France Post-Marché

Public consultation:
Withholding taxes – Directive proposal of the European Commission – 19 June 2023
FRANCE POST-MARCHE's position paper

FRANCE POST-MARCHE (FPM) is the leading association representing the post-trade business in France and Europe.

FPM represents through its 82 members a wide range of activities: market infrastructures, custodians, account-keepers and depositaries, issuer services, reporting and data management services, with a total staff of 28,000 in Europe of which 16,000 in France.

Our members acting as financial intermediaries account for 26% of the European market.

On 19 June 2023, the European Commission has published a Directive proposal to make withholding tax procedures in the European Union (EU) more efficient and secure for investors, financial intermediaries (*e.g.*, banks) and Member States' tax administrations. Once adopted by Member States, the Directive should come into force on 1 January 2027.

FPM welcomes the opportunity to contribute to the public consultation initiated by the European Commission on this proposal for a Directive on Faster and Safer Relief of Excess Withholding Taxes (FASTER Directive).

I. General comments

FPM fully agrees with the general objectives of this proposal:

- Remove barriers to cross-border investment (Capital Market Union)
- Strengthen Member States' ability to prevent and fight against potential fraud and abuse
- Improve processes for the benefit of investors

FPM also welcomes some of the practical principles that drive the proposal of the European Commission to simplify and digitalise withholding tax processes within the EU:

- Replace paper-based procedures by a digital tax residence certificate (eTRC) with harmonised format and content
- Common reporting obligations across all EU Member States
- Promotion of Relief at Source (RAS) and Quick Refund (QR) procedures to obtain reduced tax rates under domestic rules or double tax treaties
- Common process for QR requests

However, we fear that the balance between the intended objectives and the proposed means has not been well weighted by the European Commission, which will jeopardize the achievement of these objectives.

Firstly, we are concerned by the due new diligence requirements, and in particular the lack of clarity thereof, imposed on Certified Financial Intermediaries (CFI) to collect and verify documentation per income distribution. The expectation placed on CFIs to validate and

investigate the circumstances around which an income payment takes place may mean that CFIs cannot take up the relief mechanisms envisaged under the FASTER Directive nor apply double taxation treaties. The proposal creates a new and disproportionate responsibility on the shoulders of financial intermediaries having a CFI status.

This weight of both due diligence and liability is likely to lead many financial intermediaries to stop offering withholding tax relief services currently provided to their clients. Investors (especially individuals) would therefore have even more difficulties than today to benefit from reduced tax rates. As a consequence, one of the major objectives of the Directive would be missed.

The proposal fails to properly address/explain the notion of beneficial owner (registered owner in the proposal). There is an urgent need for more clarity in order for the Directive to function properly and create a level-playing field in the EU.

This proposal could thus be an obstacle to the application of double tax treaties. These new obligations, if they were to be applied as they stand by CFI, would generate very important and costly technical developments that would probably be difficult to be borne by the investors. No custodian currently has the means to develop such complex reporting and control systems as provided for in the proposal.

We are also concerned by some provisions, especially those related to reporting, that would generate administrative burdens and contradict the objective of simplification and speed initially desired by the Directive.

We would like to highlight the risk of a fragmented implementation and therefore the need to ensure Member States do not create additional/divergent requirements, with respect to the various obligations resulting from article 4, article 9, article 11 and article 13, notably in terms of reporting and due diligence.

Indeed, financial intermediaries, in order not to suffer from exponential costs, cannot support formats/requirements that do not converge towards a standard. A fragmented implementation will entail the consequences already mentioned: passing on additional costs to European customers/citizens, or even excluding customers from the benefit of the double taxation treaties.

As a conclusion, we consider that the proposal as it stands should be redesigned in order to better achieve the general objectives mentioned by the European Commission.

In this respect, an effective way of dealing with the general objectives of this proposal would be to implement, within the EU, harmonised dividend and interest withholding tax rates not exceeding the usual rates provided by double tax treaties.

II. Detailed article-by-article commentary

CHAPTER I – GENERAL PROVISIONS

Article 2 – Scope

The Directive proposal is only limited to publicly traded shares and bonds. However, we believe it should be extended to all shares and bonds that are issued by Central Securities Depositories (CSDs) located in the EU and to units in Collective Investment Vehicles

Article 3 – Definitions

The definition of registered owner (also referred to in article 1) is neither accurate nor correct, especially when applied to countries using nominee structures (*e.g.*, Ireland).

The Directive should only use the concept of "beneficial owner" and provide a clear definition of this concept (such as the beneficial owner notion as available in the OECD framework) that must be applicable for all Member States.

The definition of financial arrangement is also not clear enough. The definition of financial arrangement must be exhaustive and leave no doubt to any market party what is covered by such definition. Otherwise, it would be impossible to apply this concept and this would create uncertainty for the stakeholders[1].

CHAPTER II – DIGITAL TAX RESIDENCE CERTIFICATE

Article 4 – Digital tax residence certificate (eTRC)

We welcome the decision to require all Member States to implement a consistent, harmonised and electronic process to issue certificates of tax residence. However, we believe the proposal should go further and envisage the implementation of a common portal used by all Member States to receive and process requests for eTRCs.

There should be a provision to require Member States to allow beneficial owners to delegate the request of eTRCs to a third party (*e.g.*, financial intermediaries), along with a requirement to implement a system to allow for bulk uploads/requests of certificates of tax residence as both financial intermediaries and institutional investors may need to request many documents for many entities at the same time.

[1] Important to note that the information exchanged in the settlement chain is limited to the information enclosed in settlement instructions (such as ISIN, trade date, settlement date, place of settlement, quantity of securities to settle, cash consideration (if applicable) and name of the custodian of the counterparty connected to the central securities depositary (CSD) of the issued securities, where the securities/cash would need to settle). CFIs enter in their turn (depending on the clearing structure in a market) into transactions by way of novation with a central counterparty (CCP) to arrange for the settlement. These are stand-alone transactions. Unless CFIs are involved through other banking services, they will not know the agreement under which a settlement instruction is given. If a CFI has another intermediary bank as client that services the beneficiary, it is even more unlikely that the CFI will know the background of the settlement instruction.

The proposal should also take into account the need of Member States' investors to use eTRCs when investing in third countries. Moreover, the above-mentioned portal should also be available for investors to request certificates of tax residence to satisfy the need of third countries, which may impose their own specific requirements and may require traditional/physical certificates of tax residence. We would like to highlight that third countries will also continue to require a certification of their own local specific tax forms by investors' tax authorities.

To secure the application of reduced tax rates, it is expected that an eTRC requested for the application of tax treaty benefits clearly mentions that the investor is resident within the meaning of the tax treaty concluded between his country of residence and the income source country.

Moreover, eTRC should be adapted to fit with Collective Investment Vehicles (in many cases, these vehicles have no tax residence but a jurisdiction if establishement).

We do not agree with the term "deemed resident" and would recommend deletion of the word "deemed" (another source of uncertainty).

We ask for the removal of the reference to EUID (European Unique Identifier) as not widely used. Instead, it should be replaced by LEI (Legal Entity Identifier) to ensure usage outside the EU.

CHAPTER III – WITHHOLDING TAX RELIEF PROCEDURE

SECTION 1 – CERTIFIED FINANCIAL INTERMEDIARIES

Some clarifications should be brought on the entity/financial intermediary required to register.

For large financial intermediaries that operate across multiple Member States and third countries, it is important to have clear rules on whether the registration happens at legal entity/head office or branch level.

Article 6 – Requirement to register as certified financial intermediary

Member States should limit the registration requirements only to those financial intermediaries that would like to offer RAS under article 12 or QR under article 13 of the Directive proposal.

Based on the current version of the text, registration and reporting are also mandatory to standard refunds (article 15). Financial intermediaries should still be allowed to offer standard refund services as per current procedures, without having to register and carry out reporting.

Article 7 – Registration procedure

With respect to article 7.1(c), we note that to be registered as a CFI, a financial intermediary must provide a self-declaration of compliance with the provisions of DAC2 and AML/KYC Directives.

We would recommend that this self-declaration mention that the FI has not "repeatedly and intentionally not complied with its obligations" under DAC2 and AML/KYC Directives (as per article 8.2), instead of a general self-declaration of compliance.

SECTION 2 – REPORTING

Article 9 – Obligation to report

The reporting proposed in article 9 would require a huge technical and financial effort for a financial intermediary, without commercial return if the intermediary is finally compelled to give up the services currently provided to its clients in the application of reduced withholding tax rates due to the too risky responsibility.

Would this reporting eventually be implemented thanks to tremendous efforts from the EU Member States and the financial intermediaries, it would provide to EU tax administrations a huge quantity of data that might be difficult to reconcile.

In this context, as there are currently very strong disparities between Member States, we call for the establishment of a standard reporting framework for all Member States, without any possible adaptation (standard in terms of reporting deadlines, computer format, exchange protocol, level of detail of the information to be reported, etc).

This standardisation may help to reduce the cost of this reporting : an excess of cost for the CFI would eventually be borne by investors and may discourage them from claiming tax treaty benefits.

Besides, the reporting mechanism described in article 9.1 would require CFIs to report on a rolling basis within a 25-day period after record date. This would prove very complex to manage for financial intermediaries and also for tax administrations which would have to reconcile the data received by CFIs.

Instead, we propose that the Directive requires CFIs to issue one report per CFI and income payment, on a yearly basis. Such reporting obligation should be limited to the cases where a reduced withholding tax rate has been applied at source as per article 12 (*i.e.*, no reporting obligation if a standard domestic withholding tax rate has been applied at the income payment date under article 13 – QR - or 15 – standard refund).

The threshold of €1,000 should be removed as it would be complex to manage, especially taking into account market claims and FX variations for non-euro Member States or securities denominated in a foreign currency.

Moreover, we suggest deleting the sentence « *as well as access to their premises for the purpose of audit* » to avoid conflict with private property laws.

Finally, we would again like to highlight the risk of a fragmented implementation by Member States and therefore the need to ensure they do not create additional/divergent requirements in terms of reporting.

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SECTION 3 – SYSTEMS OF RELIEF

Article 10 – Request for relief at source or quick refund

Under article 10.1(b), to request relief, on behalf of a registered owner, a CFI has to verify and establish the registered owner's eligibility. We would like to:

- modify "has verified and established the register owner's eligibility" by "check the consistency of the beneficial owner's eligibility with the information the business line of the CFI performing the verification has access to in its normal course of business"; and,
- remove "such verification may also include a risk assessment that takes into account the credit risk and the fraud risk", as this risk assessment is impractical and not objective.

Under article 10.2(a) and (b), the anti-abuse provisions should be reconsidered as it could cause additional problems:

- legitimate buyers, including those whose transactions settle on or before record date, would be unjustifiably disadvantaged as they would be excluded from both RAS and QR procedures
- different parts of the same record date position/holding may be subject to different tax processing (RAS/QR *versus* standard refund), causing reconciliation issues for both financial intermediaries and tax administrations
- taking into account Shareholder Rights Directive II (SRDII) requirements and European corporate actions standards for income distributions, where pay-date is the day after record date[2] (currently set one business day after ex-date but due to become equal to ex-date if Europe moves to T+1), it is unclear how withholding tax agents would be made aware of the positions/transactions to be excluded from RAS ahead of pay date.

Under article 10.3(a), a Member State may notably exclude requests from relief under articles 12 and 13, where "**at least one of the financial intermediaries in the securities payment chain is not a certified financial intermediary and a subsequent certified financial intermediary 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 certified financial intermediary**".

This provision is irrelevant/impractical at the level of CFI. Indeed, CFI has no visibility on all financial intermediaries within the payment chain, on their status of CFI or not, nor on their compliance with their reporting obligations. Only tax administration may verify this rule.

As a result, there is a strong probability that there will be a reduction of investors/positions that could benefit from RAS, especially in Member States where the RAS is working very well today (*e.g.*, France – since 1994, Italy, Ireland or Spain), and an increase of standard tax refunds, contrary to the objective of the Directive.

Article 11– Due diligence of registered owner's eligibility

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[2] Please refer to article 8 of Implementing Regulation 2018/1212 where it is stated that "the payment date shall be set as close as possible to the record date, issuer deadline or the deadline set by the third party initiating a corporate event, as applicable, so as to allow for the processing of payments to the shareholders as swiftly as possible".

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Issues and impacts raised by article 11

According to the Directive proposal, Member States would require CFIs to ensure that investors are eligible to a reduced withholding tax rate:

- CFIs would collect the eTRC of the registered owner, or the appropriate proof of residence in a non-EU country. CFIs will also need to collect a declaration from the registered owner indicating that the latter is the beneficial owner of the income and is not engaged in a financial arrangement linked to the underlying publicly traded share that has not been settled, expired or otherwise terminated at the ex-dividend date.
- CFIs would also have to check this information against their own records (notably AML/KYC records).

Verification by the CFI of the eTRC and of the registered owner's declaration is especially a major issue. Currently, for instance, with respect to the French market, the income recipient has to certify to the paying agent that he is the income beneficial owner (e.g. decision of the French State of Council dated 5 June 2020, n° 423809). The paying agent has no obligation, nor legal of practical mean, to challenge this statement.

In the "Danish cases" (CJEU, 26 February 2019, joined cases C-116/16 and C-117/16), the Court of Justice of the European Union stated that "in order to refuse to accord a company the status of beneficial owner of dividends, […] a national authority is not required to identify the entity or entities which it regards as being the beneficial owner(s) of those dividends", since "that authority cannot be required to furnish evidence that would be impossible for it to provide" (…), "given the complexity of certain financial arrangements and the possibility that the intermediary companies involved in the arrangements are established outside the European Union".

How can the European Commission reasonably expect CFI to perform this diligence before the payment date or even within 25 days (having in mind that, in many cases, investors are not their direct clients), while tax administrations are unable to perform the same diligence during tax audits (needing months or years of investigation), despite their legal means of investigation?

Such provisions would significantly worsen the situation of financial intermediaries. Indeed, the weight of both due diligence and liability is likely to lead financial intermediaries to stop offering withholding tax relief services currently provided to their clients.

Investors (especially individuals) would therefore have even more difficulties than today to benefit from reduced tax rates. As a consequence, one of the major objectives of the Directive would be missed.

This situation would also be detrimental for EU tax administrations that would face an increased number of standard tax reclaims. Are EU tax administrations prepared to process standard tax reclaims in mass?

Our proposals

Article 11.1(a), as mentioned in our feedback to article 3, should refer to a single common definition of beneficial owner applicable by all Member states as for example the one available under OECD framework

Regarding article 11.1(b), in addition to the further clarifications that are needed for the definition of financial arrangement, it is unclear what is intended of the notion of “being linked to underlying publicly traded shares”. The term “linked” is vague and too broad and therefore unusable in practice.

If the eTRC is a digitalised and standardised document, this is not the case of the declaration that should be obtained by the financial intermediary from the registered owner (article 11.1).

We consider that the eTRC/proof of residence should be the only document required to be collected by the financial intermediary. Should the declaration be maintained, we require this document to be under a digitalised format and its content to be clearly defined and standardised. If not, it would result in 27 different versions of such declaration in contradiction with the harmonisation targeted by the Directive.

Regarding all the due diligence requirements mentioned in article 11.2, the verification of the eTRC by the CFI can be achieved only if it is about checking that the eTRC is correctly filled in terms of form. CFI can’t verify the substance of this form (only tax administrations can perform such a verification).

Verifications required in points (b), (c) and (d) of article 11.2 seem disproportionate compared to the Directive’s objectives.

FPM proposes:

- to limit (a) to verify that the eTRC/proof of residence is correctly filled in terms of form
- to precise point (b) : clear guidance should be provided to confirm that the CFI can rely on the information provided by the client, unless the CFI has actual knowledge to the contrary (examples of such knowledge should be provided). In other words, in terms of verification of documentation provided by the client, the standard for certified financial intermediaries should be their actual knowledge based on available information.
- to modify (c) to request the CFI to check the consistency of the investor’s request to benefit from a reduced tax rate under domestic law or a double tax treaty only with the tax documentation provided, and to clearly state that the CFI’s liability should not be engaged if it has been provided with the adequate tax documentation of the beneficial owner. It seems that there is a typo mistake on “jurisdiction” (I should be without “s”).
- to precise point (d) that is one of the most problematic requirements in the current proposal, for CFIs. The definition of financial arrangement is so unclear that it is not possible for CFIs to build any solid policy on, especially if the beneficiary is not the direct client of the CFI. We also refer to the comment above on article 11.1(b) in relation to the definition of financial arrangement as proposed. Even if the possible existence of an abusive financial arrangement could be uncovered, it is unclear what CFIs can do against that. In combination with the intended liability of CFIs there will be massive uncertainty in the market on this point. These due diligence obligations in combination with the proposed liability principle creates *de facto* a strict liability for CFIs for behaviour of clients (or even the client’s clients) over which they exercise no control.

In this context, please note comments made under article 10, namely that any consistency check should be limited to “*the information the business line of the CFI performing the verification, has access to in its normal course of business”.*

Article 12 – Relief at source system

Article 12 states that CFIs maintaining a registered owner's investment account may request RAS to the withholding agent.

The CFI applying RAS is not always the one maintaining the registered owner's investment account. This could be another financial intermediary that is the CFI's client. If the proposal is read in a strict manner, registered owners cannot be serviced if they are not the direct client of the CFI registered in that Member State.

It is unclear how this provision may work in case of multiple intermediaries in the securities chain.

Article 13 – Quick refund system

Article 13 states that CFIs maintaining a registered owner's investment account may request QR.

The CFI filing for the QR is not always the one maintaining the registered owner's investment account. This could be another financial intermediary that is the CFI's client. If the proposal is read in a strict manner, registered owners cannot be serviced if they are not the direct client of the CFI registered in that Member State.

It is unclear what is intended with this provision in case of multiple intermediaries in the securities chain.

In line with our previous comments under articles 9, we strongly recommend any reference to a reporting to be removed in article 13.2. The delay mentioned in this article should therefore start from the day of the request.

In articles 13-1 and 13-2, for practical reasons (for both CFI and tax administrations), the successive delays of 25 days should be computed on the basis of "business day" instead of "calendar day".

Article 16 – Civil liability

Article 16 creates a new civil liability for a financial intermediary that does not comply, intentionally or negligently, with its obligations.

The notion of 'civil' in the header of the provision leads to uncertainty as to what is intended and should be deleted. This provision on liability should only be invoked against a CFI by tax authorities (or the public prosecutor in case of criminal charges) and for that there should be a solid basis in applicable administrative (tax) laws, not in civil law.

In the current proposal, CFIs lack protection against allegations of tax authorities as the liability is proposed in a stand-alone manner that is disconnected from any procedures that tax authorities may instigate against beneficiaries that allegedly abused national tax laws (and for which the CFI is held liable). The sole basis of liability should be administrative tax law.

The main principle must be, at all times, that tax authorities, in case of suspicions of abuse by the beneficiary, should firstly impose levies on that beneficiary. The CFI should only become liable if it intentionally acts against the law.

We fear that this provision may be used by tax authorities, when they suspect an underwithholding but find difficult to identify the beneficiary or to reach this beneficiary abroad : the temptation may then exist to firstly impose levies on well identified and easily reachable CFI located in the jurisdiction of the concerned tax authorities, instead of pursuing the beneficiary.

Given the above, the current wording does not meet the principles of proportionality and subsidiarity as regards the protection of the position of the CFIs. CFIs act as agent and not as principal when providing RAS, QR and/or standard refund services. Therefore, if CFIs meet their clearly and exhaustively described due diligence requirements as agents, they should be off the hook at all times.

As such a financial intermediary that has performed the set out due diligence tasks (which need to be clear and unambiguous) in good faith should not be subject to penalties, fines or other sanction. We would propose to remove “negligently” as it seems disproportionate. In addition, the financial intermediary should be given the possibility to exculpate by correcting a mistake within a certain timeframe before it can be held liable. The competent authority should have the burden of proof. As financial intermediaries only provide administrative support on tax filings and are not allowed to provide tax advice, it is disproportionate to set out a full liability for the customer’s tax debt.

As a closing remark, there needs to be a facility that in case of doubt, CFIs can notify tax authorities of a possible unjustified refund before it is granted and that in case of such notification made in good faith, the CFI will be protected against liability and/or supplementary levies.

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CHAPTER IV – FINAL PROVISIONS

Article 22 – Transposition

It is indicated that Member States should adopt and publish this Directive by 31 December 2026, at the latest, and apply such provisions from 1 January 2027. However, in case of a late transposition by a Member State, financial intermediaries would not have enough time to adapt and register to become a CFI.

We believe all Member States should apply the Directive’s provisions on the same date, which should be defined as 18 months after the above-mentioned deadline for adoption/transposition by Member States, making the effective implementation date, the 1 July 2028.