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Re: European Commission proposal for a Council Directive on Faster and Safer Relief of Excess Withholding Taxes

Dear Sirs,

The Association of Global Custodians ("AGC")[1] Tax Committee very much welcomes the European Commission's goal of improving withholding tax procedures whilst tackling potential tax fraud in connection with withholding tax relief – we are pleased to see its proposal for a Council Directive on Faster and Safer Relief of Excess Withholding Taxes (hereinafter "the proposal"). Our members have long supported the removal of tax barriers to cross border investment and sought harmonization in this area to simplify the process for all stakeholders whilst bringing about faster, more efficient relief for investors. The proposal by the European Commission ("EC") is an important next step on the road to making this a reality.

The current proposal presents some encouraging and positive developments promoting an efficient and sustainable model for claiming tax relief – most notably the move to a common digital certificate of tax residence ("eTRC"). Additionally, AGC supports the principle of common reporting and the intention to ensure either relief at source ("RAS") or quick refund ("QR") is offered in every market. Access to either RAS or QR in every market will increase the attractiveness of investment into the European Union, while common reporting will enhance tax administration and efficiency.

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[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.

While we support the goals of the EC's proposal, there are certain elements of the proposal which would benefit from closer consultation between stakeholder groups to ensure the delivery of a system that proves effective for all. For this reason, AGC recommends the proposal is taken forward in phases, starting with the introduction of the eTRC, whilst work continues developing and setting out more detail on the relief procedures envisioned in Chapter III of the proposed Directive. Alternatively, should this phased approach not be feasible, the AGC recommends extending the timeline for implementation. Full implementation by January 1, 2027, does not allow for proper consideration or development of solutions when the deadline for Member States to adopt the directive is December 31, 2026. A period of at least 24 months between these dates is required for the development of appropriate solutions, particularly where automation is required and preferably a "go-live" date that permits a good lead time prior to peak dividend income season. The AGC also recommends continued industry collaboration during the drafting of rules, development of solutions, and periodic reviews following implementation.

In the provision of tax services, the cornerstone for custodians is the availability of clear, operable procedures by the markets of investment that provide for a very good understanding of a party's responsibilities, particularly where there are obligations towards a tax administration. It is critical that very clear, complete, and instructive guidance is available in connection with these obligations, with examples provided where relevant. Furthermore, due to the high volumes of transactions that are handled, it is imperative that procedures allow for straight through processing with minimal manual intervention. In the absence of such clear guidance and definitions, there is the potential that withholding tax relief at source is reduced whilst compliance costs increase, which is why we suggest a phased approach to implementation to allow time to establish guidance and definitions.

As previously shared, our preferred option has always been the introduction of a common system of relief at source with a simplified and streamlined withholding tax refund procedure. We see that this proposal looks to introduce relief at source and if not possible, quick refund, enabling faster relief.

The proposal also foresees an important and larger role for financial intermediaries, namely to:

- Register as certified financial intermediaries ("CFI")
- Report income payment information to the competent authorities
- Monitor holding period of shares and the possible existence of financial arrangements that are not settled, expired or terminated by the ex-dividend date
- Perform due diligence and verify client documentation and information

This letter seeks to provide suggestions for enhancing the current policy proposals to address our member banks' key concerns.

Common digital tax residence certificate (“eTRC”)

The proposals to introduce an eTRC, and an online portal through which to request the eTRC, are very positive developments, with the primary benefits of reducing physical paper documentation and enabling faster issuance of the eTRC. The proposal also offers an element of certainty and standardization with respect to the validity period of the eTRC (minimum validity period of the calendar year in which it is requested).

The AGC supports the introduction of an eTRC and asks for the following enhancements to the proposal:

- When considering the development of the online portal to submit requests, it should include functionality for financial intermediaries to submit bulk requests for eTRC on behalf of their clients, meaning requests for several clients may be submitted simultaneously, and without the need for individual employees to enter their personal details to perform the request. Allowing financial intermediaries to submit bulk requests will significantly improve the efficiency of the online portal.
- European investors will still be required to supply certificates of residence for markets outside of the European Union (“EU”) and where those markets do not accept eTRC, investors must still retain the ability to request physical certificates to continue claiming relief in those markets, preferably via the same online portal. Where possible, the EC on behalf of the Member States, may consider discussing the acceptance of the eTRCs in third country markets such as Switzerland, the United Kingdom and Norway, to ensure their acceptance, particularly since some Member States have elected to no longer provide signatures and stamps to third country tax authority withholding tax relief forms.
- Similarly, certificates of residence issued by third countries should be confirmed as acceptable for the purpose of the proposal, to ensure that all investors may benefit from the procedures and ensure they are not disadvantaged.
- Some markets outside the EU require certificates of residence that reference a specific tax treaty. If the EC considers our proposal above, flexibility may be required to address the requirements of these external markets.
- The European Unique Identifier Number (“EUID”) should be replaced by the LEI as this will prove more useful to recipients in jurisdictions outside of the EU and will still enable an efficient identification of EU companies.
- The proposal notes that Member States shall provide an eTRC "to a person deemed resident in their jurisdiction for tax purposes." It is not clear what is meant by "deemed resident", so we would like to ask for clarification of why the term was included and its meaning. If there is no additional meaning, we propose that the word "deemed" be deleted from the proposal.

Relief where eTRC is not required

We have previously discussed whether investors need to provide an eTRC in circumstances where it is not a pre-requisite for relief. The AGC notes that certain Member States have introduced reductions and exemptions from withholding tax into their local legislation based on criteria other than the tax residency of investors. For example, a number of Member States allow for an exemption from withholding tax based on the UCITS status of the investor. In certain circumstances, an investor may be UCITS-compliant, but not able to procure a certificate of tax residency from the local tax authority. We would like to ask for clarification if the proposal envisages application of relief in these circumstances, where a certificate of residency is not required.

Due diligence and verification

With respect to the collection of information and subsequent verification processes foreseen in the proposal, we note the following activities are required to be undertaken by a CFI:

- Collect and verify the tax residence certificate.
- Collect and verify the registered owner's tax residence and declaration, declaring that they are the beneficial owner of the payment according to the source country's legislation, which "must be verified against internal control mechanisms for compliance with obligations relating to money laundering and terrorist financing or comparable information required in third countries".
- Verify the registered owner's entitlement to a withholding tax rate based on the investor's specific circumstances, noting this may include a risk assessment that takes into account the credit risk and fraud risk.
- Indicate, based on information available to the CFI, if there is an awareness of the possible existence of any financial arrangement involving the underlying security that has not been settled, expired or terminated by ex-date. Reporting on this should only be required by CFI who may have been directly involved in the relevant financial arrangement.

The CFI may be found to be liable due to inadequate compliance with these obligations. There are a number of concerns the above requirements present based on the available detail in the proposal.

Registered owner

Article 3 (14) defines the term registered owner as "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." Whilst we appreciate that the European Commission has acknowledged the challenges associated with the beneficial ownership concept, and this proposal does not seek to address that at this time, this term presents some challenges in the text. The interpretation of "registered owner" may not retain its intended meaning in this context, and whilst we understand account owner is not a term that may replace it, this seems to be closer to what we

understand registered owner reflects. We acknowledge this is not a simple term to address in the proposal and suggest that alternatives could be discussed further should a phased approach be adopted. We also note that adopting a streamlined approach to determining beneficial ownership, rather than requiring financial intermediaries to collect information based on the different standards of each Member State, will provide significant streamlining and simplification benefits.

Verification

In our previous submissions, we have shared that financial intermediaries, such as global custodians, rely on information and representations received from our clients to ensure the correctness of a tax relief application and therefore are dependent on the quality of information provided by clients. If there is a misrepresentation or unknown inaccuracy in such information and such misrepresentation or inaccuracy is no fault of the financial intermediary (i.e., to the extent its systems and control environment have performed to the standard expected) then the financial intermediary should not be liable for any resulting tax loss. In other words, a financial intermediary should only be liable for any tax loss resulting from inaccurate or incomplete due diligence conducted by that financial intermediary.

The expectation that a financial intermediary should verify the entitlement of their client to a lower withholding tax rate (Article 11 (2)(c)), without the concept of beneficial ownership being clearly defined, and without access to all the information related to a beneficial owner's facts and circumstances to make that determination, does not seem reasonable. This is the reason why this determination can only be made by the beneficial owner themselves. A CFI may perform an incorrect assessment for which they will be held responsible and therefore the AGC requests for this requirement be removed from the proposal. It is within the capability of global custodians, upon provision of clear and specific guidance, to verify the information in an eTRC and a beneficial owner declaration against information acquired under our obligations relating to Anti Money Laundering/Know Your Client ("AML/KYC") regulations and additional client declarations for tax purposes in accordance with Article 11 (2)(b). Accordingly, we recommend that the proposal be revised to provide that a CFI can rely on the information provided by clients, unless the CFI has actual knowledge, based on information collected in the ordinary course of business (such as through meeting AML/KYC requirements), that the information provided by the client is incorrect. We would also seek that the risk assessments for credit or fraud risk mentioned in Article 10 (1)(b) are clearly stipulated in guidance for the CFI.

With respect to the requirement for a CFI to indicate if they are aware of the possible existence of a financial arrangement, we would ask that the circumstances in which a CFI would be expected to identify such an arrangement is limited to actual knowledge and information received in undertaking its ordinary activities when acting as a CFI, and not include any information that may have been provided to a separate line of business within the same legal entity or affiliated/related parties. The custodian business may not have (or be permitted to have) information regarding arrangements that may be considered pertinent to the reporting in cases where that information is provided to other lines of businesses or affiliated/related

parties, and it is not reasonable to require custodians to be aware of information that they cannot access.

In addition, without further clarification of what is expected to be understood by “possible existence” of a financial arrangement, a CFI may not be able to offer tax relief services unless the investor can declare they will only hold assets, to avoid any possibility of falling in scope of this measure. We would recommend further defining this to enable a CFI to accurately and fully determine if they have met the requirement. As may be noted by the above, it is critical for terms and concepts to be defined at the level of the directive to allow a CFI a level of certainty that they are compliant and adhering to the standards required of them, as well as to ensure those definitions, terms and concepts are common across the Member States in order to avoid divergence in procedure from one Member State to another.

We also propose that with respect to Article 11 (2) (d), the threshold for verifying the possible existence of financial arrangements (where “the dividend paid to the registered owner for each group of identical shares held does not exceed EUR 1000”) is removed or alternatively made optional. It is operationally burdensome to manage such a threshold, particularly where a CFI will not have visibility into whether the threshold has been met.

With respect to the declaration by the registered owner, the proposal is unclear as to whether it must be collected on a per payment basis or if this will be a declaration valid for a period of time. If the expectation is that this is collected and verified on a per payment basis, it will be practically impossible for financial intermediaries to comply. Financial intermediaries handle millions of income distribution payments, and it is not practical to collect, review and verify the information for each client prior to each payment. We suggest that the declaration be collected on an annual basis and for investors to provide a confirmation to the financial intermediary at the start of the year that the investor hast not engaged, and will not engage, in a financial arrangement for the purpose of a tax benefit (amendment to Article 11 (1) (b)). On a global basis, it is a standard practice for such declarations to be valid for a specified period of time (typically, at least a year) and it is important to note that it is typically only within the knowledge of the investor themselves whether they have entered into a financial arrangement which affects their eligibility to withholding tax relief. In addition, there should be a consistent template used by all Member States for the self-declaration. We recommend that the EC set forth minimum standards for a self-declaration in an annex to the proposal and require Member States to follow the standards set forth in the annex (similar to the approach taken with respect to the eTRC).

Reporting for non-CFI

Article 10 (3) suggests that end investors for which at least one custodian in the custody chain is not registered can still benefit from the procedures, providing that a CFI provides reporting on behalf the uncertified custodian. It will be important that there is full certainty as to how this reporting should be provided, and that the reporting modalities do not differ by Member State. We would also seek clarification of the liability imposed on the CFI reporting the information from the non-CFI given there is limited verification of information that may be possible, due to the indirect nature of the client relationship with the end investor.

Areas for potential divergence

We note that the proposal offers a certain level of flexibility, but this has potential to lead to independent requirements by each Member State with respect to the reporting obligation. We request that the proposal be revised to clarify that Member States may not add further reporting requirements. Where possible, we would seek that Member States utilize the same templates for documentation including the declaration and the required reporting, as well as harmonized definitions for terms and concepts (as recommended above). Introducing different requirements in either of these areas will increase complexity and risk for ensuring correct reporting and verification. In particular we would seek a single declaration format to be used with clear guidance on what information must be verified (limiting this to information that is available to the verifying party), and the due diligence procedure expected to be followed, preventing a need for up to 27 different declarations and verification procedures.

Further, it is equally important that harmonization is achieved in the implementing acts relating to (i) issuance of eTRCs (Article 4), (ii) reporting obligations of intermediaries (Article 9), and (iii) the QR request (Article 13). Accordingly, we recommend that Member States consider introducing standard forms and templates for both RAS and QR.

Reporting

According to Article 9, a CFI will be required to report information as listed in Annex II to the competent authority as soon as possible after the record date. Where a transaction is pending settlement, the reporting for that transaction will take place as soon as possible after settlement, but if by record date +20 days it remains pending, then it is necessary to report "on the 20th day and within the next 5 following days", indicating what remains pending for settlement. The requirement suggests there will be the need for multiple daily reports to be submitted, with running adjustments for settlement. This requirement will prove extremely burdensome operationally for both CFI and the competent authorities, due to very high volumes of reporting being sent on a daily basis, particularly during the first six months of the year when most European companies pay dividends.

The AGC suggests the EC consider amending the proposal to require reporting at a set date for the distributions whose record date occurs in a month, allowing sufficient time for failing transactions to be reviewed and reconciled, and allowing for more accurate reporting the first

time with fewer or no adjustment reports required. The preference of the AGC for such reporting has always been on an annual basis, but we understand the proposal requires reporting to be performed sooner as part of the RAS and QR processes. Therefore, we would suggest, for example, the proposal could require reporting on a quarterly basis. This will allow additional time for failing trades to settle and reconciliations to take place, as this can sometimes take a number of weeks and, in some cases, months. Amending the proposal in this manner would also benefit tax administrations, which would otherwise be required to process a large volume of daily adjustment reports.

We request clarifying guidance on the methodology that should be used to calculate the holding period (the proposed two days).

The proposal states that, “A common EU-wide reporting standard would save compliance and related technology costs for financial intermediaries operating across borders as they would be faced with one reporting standard across the whole EU, instead of a patchwork of different reporting requirements”. In light of the above comments regarding the potential levels of reporting that may be expected, it may be beneficial for the EC to develop a single portal (both for the reporting and for eTRC requests) with Member States for the reporting to be delivered and received through, whilst ensuring that data is protected in line with GDPR.

AGC also requests a removal of penalty to a CFI for sending high volumes of adjustment reports as the nature of trading means there are likely to be numerous corrections when reporting is in close proximity to the record date.

We would also like to seek clarity on Annex II, section D for the section titled “Relevant dates”. This requires the inclusion of the “ex-dividend date, record date, settlement date (if done or a mark in case not yet produced), payment date, coupon date.” Specifically, AGC seeks clarification of what would be sought under the field for “settlement date”? Investors trade regularly so is the expectation that the last purchase trade settlement date is included, notwithstanding that it would be unlikely to reflect the full position?

Anti-abuse measures

The proposal puts forward two reporting requirements that are aimed at helping to combat withholding tax abuse, (i) information about the holding period of underlying securities and (ii) information about financial arrangements linked to the securities for which the taxpayer is requesting relief.

With respect to the holding period, the proposal specifically mandates that Member States do not grant relief for shares purchased within two days of ex-date. AGC requests modification to this rule, highlighting this approach does not explicitly eliminate tax avoidance and could result in the loss of benefits for a claimant in a market of investment which does not have an operable reclaim procedure.

Among the problems that this exclusion will create are:

- Legitimate purchasers, including those whose trades settle on or before record date, will be unjustifiably disadvantaged.
- In theory an investor's share position would be subject to different processing for tax relief – partly under RAS or QR where the holding period is met, and partly under standard refund for the excluded position bought within two days. In reality financial intermediaries may not be able to support this model and will exclude the entire position from RAS because it may not be possible to adjust positions with the withholding agent so close to the ex-date and in the absence of QR, financial intermediaries will default to sending a standard refund claim to the tax administration.
- There is a potential for an impact on trading two days before ex-date, as trades executed three days before ex-date will have a different status from trades executed two days from ex-date.

Member State tax administrations have taken different approaches to tackling this issue already by requiring claimants to own the eligible position for a significant period of time prior to and after the record date to eliminate tax abusive trading strategies. It would be beneficial if all were to address this in the same manner which would allow certainty for all cross-border investors to the treatment of market claims.

With respect to the term "financial arrangements", as noted in the proposal, the definition is very broad. There is a need for a more granular, and more operational definition so that all parties, including the custodian and its clients, can be certain as to what activity falls within the FASTER relief procedures and what doesn't. In addition, the current exclusion of positions with financial arrangements would potentially exclude a very substantial number of positions from the FASTER relief processes.

Article 10 (3)(b) creates the possibility for Member States to exclude securities positions that can benefit from an exemption from the FASTER relief procedures. It should be expected that Member States use this possibility only very rarely, given that many investors who can benefit from an exemption, such as supranationals, are entities of high repute. It would be useful to have a better understanding of the circumstances in which Member States would use this possibility. For example, the EC may wish to consider setting standards for when an exclusion might be appropriate.

Registration

The proposal requires EU financial intermediaries to register with each Member State. This seems out of step with other areas in European financial services whereby a passporting regime is available to provide a simpler and faster route to registration and providing services cross border. The AGC recommends that the EC develop a common registration portal, with a single sign-on across all Member States and linked to all registration guidance.

The proposal requires mandatory registration by large institutions. However, it may be the case that for commercial reasons, an institution chooses not to offer tax services in a certain market and therefore does not wish to register as a CFI for the provision of relief to their clients. It should be possible for these institutions, when registered in a common portal, to select those markets where they wish to provide tax services. Furthermore, we request clarification on which legal entity is required to register on behalf of an institution. For example, are foreign branches required to register? If so, where should foreign branches register?

In addition, we request clarity regarding registration for third-country CFIs (such as U.S. and UK custodians). The proposal includes a requirement that third-country CFIs should be governed by equivalent legislation to the requirements for EU financial intermediaries, but this requirement would benefit from a clear definition of equivalent legislation.

Additional comments

We do believe it may be helpful for a broader clarification of what is in and out of scope of the proposal to be shared. For example, is it a requirement that a CFI must submit the request for a standard reclaim, given that Article 15 requires the provision of information in accordance with the obligations of Article 9?

Domestic investors do not fall within the scope of the proposal. However, it may be the case that elements of the proposal, such as the eTRC and the relief at source procedure, would also be of benefit to domestic investors. It would be appropriate to investigate and to develop synergies with the processes applicable to domestic investors.

As mentioned above, in its current form, the proposal will exclude many positions from the FASTER relief procedures, including positions that may currently benefit from RAS and QR procedures. Excluded positions will include positions subject to financial arrangements, positions traded within two days of ex-date, positions for which the investor can benefit from an exemption, and positions for which a party in the custody chain has not provided reporting.

Accordingly, it will be very important that the legacy reclaim procedures function appropriately and in all Member States. To the greatest extent possible, Member States should improve their legacy reclaim arrangements, by incorporating the eTRC, and elements from the FASTER relief procedures (the declaration by the beneficial owner), in these arrangements.

In addition, Article 16 of the proposal indicates that CFIs may be subject to civil liability if the CFI "does not comply, intentionally or negligently" with their obligations under Articles 9 through 13. We recommend that "or negligently" should be eliminated from the proposal; CFIs should only be subject to civil liability for intentional non-compliance with their obligations under the proposal. Should a CFI be found intentionally negligent, we would request that the consequences of such a finding be limited to a scale of penalties and fines, and suspension or de-registration of the CFI in extreme circumstances. Similar to the Finnish TRACE regime, the possibility to re-register should be considered once conditions that led to de-registration have been addressed.

Finally, we would like to reiterate our view that the proposal would benefit from implementation in phases and that CFIs be provided with a minimum of 24 months from the date that the final technical guidance (reporting and relief procedures) is adopted by Member States before it must be implemented by CFIs.

The AGC Tax Committee greatly appreciates the opportunity to provide feedback on this important initiative and would be happy to meet with you to discuss our feedback or to provide any additional information that you may need.

Sincerely yours on behalf of the Association,

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