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VIA ELECTRONIC DELIVERY

European Commission
Attn: Mr. Reinhard Biebel
Director, TAXUD.D.2 (Direct Tax Policy & Cooperation)
Rue de Spa 3 / Spastraat 3
1000 Bruxelles / Brussel
Belgium

Dear Mr. Biebel,

Re: Response to Inception Impact Assessment on new EU system for the avoidance of double taxation and prevention of tax abuse

This letter is submitted on behalf of the Tax Committee of the Association of Global Custodians ("AGC" or "Association"),[1] in response to your invitation to comment on the Inception Impact Assessment document.

The issue of inefficient withholding tax relief procedures has been on the EU agenda for a long time. During that time, there have been numerous communications urging Member States to improve those procedures. However, the issue remains one of material concern for members who still see opportunities for significant concrete steps to be taken by Member States (individually) and by the EU institutions (collectively) to improve the procedures. The AGC also recognizes the importance of tackling market integrity risks, in particular those associated with dividend arbitrage trading schemes,

[1] The Association is an informal group of 12 member banks that provide securities safekeeping and asset servicing functions to cross-border institutional investors worldwide, including investment funds. In providing global custody services, AGC members routinely seek appropriate withholding tax relief on behalf of custody clients by processing millions of such claims in the aggregate each year, affecting substantial amounts of cross-border portfolio investment flows in and out of countries worldwide.

which have taken place in some jurisdictions such as Germany, Denmark, Belgium, and Austria.

Addressing these issues is critical to our members, particularly in their roles as global custodians who safeguard and administer securities owned by their clients,[2] including the settlement of trades, and collection of income and tax entitlements. An informal survey of AGC members reveals that the member banks hold over $70 trillion (€60 trillion) worth of assets in safekeeping; have tens of thousands of global custody clients worldwide; and process millions of separate dividend payments annually.

The "Action Plan for fair and simple taxation supporting the recovery strategy"[3] referenced in the Inception Impact Assessment document, states that cost for cross-border investors has been estimated to amount to more than €8 billion a year, based on tax forgone and opportunity cost. We believe this number may be now out of date and likely higher particularly if we consider the impact the COVID-19 crisis has had on cross-border investors to access withholding tax relief through a process that is heavily reliant on the movement of physical documentation.

The AGC welcomes the opportunity to present our views and is supportive of the European Commission's objectives of making withholding tax relief procedures more efficient and increasing the ability of tax administrations to identify treaty abuse.[4] The AGC also wishes to note that it is our view that only centralized initiative like the one the European Commission is now undertaking can, efficiently, solve the problems identified in the consultation document. As such, the Association wishes to suggest some broad principles for designing solutions to achieve those objectives.

AGC thoughts on a future tax relief system

The best approach to providing treaty-based withholding tax relief is to have a well-functioning relief at source system. Such a system optimizes cash flow to the investor, thereby allowing cash to be immediately reinvested in the market, which encourages investment and growth. Such a system should also be accompanied by a well-functioning reclaim system as a fallback to deal with occasional but inevitable cases where it is not possible to apply relief at the time of payment (e.g., due to a delay in receiving entitlement documentation from the investor). Therefore, policy options

[2] Global custodians' clients are typically institutional investors located in different jurisdictions and are mainly comprised of asset owners (e.g., state-owned pension funds and investment funds, collective investment vehicles, pension funds), banks and other financial intermediaries, and international and supranational organizations.
[3] COM(2020) 312 final.
[4] The AGC has previously submitted comments to the EC in support of reforms to European withholding tax procedures on 3 July 2014 (in response to the consultation on tax problems faced by EU citizens when active across borders within the EU), 13 May 2015 (in response to the consultation on the European Commission Green Paper, Building a Capital Markets Union), 15 November 2016 (in response to the consultation on the cross-border distribution of investment funds across the EU), 15 November 2017 (in response to the CMU consultation), and 4 August 2020 (in response to the consultation on the CMU project and the High-Level Forum (HLF) Report recommendations).

should include both a standardized EU-wide system for withholding tax relief at source (Option 2 in the Inception Impact Assessment) and simplified and streamlined withholding tax refund procedures (Option 1). Enhancing the existing administrative cooperation framework (Option 3) is also likely to be necessary.

1. Primary model – Relief at Source

The lack of a standardized EU-wide system for withholding tax relief at source is a major impediment to the free flow of investment within the EU. Moreover, some EU Member States do not provide relief at source for treaty claims (e.g., Austria, Belgium, Germany, Netherlands, etc.). Providing a well-functioning relief at source system is the best way to ensure treaty reductions to withholding tax have the effect of removing obstacles to cross-border investment.

Such a relief at source system should have, at a minimum, standardized documentation and verification requirements, a reliance on investors to self-certify their tax status, and a common and efficient electronic information transmission mechanism. These characteristics are paramount to minimize the need for duplicate records, ensure the integrity of the data, and reduce the friction of excess costs (e.g., administrative expenses) associated with cross-border investment. Other welcome attributes of a broad relief at source model would be the reasonable validity period of tax documentation during which the withholding tax agent could apply reduced withholding tax rates (e.g., three years from the end of the year of issuance), a common categorization of investors, and the use of a single tax ID to identify each investor.

We believe that such a relief at source model would benefit all stakeholders involved in the process, in particular:

1. **National tax authorities** (in both income source and investor residence countries) -- who would benefit from improvements to the withholding tax process that may streamline procedures (relief processing as well as tax residency certification), reduce the risk of fraud, reduce unnecessary foreign tax credit claims, and allow for better tax transparency of the relief process.

2. **Investors** – who would be able to significantly reduce tax compliance costs arising from a multitude of systems and documents and who would receive their passive income at the tax rate they are entitled to at the time of the payment, enabling the reinvestment of that income back into the European capital markets.

3. **Intermediaries processing tax relief and asset owners entitled to tax recovery** -- who would obtain greater operational processing efficiency, tax entitlement certainty, and reduced risk.

Ultimately, the **EU internal market** would profit from such a model as it enables a smoother cross-border exercise of the EU fundamental freedoms, in particular the Freedom of Capital.

International Relief at Source Models to be Considered

The withholding tax relief at source system in the United States is widely recognised amongst investors and financial intermediaries as a pragmatic a relatively simple model that has enabled a well-functioning tax relief model, which the EU Commission may want to consider while developing the policy options.[5] Some of the US relief at source model features are:

- Investors can provide to an upstream withholding agent a self-certification using either a Form W-9 for US residents or a Form W-8 for non-US investors.

- The majority of the US W-8 forms have a validity period of three years from the end of the year in which they are signed, unless the recipient can obtain a US domestic tax identification number.

- The forms do not require certification by the investor's home country tax authority[6] and can be delivered electronically, and a "wet" signature is not required.

- As long as information provided on the Form W-8 is consistent with what the custodian has on file relating to the investor's account, the custodian is able to pass the document to the withholding agent who can rely on it.

- Investors self-certify they are eligible for treaty relief. Custodians are not at risk for providing an administrative service to their clients who are responsible for their own tax affairs.

The US relief at source system also includes a very useful set of procedures under which a withholding agent is able during a limited time period to make retroactive adjustments to the amount of withholding to correct for overwithholding (e.g., where investor documentation is obtained between the date of the payment and the due date of the withholding tax return).

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[5] A thorough summary of the US withholding tax system and its application to non-resident aliens and foreign entities can be found at the following US IRS link: 2021 Publication 515 (irs.gov).

[6] Instead, the representations made therein are done under "penalties of perjury" by the beneficial owner of the income, i.e., the investor bears the responsibility for the information provided and is the person liable towards the IRS (rather than the financial intermediary, unless the latter knows or has reason to know that the investor's claim to relief is inaccurate).

The Commission may also want to consider the Canadian and Irish tax systems,[7] which provide a simple set of codified tax relief at source forms for beneficiaries, for example Canada's NR301 (Canadian Declaration of eligibility for benefits (reduced tax) under a tax treaty for a non-resident person; valid for three years) and Ireland's V2 forms (non-resident forms valid for five years).

2. Supplementary model – Tax Reclaims

We acknowledge that even where a well-functioning relief at source system may be in place, the ability to make reclaims will be necessary in certain cases. This may be the case, for example, where certification to avail for relief at source is not provided timely. As such, having a simplified and streamlined procedure for making reclaims in the EU is critical. This could include, for example:

- A common reclaim form in all EU countries, or the utilization of a standardized withholding tax relief form for both relief at source and reclaim purposes;
- A common standardized package of supporting documentation and associated guidance;
- A set of common definitions (such as tax residence for treaty purposes, beneficial ownership, liability to tax, etc.), including categorization of investor types; and
- True digitalization of the reclaim process to move away from the current highly manual and paper-based reclaim process, which many governments continue to support.

We believe this would reduce handoffs in the reclaim process and improve efficiency in the collection of tax relief.

3. Administrative cooperation

Enhancing the administrative cooperation framework within the EU with regard to the collection of withholding taxes, both for reporting and beneficial owner exchange of information, can serve the dual purpose of helping tax authorities to identify treaty abuses and providing the confidence needed to adopt standardized and proportionate relief at source procedures. We believe that if such exchange of information could utilize the technology solutions created when the Common Reporting Standard ("CRS") was developed (this was utilizing XBRL transmission protocol – as developed by the

[7] A high level overview of the Irish and Canadian withholding tax systems may be found at the following links respectively: (Ireland) Dividend Withholding Tax (DWT) (revenue.ie) and (Canada) Non-Residents and Income Tax – 2020 - Canada.ca.

OECD in its work on TRACE), we could see huge advances in streamlining the withholding tax relief processes for the benefit of all stakeholders. Exchange of information could well mean that the need to rely on government-issued Certificates of Tax Residence could be eliminated.

Developing a successful relief at source system

Clear roles and expectations

For a withholding tax relief at source system to operate successfully, there must be a careful balancing of various objectives based upon a full understanding of the roles and capacities of the various stakeholders.

For financial intermediaries like global custodians, who process high volumes of payments and have limited lines of sight into the circumstances surrounding investors and their participation in particular transactions, including those that may be arranged through their related entities, the determination of whether the risk associated with participating in a relief at source regime is manageable or not will depend upon numerous factors, including:

- the number of data points the financial intermediaries are required to evaluate,
- the availability of the relevant data,
- the cost of collecting the relevant data (including, e.g., cost associated with non-standardized data and documentation requirements),
- the clarity and conclusiveness of the guidance concerning the validation requirements to be completed on the data,
- the extent to which necessary processes can be automated, and
- the commercial and legal ability to transfer risk to investors or other intermediaries better positioned to manage the risk due to better visibility of the circumstances surrounding the investor and the particular transactions they enter into.

Consideration of the above is critical to allow global custodians to adapt and enhance their systems in line with the legislation and tax authorities' expectations and put in place contracts and indemnities with other market participants in the custody chain.

Here again, we would like to emphasize that as long as information provided on the treaty relief form is consistent with information collected by the custodian at the time of onboarding clients, the custodian should be able to pass the document to the withholding agent, who should be able to rely on it.

A regime that does not allow financial intermediaries to realistically manage their risk, taking into account these factors, will not successfully provide investors with their due treaty relief, as custodians do not want to take on an investor's risk when there are no clear guidelines. Ultimately, a system that largely transfers risk and liability to financial intermediaries will lead to fewer tax services being provided by the latter as they feel that the incentive to provide such services is outweighed by the potential cost. In such a scenario, a proposal to revamp the withholding tax framework will have the counterproductive effect of increasing tax collections by Member States in situations where investors should be receiving withholding tax relief. Consequently, the internal market will be harmed as capital will flow less freely.

Applicability beyond the EU

Any system developed for use within the EU should be designed with a view toward its potential application more broadly. Investors are located both within and outside the EU, investment flows circulate both within and into and out of the EU, and financial intermediaries are established and operate both within and outside the EU.

The EU's approach to issues like standardization of documentation requirements, reporting obligations, and exchange of information among tax authorities should take into account the potential ability to transpose that approach to non-wholly-EU settings, where legal mechanisms may differ from those available for purely internal EU use.

Coordination with potential improvements to withholding tax relief procedures in other markets (including, for example, improvements based on the OECD's TRACE proposal) will help to reduce costs and complexity and to develop momentum for more widespread improvement.

Consideration must also be given to the extent to which source country tax authorities may be able to rely on existing exchange of information and due diligence mechanisms in determining how extensive their due diligence requirements need to be. For example, DAC6, CRS, and the UK's Corporate Criminal Liability Offence are all laws that oblige the reporting of harmful practices or tax advantaged schemes. As such, it should follow that financial intermediaries participating in the tax relief process and that already comply with these reporting obligations, would have a robust set of compliance tools. We would be supportive of a system where source country tax authorities within the EU design their due diligence and reporting requirements taking into account a suite of due diligence obligations already carried out by financial intermediaries, eliminating the need for collecting documentation twice and reducing implementation costs.

Here again, there is an opportunity to look to the US Form W-8 as an example of obtaining a collection of information on the beneficiary, as well as information required under FATCA. The CRS self-certification can be combined with the treaty relief form to eliminate the need for two separate documents.

Opportunities for the use of new technology

As noted above, digitalization of procedures should be a key element of all policy options to be considered. Current paper-based procedures are costly, slow, and inefficient. They are also susceptible to interruption by situations such as the recent COVID-19 crisis.

Digitalization of procedures would reduce costs, produce more reliable data, and greatly improve the efficiency of relief at source, reclaim, reporting, and intergovernmental exchange of information processes.

We propose one digitalized form across all jurisdictions that could be completed online with validation logic that could be used to verify treaty tax rates based on attributes of the payees. Treaty tax relief forms have certain core similarities across source countries in terms of information requested from the claimant. We see this as an opportunity the Commission should seize to streamline and simplify the data gathering.

Consideration should also be given to the use of new emerging technology, which may include:

- Data lakes (a subset of blockchain), which would give multiple participants access to one trusted source of electronic documents authenticating customer data in a consistent manner across all markets and intermediaries.

- Secure digital portals for uploading customer claim information (so that encrypted spreadsheets and physical reclaim forms are no longer required).

- Digital solutions regarding documentation and signatures.

The above will allow for better real time scrutiny of tax relief claims by tax administrations and will create efficiencies in the process.

Consultation with relevant stakeholders

Robust consultation with relevant stakeholders, particularly with industry bodies of those financial intermediaries expected to play significant roles in any new procedures, will be a critical requirement for achieving a successful solution at an EU level.

A constructive dialogue between policymakers, financial industry representatives, and technical experts will greatly contribute to improving the chances of developing solutions that address all objectives in a successful and proportional way.

The AGC is committed to providing constructive input throughout the process of developing proposals for improved tax relief procedures.

Enhanced diligence in certain high-risk cases

The AGC appreciates the need for any new system to incorporate elements that will effectively reduce instances of inappropriate claims of treaty entitlement. Various options may be worth considering that will provide for enhanced requirements in identifiably higher risk situations. Although the introduction of diligence that diverges from the common standard will increase the cost for market participants, the AGC recognizes that in specific cases it may be required to provide the source countries' tax authorities with appropriate control of their tax system.

Decisions about appropriate solutions will have to take into account a balancing of the various elements involved, including the ability to define the criteria for identifying higher risk situations, the clarity of the guidance relevant to assessing treaty eligibility, the capacity of various parties to access relevant data points and manage the risk associated with applying the procedures contemplated, and the effect of any proposed solution on the practical availability of relief at source.

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The AGC appreciates the opportunity to provide comments on this important initiative. As indicated above, we greatly appreciate the Commission's efforts to ensure the proper functioning of the Capital Markets Union, simplify withholding tax procedures, and prevent tax abuse. In developing a pan-European solution for a well-functioning tax relief at source system, allowing sufficient time for consultation and implementation (particularly if it will require technology enhancements) is critical for its success.

Sincerely yours on behalf of the Association,

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