Faster and Safer Relief of Excess Withholding Taxes

2023/0187(CNS) - 19/06/2023 - Legislative proposal

PURPOSE: to make withholding tax procedures in the EU more efficient and secure for investors, financial intermediaries and Member State tax administrations.

PROPOSED ACT: Council Directive.

ROLE OF THE EUROPEAN PARLIAMENT: the Council adopts the act after consulting the European Parliament but without being obliged to follow its opinion.

BACKGROUND: ensuring fair taxation in the internal market and the good functioning of the Capital Markets Union (CMU) are political priorities for the European Union (EU). In this context, removing obstacles to cross-border investment, while combating tax fraud and abuse is critical.

In the EU, investors may be generally obliged to pay tax twice on the income they receive from holding securities (namely dividends on holdings of equities and interest on holdings of bonds) in a cross-border context.

First, taxes may be levied in the country of the issuer of the securities (the source country) in the form of a tax withheld from the gross securities income, (withholding tax (WHT)). Secondly, taxes may be levied in the investors country of residence (the residence country) in the form of income tax.

To avoid double taxation, many EU Member States have signed double taxation treaties, which avoid the same individual or company being taxed twice. These treaties allow a cross-border investor to submit a refund claim for any excess tax paid in another Member State.

The problem is that these refund procedures are often lengthy, costly and cumbersome, causing frustration for investors and discouraging cross-border investment within and into the EU. Currently, the withholding tax procedures applied in each Member State are very different. Some Member States have experienced large-scale tax abuse schemes known as Cum/Ex and Cum/Cum. Cum/Ex schemes work as fraudulent multiple reclaim schemes when entitled to a single reclaim.

In order to strengthen Member States ability to prevent and fight against potential fraud or abuse, it is necessary to put in place a common framework for the relief of excess withholding taxes on cross-border investments in securities that is resilient to a risk of tax fraud or abuse.

CONTENT: the aim of this Commission proposal is to make EU withholding tax procedures more efficient, while strengthening them against the risk of tax fraud and abuse.

In particular, the proposal lays down rules on the issuance of a digital tax residence certificate by Member States and the procedure to relieve any excess withholding tax that can be withheld by a Member State on dividends from publicly traded shares and, where applicable, interest from publicly traded bonds paid to registered owners who are resident for tax purposes outside that Member State.

The following actions intend to make life easier for investors, financial intermediaries and national tax authorities:

A common EU digital tax residence certificate (eTRC) will be introduced by all Member States and will make withholding tax relief procedures faster and more efficient. For example, investors with a diversified portfolio in the EU will need only one digital tax residence certificate to reclaim several refunds during the same calendar year. The digital tax residence certificate should be issued within one working day after the submission of a request. At present, most Member States still rely on paper-based procedures.

Two fast-track procedures complementing the existing standard refund procedure: a relief at source procedure and a quick refund system, which 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.

- under the relief at source procedure, the tax rate applied at the time of payment of dividends or interest is directly based on the applicable rules of the double taxation treaty provisions;

- under the quick refund procedure, the initial payment is made taking into account the withholding tax rate of the Member State where the dividends or interest is paid, but the refund for any overpaid taxes is granted within 50 days from the date of payment.

These standardised procedures are estimated to save investors around EUR 5.17 billion per year.

A standardised reporting obligation will provide national tax administrations with the necessary tools to check eligibility for the reduced rate and to detect potential abuse. Certified financial intermediaries will have to report the payment of dividends or interest to the relevant tax administration so that the latter can trace the transaction. In particular, large EU financial intermediaries will be required to join a national register of certified financial intermediaries. This register will also be open to non-EU and smaller EU financial intermediaries on a voluntary basis.

Taxpayers investing in the EU through certified financial intermediaries will benefit from fast-track withholding tax procedures and avoid double taxation on dividend payments. The more financial intermediaries register, the easier it will be for tax authorities to process refund requests, regardless of the procedure used.

Budgetary implications

The main budgetary implications of the initiative for the Commission include implementing the electronic tax residence certificate and establishing the formats and communication channels to be used by financial intermediaries to report to the national tax authorities.