation to register as CFI can still opt to be registered as such.

Financial intermediaries that do not comply with registration requirements may be subject to penalties. In addition, only Registered Owners engaged with financial intermediaries that are certified to provide those 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 or legal person that is entitled to receive dividend or interest income from securities subject to tax withheld at source in a Member State.

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 to the competent authority, within specific timelines, a relevant set of information. For that purpose, the Proposal lays down a common set of reporting elements in [Annex II](#), providing national tax administrations with the necessary tools to check eligibility for the reduced rate and to detect potential abuse.

The reporting will take place via a standardised XML format scheme. The timeline to report the information comprised in Annex II is 25 days² at the latest from the record date, which is the date at which the issuer of a security checks its records to identify securityholders eligible for a dividend or interest payout.

² “As soon as possible after the record date, unless a settlement instruction in respect of any part of a transaction is pending on the record date, in which case the reporting for that transaction shall take place as soon as possible after the settlement. If 20

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 transparency and to allow for the proper reconstruction of the payment chain before applying the relief procedures set out in this Directive (relief at source or quick refund). Therefore, Member States may request that CFIs obtain this information from such non-CFI and report accordingly for the relief procedures laid out in this Directive to be applicable.

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.

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

Taking into account the different approaches in Member States, two types of procedures are envisaged: (i) relief at source by direct application of the appropriate tax rate at the time of withholding and (ii) quick refund within a maximum of 50 days of the date of payment of the dividend or, as the case may be, of the date when the bond issuer must pay interest to the bondholder (coupon date).

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 latter 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 quick refund on behalf of Registered Owners, CFIs will have to verify these Registered Owners are eligible for the reduced WHT rate and the absence of certain financial arrangements linked to the securities, and which could create a risk of Cum/Cum or Cum/Ex 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 these Registered Owners are eligible for such reliefs.

CFIs will need to collect certain information from Registered Owners, including a declaration that they are the beneficial owners of the income received and the absence of certain financial arrangements linked to the securities, and which could create a risk of Cum/Cum or Cum/Ex scheme. One aspect particularly interesting of the Proposal is that CFIs will also have to verify, based on the investor's specific circumstances, (1) the Registered Owner's entitlement to a specific reduced WHT rate in accordance with a double tax treaty between the source Member State and the jurisdictions where the Registered Owner is resident for tax purposes or specific national legislation of the source Member State, and (2) the possible existence – thus not the existence as such but only the potentiality - of any financial arrangement involving the underlying securities that has not been settled, expired or otherwise terminated at the ex-dividend date, unless the dividend paid to the registered owner for each group of identical shares held does not exceed EUR 1000.

days after the record date, settlement is still pending for any part of the transaction, certified financial intermediaries shall report within the next 5 calendar days indicating the part for which settlement is pending".

At this stage, the scope of the verification required is, however, unclear. Should CFIs perform a complete legal and tax analysis of the situation of the Registered Owner, or would a “reasonable” verification be sufficient? Moreover, taking into consideration legal uncertainties around the sole notion of “beneficial owner” for which there is neither a legal definition nor a unanimous and constant case law delineating that notion, on which basis could CFIs verify the entitlement to a specific reduced WHT rate?

Option 1: Relief at source system

Under this option, CFIs maintaining a Registered Owner’s investment account will be allowed (or will be required) to request relief at source on behalf of such Registered Owner by providing to 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 to request a quick refund of the excess WHT on behalf of such Registered Owner, if some information is provided by the CFIs at the latest within 25 calendar days from the date of payment 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, included late payment interest if applicable³, is made within 25 days from the date of the request or from the date reporting obligations under this Proposal have been met by all relevant CFIs, whichever is the latest. This should take place within 50 calendar days from the date of payment.

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.

In addition, Member States may exclude the benefit of the systems of relief under the Proposal where at least one of the financial intermediaries in the securities payment chain is not a CFI and a subsequent CFI in the chain has not provided to the competent authority the information that the financial intermediary should report under this Directive if it were a CFI. They could also exclude the benefit of systems of relief when an exemption of the WHT is claimed.

Finally, systems of relief under the Proposal will never be provided where the dividend has been paid on a publicly traded share that the Registered Owner acquired within a period of two days before the ex-dividend date or when 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 at the ex-dividend date.

³ At a rate equal to the interest or equivalent charge applied by the Member State to late payments of income tax by registered owners, or, if the national legislation of the Member States does not include such provision, at the Euro short-term rate plus 50 basis points or the equivalent interest rate used by their Central Bank plus 50 basis points, if they are not part of the European Exchange Rate Mechanism.

Where the relief at source and quick refund systems set out in this 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, are 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 on 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 withholding tax procedures for non-resident portfolio investors to the extent it should facilitate cross-border investment within the EU. We especially welcome the introduction of the eTRC, its broad scope of application and the very short deadline in which tax authorities will have to provide it.

Nevertheless, this Proposal creates new heavy reporting and due diligence duties on CFIs with a potentially high degree of liability. At this stage we can, however, already note that, as the systems of reliefs 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 reliefs 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 so if a CFI concludes that they do not meet the eligibility condition, it should be allowed to refuse to request the benefit of a system of relief on behalf of a Registered Owner. However, it is 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 verification 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 a case, the systems of relief would not be applied and the Registered Owner or its authorised representative could still request for 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 Proposal is now in the hands of the Council of the EU and the EU Parliament. Once adopted, the Proposal should be implemented into national legislation by 31 December 2026 and come into force on 1 January 2027. We will keep you informed of any further developments in the legislative process.

Do you have further questions?



ANTOINE DUPUIS
Partner,
International & Corporate Tax
antoine.dupuis@atoz.lu
T + 352 26 940 207



MARIE BENTLEY
Knowledge Director
marie.bentley@atoz.lu
T +352 26 940 903