EBF TAX BLUEPRINT

Recommendations for a fairer and more efficient EU tax framework

EBF
European Banking Federation

FOREWORD

International tax rules have been significantly amended over the past few years to address base erosion and profit shifting. To ensure a fairer and more efficient tax framework, they will need to be further adapted to the globalisation of business and the digitalisation of economic activities.

In parallel, the tax transparency agenda has resulted in the development of a global automatic exchange of financial account information.

As global economy recovers from the Covid-19 pandemic, governments will need resources. Given the continued adaptation of tax rules and increased transparency, the push to reinforce the fight against tax evasion will be greater than ever. Expressly, the governments will need to address the potential erosion of the corporate tax base and the flow of funds that are moved to offshore accounts and shell companies.

Banks will be requested to play an important role in supporting these efforts both as taxpayers contributing to public finance and as gatekeepers of the financial system.

The European Banking Federation (EBF), which represents European banks, supports the Commission's Tax Action Plan of July 2020 which aims to develop a fairer and more efficient tax framework. The EBF also backs the efforts to remove tax obstacles in the Single Market outlined by the Capital Markets Union (CMU) Action Plan of September 2020.

As gatekeepers of the financial system, banks play a pivotal role in tax procedures applicable to financial accounts and investment income payments.

- Banks provide a significant contribution to the public authorities' fight against tax evasion through conducting due diligence and complying with reporting requirements. They act as Reporting Financial Institutions under FATCA, the OECD Common Reporting Standard (CRS) and the EU Directive on Administrative Cooperation (DAC). Banks have made significant investments to implement and comply with relevant standards and regulations. Such obligations must be efficient, well-calibrated, clearly framed and coordinated. Any new rules or amendments must be introduced with sufficient lead time to enable banks to meet their legal obligations. Banks are committed to compliance requirements provided these remain proportionate.

- The complexities of withholding tax relief and refund procedures remain a major obstacle to cross-border investment across the continent. The EU Code of Conduct on withholding tax procedures must be further harmonised and standardised. It should also leverage international tax developments, such as the OECD TRACE Implementation Package, to put in place an EU withholding tax relief at source system.

Banks as taxpayers are facing the VAT and corporate taxes, and potentially a financial transaction tax (FTT) and a digital tax which might significantly affect their P&L.

Banks' ability to finance the European economy and compete globally should not be impaired by undue strains on banks' cost structure brought on by excessive taxes.

- Taxes, including the "hidden VAT cost" for banks and insurance companies, have a major impact on banking groups' profitability in Europe. The impact of the VAT treatment of financial services should be urgently considered given that the current regime creates distortion and legal uncertainty.
- Distortions and other undue tax disincentives should be removed. The EBF believes that the benefits of the Capital Markets Union can only be unlocked if the capital markets within the EU are free of policies like the financial transaction tax (FTT), which would limit or reduce their liquidity and efficiency.
- EU initiatives in the field of corporate taxation should be aligned with proposals discussed at the OECD level to foster a genuine level playing field on base erosion and profit shifting.
- The specifics of the banking sector must be taken into consideration as the sector is already highly regulated. Banks are subject to capital, leverage and liquidity rules and standards which obviate many of the risks identified concerning base erosion and profit shifting.
- Corporate tax rules are in the process of being adapted to the globalization of business and the digitalization of economic activities, resulting in frictions between bank's capital requirements and corporate income tax rules. Corporate taxation should be adapted to banks' specificities and regulations and appropriate carve-outs should be provided.

The European banking sector is a key contributor to public budgets and is increasingly requested to play an auxiliary role to the tax authorities. The recommendations and proposals set out in this Blueprint aim to ensure tax certainty and proportionality, to strengthen the ability of European banks to finance the EU's economy and to compete globally while enhancing the efficiency and integration of the EU internal market. A modernized EU tax framework is essential to achieving a more integrated Internal Market. The EBF stands ready to discuss the proposals outlined in this Blueprint and related challenges with policymakers.

Wim Mijs

CEO of European Banking Federation

EXECUTIVE SUMMARY

This Blueprint puts forward a set of 10 policy recommendations around four main pillars:

Tax reporting

Withholding tax procedures

VAT and other indirect taxes

Corporate income tax

The 1st pillar of the Blueprint targets the necessity for a more harmonised approach in reporting tax-related information and combatting tax evasion. Further alignment between FATCA, the CRS and DAC2, would reinforce the global approach to the tax reporting framework and would ensure a level playing field and the effectiveness of the fight against tax evasion. Such alignment would also provide a practical solution to the pending issue of Accidental Americans.

When it comes to reporting, banks can only provide tax authorities with indicators. They do not assess or prejudge the tax liability of these income payments according to the tax law applicable in the residence country. This liability can only be established by the tax authorities of the residence country after assessment, in the light of the domestic tax law, of the data reported, and after verification of the related tax returns. Moreover, banks should not be asked to carry out further investigations that are the sole responsibility of the tax authorities.

In addition to the legislative framework, DAC 6 guidance is urgently needed in order to clarify and coordinate how the rules should be applied in practice and to allow Financial Institutions and other stakeholders to determine whether they qualify as an intermediary, as at present domestic transposition laws and guidance may vary on a technical level.

Technological development and the rise of crypto-assets and e-money may soon lead to an extension of the scope of reporting requirements to virtual assets. The extension of DAC 2 to virtual assets service providers should be based on the general concept of 'same services, same risks, same rules'.

The 2nd pilar addresses the existing complexities of withholding tax procedures. EU Governments should take steps to implement a standardised and harmonised system for tax relief at source and simplified tax refund procedures.

An EU-wide common and standardized system for withholding tax relief at source has the potential to reconcile the interest of the Single Market by removing tax obstacles which are tantamount to double taxation and the interest of public finance by ensuring that treaty benefits are properly granted.

The 3rd pillar highlights the need for more legal certainty and enhanced neutrality of the VAT regime applicable to Financial Institutions.

Due to outdated VAT rules applicable to financial services, there is a high level of legal uncertainty regarding how to treat financial services within an increased digitalised environment. Moreover, the rules are interpreted and applied inconsistently by Member States, resulting in distorted competition within the EU.

Non-neutrality arises from the VAT exemption regime that is applied to financial services. Exemption means that most services provided by Financial Institutions are not subject to VAT. VAT incurred on expenses by Financial Institutions is, however, only recoverable to the extent that the services supplied are in turn subject to VAT.

Another potential cause for distortion of competition is the Financial Transactions Tax (FTT), which lacks global support and could lead to numerous uncoordinated approaches to taxing financial transactions, particularly where Financial Institutions are outside of the FTT-zone. An FTT would distort asset markets, decrease liquidity and increase transaction costs.

The 4th pillar highlights issues in relation to the initiative on a EU Digital Levy.

Banks' operating models and applicable regulations ensure that banks set up a physical presence and hence have a taxable nexus where they face customers. The existing corporate tax framework therefore adequately captures profits earned by banks.

An EU Digital levy proposal should consistently reflect this and provide for an equal carve-out for banking services as is provided for in the OECD pillar 1 blueprint.

The aforementioned pillars and related policy recommendations are elaborated in more detail in the document below.

POLICY RECOMMENDATIONS

#1

COMPLY with well calibrated tax reporting

RECOMMENDATION 1:

Further harmonise compliance obligations under FATCA, CRS and DAC2 in order to level the playing field globally and provide a permanent solution to the issue of Accidental Americans under FATCA and IGAs so that banks do no longer face the risk of being considered FATCA non-compliant when reporting US persons without a US TIN

RECOMMENDATION 2:

Adopt a more proportionate, principle-based approach to the automatic exchange of financial account information under FATCA, CRS and DAC 2 to allow tax authorities to focus on material risks of tax fraud; reporting shall remain limited to data available to banks and that data shall serve as an indicator, as opposed to a proof, of tax liability

RECOMMENDATION 3:

Provide detailed DAC 6 guidance to ensure across the EU a consistent interpretation of the definitions of intermediaries and hallmarks

RECOMMENDATION 4:

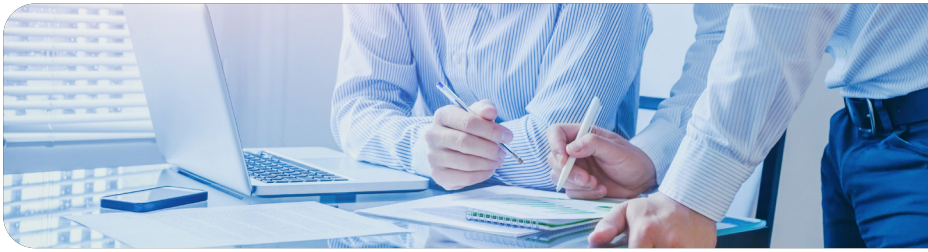
Extend the scope of CRS/DAC to include e-money, virtual assets and cryptocurrencies (DAC8) based on the general concept of "same services, same risks, same rules" with no additional requirements for Financial Institutions, and align the definitional framework to the AML framework, the Digital Finance Strategy and the proposed Regulation on Markets In Crypto-Assets (MICA)

#2

SIMPLIFY withholding tax procedures

RECOMMENDATION 5:

Create common pan European definitions and standards for withholding tax processing and build a workable EU withholding tax relief at source system while minimising the burden of paper-based tax processing, alleviating the continuing impacts of COVID 19 and preventing tax fraud



#3

NEUTRALISE VAT distortions and other undue tax disincentives

VAT ON FINANCIAL SERVICES

RECOMMENDATION 6:

Increase legal certainty and avoid distortions of competition by making the VAT rules for financial services fit for the digital age and new entrants

RECOMMENDATION 7:

Increase VAT neutrality for financial services to remove barriers to economic efficiency

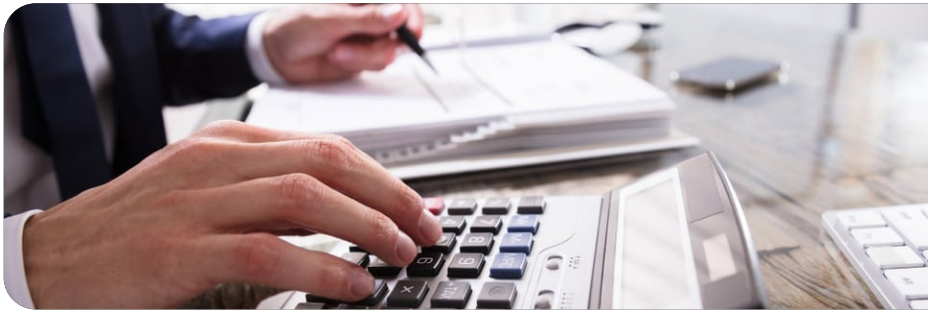
#4

RING-FENCE banking activities from other highly digitalised businesses when designing new corporate tax rules

FINANCIAL TRANSACTIONS TAX

RECOMMENDATION 8:

Refrain from introducing an EU FTT, which would limit the efficiency and liquidity of the derivatives, bonds and stock markets in the EU and would reduce the returns for savers



RECOMMENDATION 9:

EU initiatives in the field of corporate taxation should take into consideration banks' operating models and applicable regulations which ensure that banks set up a physical presence and hence have a taxable nexus where they face customers

RECOMMENDATION 10:

There is no ground for bringing financial services into the scope of an EU Digital Tax

#1

COMPLY
with well calibrated tax reporting

Our recommendations

1

Further harmonise compliance obligations under FATCA, CRS and DAC2 in order to level the playing field globally and provide a permanent solution to the issue of Accidental Americans under FATCA and IGAs so that banks do no longer face the risk of being considered FATCA non-compliant when reporting US persons without a US TIN

2

Adopt a more proportionate, principle-based approach to the automatic exchange of financial account information under FATCA, CRS and DAC 2 to allow tax authorities to focus on material risks of tax fraud; reporting shall remain limited to data available to banks and that data shall serve as an indicator, as opposed to a proof, of tax liability

3

Provide detailed DAC 6 guidance to ensure across the EU a consistent interpretation of the definitions of intermediaries and hallmarks

4

Extend the scope of CRS/DAC to include e-money, virtual assets and cryptocurrencies (DAC8) based on the general concept of "same services, same risks, same rules" with no additional requirements for Financial Institutions, and align the definitional framework to the AML framework, the Digital Finance Strategy and the proposed Regulation on Markets In Crypto-Assets (MICA)

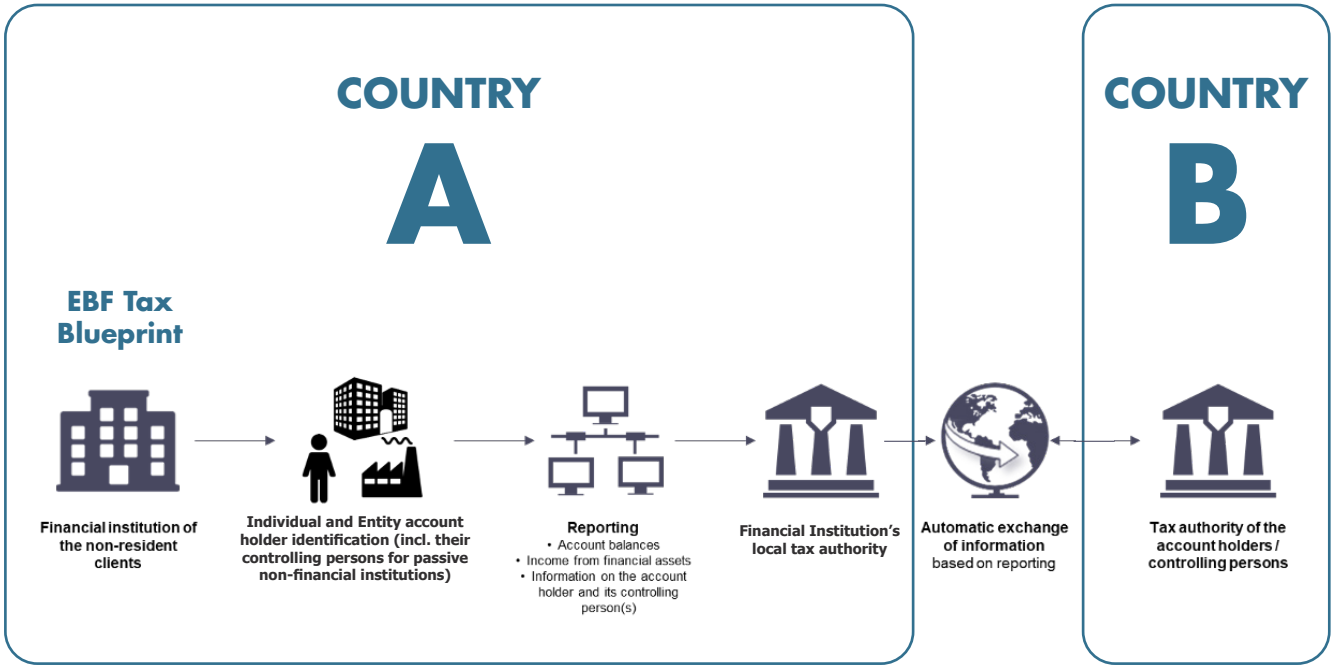
With their essential role as gatekeepers, banks control the access of customers to the financial system, in their capacity as "obliged entities" under Anti-Money Laundering rules and in parallel as "Reporting Financial Institutions" in the tax reporting framework. In 2010, which was a turning point in the history of automatic exchange of financial account information for tax purposes, the US enacted FATCA, which stands for "Foreign Account Tax Compliance Act". FATCA is aimed at tracking US taxpayers who could evade their tax obligations in their home country either through offshore bank accounts held with Foreign Financial Institutions or through investments in shelf-companies set-up outside the USA ("Non-Financial Foreign Entities" i.e. entities that are not classified as Financial Institutions). The FATCA Regulation has been complemented by subsequent Inter-Governmental Agreements (IGAs) allowing its implementation in partner jurisdictions. Later, FATCA emerged as the incubator and catalyst for the development of an international and European tax reporting system and served as a model for the OECD "Common Reporting Standard" (CRS) and the EU Revised Directive on Administrative Cooperation (DAC2), which is its translation in EU law. Through their compliance with FATCA, the CRS and DAC2, Financial Institutions contribute to the fight against tax evasion.

Financial Institutions' tax reporting obligations

Apply due diligence procedures to identify in its client base direct and indirect accountholders who are resident in a partner or participating jurisdiction:

- Identify direct accountholders who are individual persons or entities and establish their residence country; and
- Identify non-financial foreign entities (that are not classified as Financial Institutions), regardless of their legal form (including trusts and foundations) and apply a look-trough approach for those entities which are passive entities (not engaged in a non-financial business) in order to identify individuals who exercise a controlling influence on these entities ("controlling persons").

Report account information (personal data including name, address, tax residence and Tax Identification Number – TIN, and financial information including account balance and all investment income including sales proceeds), directly or indirectly (mostly via the tax authorities of the Financial Institution) to the tax authorities of the jurisdictions where the clients or controlling persons are resident.



1 Further harmonise compliance obligations under FATCA, CRS and DAC2

While a review of the CRS is examined by the OECD, further harmonisation between FATCA, the CRS and DAC2 would reinforce the global approach to the tax reporting framework and would ensure a level playing field and the effectiveness of the fight against tax evasion. Such alignment would provide a practical solution to the pending issue of Accidental Americans.

Currently, FATCA is not fully harmonised with the CRS which has not been adopted by the US. As a result, there are divergences between FATCA- and CRS-due diligence and reporting provisions, in particular as they apply to existing accounts (as opposed to on-boarding procedures applicable to new accounts).

Under the CRS, Financial Institutions may validly determine the status of a pre-existing accountholder based on the AML/KYC documentation absent a valid self-certification. Reporting only takes place in the presence of express indicia relating to a "reportable jurisdiction". If the TIN is missing, the Financial Institution reports the date and place of birth (if held) or beneficiaries.

FATCA and related Intergovernmental Agreements (IGAs) require Financial Institutions to review their client base using specific US indicia. When an indicium is found, the accountholder is presumed to be a US reportable accountholder, unless information (self-certification and corroborating evidence) is received by the Financial Institution that the accountholder is not a US reportable accountholder. It is mandatory to include a US Tax Identification Number (TIN) in the reporting of US reportable accounts. Failure to report TINs for pre-existing accounts may result in a bank being considered as in significant non-compliance with FATCA and IGAs which is, to our view, an incorrect and disproportionate outcome, considering (1) the consequences potentially attached to such status under US law and its unilateral administration by the US Internal Revenue Service (IRS) as well as (2) the limited reciprocity granted by the United States under the IGAs. The FATCA IGA requires that Financial Institutions request TINs from reportable US pre-existing account holders. If account holders do not provide a TIN that does not mean the Financial Institution is not in compliance with its obligations under the IGA. Further, it is noted that in certain circumstances FATCA IGAs require "default" reporting of accountholders even in the absence of express indicia – such as entity account holders presumed to be reportable under FATCA and recalcitrant new account holder. Alternatively, due to the broadness of the indicia, certain non- US persons are reported due to indicia such as a US phone number and such persons simply do not have a US TIN. This causes non-US accountholders, who do not have US TINs, to be reported without a US TIN.

Since the implementation of FATCA, Financial Institutions in Europe have striven to collect US TINs from their customers with US indicia in full accordance with the IGA. However, a significant number of clients have failed to produce US TINs. One of the reasons for this may be the fact that default reporting under FATCA results in quite a significant number of false positives. Further, other reported accountholders are dual nationals who have been granted automatic citizenship under US nationality law because they were born in the US, but they left US as children, do not have a US passport, live outside the US and do not consider themselves US citizens (so-called "Accidental Americans"), while others may have died (dormant accounts). They are facing burdensome administrative requirements resulting from the fact that the US tax duties and obligations on worldwide income are imposed on all US persons, i.e. all US resident individuals and all US citizens.

An EBF survey updated in March 2021 on individual accounts held with European banks may give an idea of the number and proportion of EU residents who could fall under the concept of Accidental Americans. This survey is based on a sample of 458 banks in 7 EU Member States: the percentage of individual accounts in the client base that are held by presumed US persons may be estimated at approximately 0,13% ; and the percentage of individual accounts in European banks' client bases that are held by presumed US persons who have never presented their bank with a US TIN is estimated at approximately 0,067%.

In 2017, the US Treasury provided a transitional relief according to which Foreign Financial Institutions in Model 1 IGA jurisdictions would not be in significant non-compliance with an applicable IGA solely as a result of a failure to report US TINs for pre-existing accounts, provided the Financial Institution reports the accountholder's date of birth, makes annual requests for the TIN, and searches its electronic records for missing US TINs before reporting information. Such transitional relief lapsed at the end of 2019.

We recommend the US to better align the FATCA due diligence and reporting requirements to the CRS, which notably provides for the reporting of residence country (including multiple jurisdictions) based on express indicia.

For pre-existing individual accounts, we recommend the US to provide for a permanent widening of the above transitional relief for missing US TINs and either:

- broader codes that align with the situations under a FATCA IGA that could cause an account holder to be reported; or

- codes specific to the types of indicia present – e.g. a specific code for US place of birth.

As regards pre-existing entity accounts, in the absence of a valid self-certification, reporting under FATCA should be limited to occurrences where US indicia have been identified with respect to one or more beneficiaries, in line with corresponding CRS requirements.

2 Adopt a more proportionate, principle-based approach to the automatic exchange of financial account information

In the on-going OECD review of the CRS, which will be reflected in the DAC, the overarching objectives and fundamentals of the automatic exchange of information should be kept in mind.

The information reported by banks under CRS/DAC2 provides the tax authorities in the home country with information about income payments made to taxpayers who are resident in that country.

Banks can only provide tax authorities with indicators. They do not assess or prejudge the tax liability of these income payments according to the tax law applicable in the residence country. This liability can only be established by the tax authorities of the residence country after assessment, in the light of the domestic tax law, of the data reported, and after verification of the related tax returns.

Banks can only report the information that is readily available to them. If they need more granular information, tax authorities can use other tools than CRS/DAC2 reporting. Banks should not be asked to carry out further investigations that are the sole responsibility of the tax authorities. Banks are transparent and are willing to give tax authorities information that is readily available to help against tax evasion and tax fraud. However, every request by tax authorities must be preceded by a check between the tax administrations and the European supervisory authorities to avoid duplication of communications. In this context, it is worth reminding that the holding of a bank account in another jurisdiction is in many occurrences a necessity in the current European context and should not be systematically construed as an indicium of tax fraud or tax evasion by tax authorities. Disproportionate investigations may constitute a barrier to the free provision of (financial) services and the free flow of capital across the EU and may conflict with the GDPR.

3 Provide detailed DAC 6 guidance

It is of paramount importance that the EU Member State laws and guidance implementing Council Directive 2018/822/EU (DAC 6 rules) are harmonised. A consistent DAC 6 regime would be of benefit to tax authorities, policymakers and industry.

For tax authorities and policymakers, a harmonised regime ensures each EU Member State is collecting and sharing comparable data. Any material divergence in the definition or interpretation of what is a reportable arrangement or who has an obligation to report will heighten the risk of data inconsistency. It is noted that the directive focuses on cross-border transactions and the automatic, cross-border exchange of information. Therefore, when drafting DAC 6 rules and guidance, tax authorities and policymakers must be cognisant of the fact their interpretation will not only affect the quality and type of data they receive, but also the data they share with other jurisdictions.

For industry, particularly multinational businesses operating across multiple jurisdictions, a consistent and harmonised set of DAC 6 rules minimises the cost of compliance when doing business across multiple EU Member States.

The EBF has conducted a survey to track qualitative divergence amongst EU Member States across key DAC 6 definitions or concepts. While it is encouraging that very few EU Member States have introduced additional hallmarks or expanded the scope of covered taxes[1], it is noted:

- Some jurisdictions have published white lists;
- Many (but not all) jurisdictions have provided guidance that the main benefit test is not met where a tax advantage conferred is consistent with law and policy; and
- Many jurisdictions have provided helpful guidance regarding when a "service provider" Intermediary might be considered to have "reason to know" he/she has provided relevant services for a reportable arrangement; in this respect, the EBF would recommend an alignment of guidance on the definition of service provider under paragraph 52 of the OECD Model Mandatory Disclosure Rules for CRS Avoidance. Arrangements and Opaque Offshore Structures would generally not capture Financial Institutions when carrying out routine banking transactions (e.g. custody, opening of a bank account) because the nature of their involvement and the information readily available to them would typically not meet the "reasonably be expected to know" standard.

While most of the clarifications provided by tax authorities are welcome, it remains troubling that some jurisdictions remain silent on key concepts and there is a lack of clear consensus amongst Member States on key items of guidance, such as the interpretation of the main benefit test. This is particularly worrying for banks, which tend to operate across multiple jurisdictions via branch networks. Due to the way reporting obligations are defined under DAC 6, branches are simultaneously subject to the DAC 6 rules of both their branch and head office jurisdictions. This exacerbates uncertainty where jurisdictions have an inconsistent implementation of DAC 6.

Lastly, it is unclear whether an Intermediary may be barred from reporting due to the operation of legal professional privilege or other similar concepts. Member States have varying views on whether the concept of privilege applies only to advisors who are lawyers or whether this concept should also be extended to accountants. The fact that some jurisdictions – e.g. France – have also extended this concept to include banking secrecy, while others have not, creates a complex matrix of responsibility for Financial Institutions to track.

[1] It is noted that this exercise has been limited to a high level analysis, and has not examined differences in the interpretation of hallmarks, the main benefit test or what criteria causes an arrangement to be considered "cross-border". If such an in-depth analysis were to be included, further differences in interpretation would be identified.

4 Extend the scope of CRS/DAC to include e-money, virtual assets and cryptocurrencies based on the general concept of "same services, same risks, same rules"

Given the rise of crypto-assets and e-money, an extension of the scope of the tax reporting framework to e-money, virtual assets and crypto-currencies is currently under examination by the EU and the OECD. The OECD has already carried out extensive work on that topic and should be in the driving seat to ensure a global level playing field. In the EU this extension will be transposed in EU law via an additional revision of the DAC which is already referred to as DAC 8.

The starting point must be a uniform framework, which should be aligned to the Anti-Money Laundering (AML) framework, including guidance on Virtual Assets (VA) and Virtual Asset Service Providers (VASP) provided by the Financial Action Task Force (FATF) and the corresponding definitional framework set out by the EU AML Directives, and the underlying definitions provided in the context of the Commission's Digital Finance Strategy and the proposed Regulation on Markets In Crypto-Assets (MICA). The AML framework already contains useful definitions introduced by the AMLD 5 and will be overhauled in 2021 by legislative proposals which will most probably introduce additional definitions.

The extension of DAC 2 to VASP should be based on the general concept of 'same services, same risks, same rules'. For example, where the custody and administration of crypto-assets is similar to the concept of holding financial assets for the account of others, the reporting obligation of the VASP should be aligned by DAC 8 to the obligation which is currently imposed on Custodial Institutions under DAC 2. The scope of DAC 8 should also include the conversion into fiat currency by a VASP of so-called "cold wallets" that are held without the involvement of a VASP.

Operations that do not have the same functionalities as a financial account or as "classic" money, where it would be difficult to ask for a self-certification, should be left out of scope or benefit from an explicit carve-out. This is the case of electronic currency solutions which are developed by banks and operated in specific places and for short periods of time (during an artistic festival), or for clearly identified categories of expenditure.

As stated above, the tax liability of income payments which are reportable under DAC 2 is established according to the tax law applicable in the residence country. The same principle should preside the taxation of income or gain from crypto-assets. The reporting of crypto-assets under the DAC should therefore be based on an agreed upon simple and objective methodology that would eliminate any valuation judgements or complex valuation methodologies. This is particularly true since the valuation of crypto-assets in terms of fiat currency may be difficult or very volatile. DAC 8 should clarify in particular how the reporting of gross proceeds from the sale or redemption of Financial Assets under DAC 2 would work in the context of the reporting by VASP that converts crypto-assets in fiat currency or other crypto-assets.

Definitional framework

AMLD 5 defines:

1. providers engaged in exchange services between virtual currencies and fiat currencies
2. custodian wallet provider
3. virtual currencies

The overhaul of the EU AML framework in 2021 is on-going and will result in a revised AMLD and the adoption of AMLR and, as regards e-money and crypto assets, should leverage on the extensive and important work that has been done by the Commission in the context of MICA which draws a distinction between:

1. crypto-assets that qualify as financial instruments and should be regulated as such because they pose the same risks of a financial instrument; and
2. crypto-assets that have different functions (e.g. utility tokens or payment tokens) and do not pose the same risks.

#2

SIMPLIFY
withholding tax procedures

Our recommendations

Create common pan European definitions and standards for withholding tax processing and build a workable EU withholding tax relief at source system while minimising the burden of paper-based tax processing, alleviating the continuing impacts of COVID 19 and preventing tax fraud

The importance of simplifying and standardising withholding tax procedures relating to cross-border portfolio investments has been highlighted in many reports from expert groups, including the reports of the Giovannini Group (in 2001 and 2003) and of the CMU High Level Forum (in 2020). The complexity, and cost and inefficiency of existing tax procedures are a major barrier to cross-border investment, and to the creation of a Capital Markets Union.

The process for claiming withholding tax relief has deteriorated over time in many countries, resulting in increased costs and protracted delays for cross-border portfolio investors.

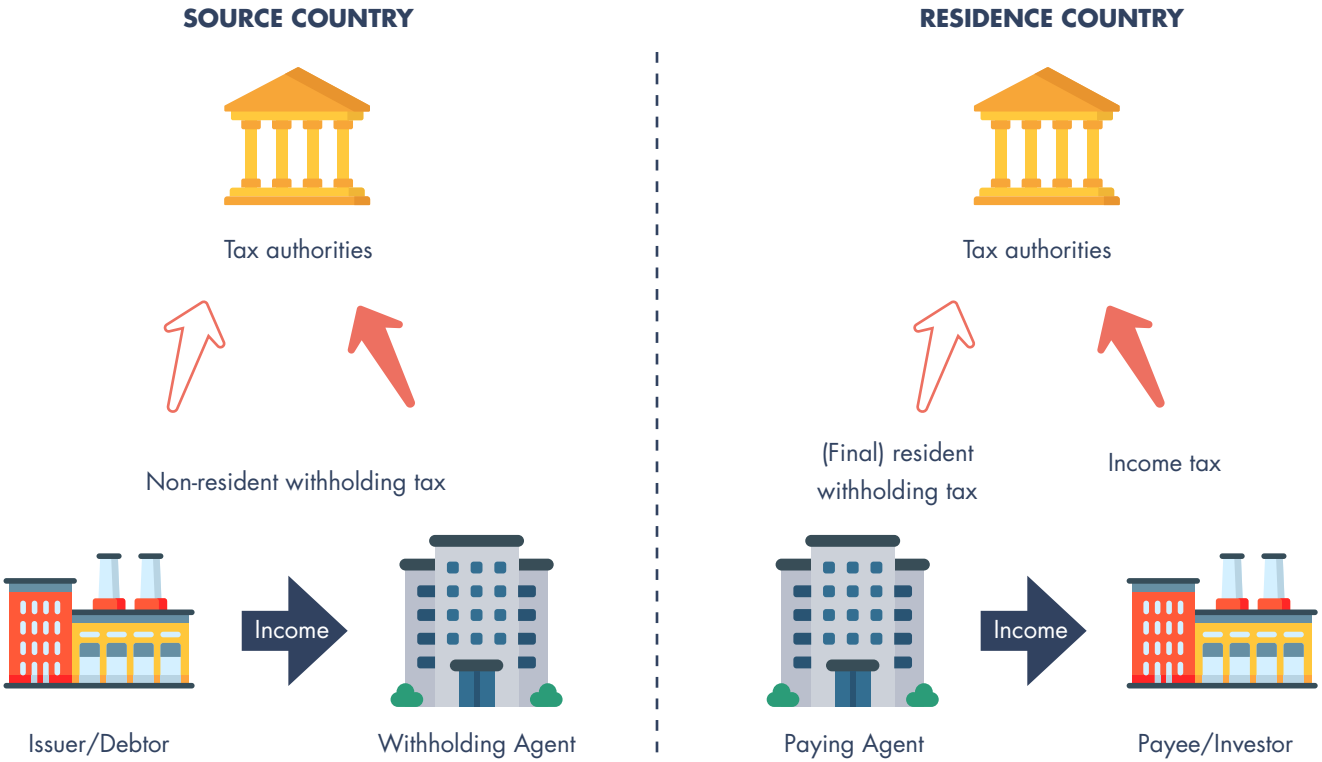
The types of burdensome procedures increasingly faced by investors include:

- Extensive, non-standardised documentation requirements, often for each income payment;
- The need to hire local counsel to pursue relief procedures;
- Requirements for residence country tax administrations to provide certificates tailored to requirements of the source country;
- Unclear or unreasonably complicated requirements for withholding tax relief on payments to Collective Investment Vehicles (CIVs), contrary to the OECD's recommendations; and
- Lack of an effective refund procedure.

Even though the financial intermediary has access to accurate customer information and is subject to high compliance regulation standards, obtaining tax relief to which its customers are entitled is often not practicable given the above complexities. Investors therefore often forego the relief. Full withholding at the maximum tax rate is then the outcome.

This situation also facilitates abuse of treaty benefits and tax evasion schemes like the CUM-EX files which consist in taking advantage of tax loopholes in certain jurisdictions by rapidly exchanging stocks "with" and then "without" dividends between parties that then claim tax rebates on taxes only paid once.

The COVID-19 crisis has highlighted many of the inefficiencies of current procedures.



Treaty benefits and withholding procedures

For cross-border investment income payments, Double Taxation Treaties (DTTs) provide for the following taxing rights:

- The country of residence of the payee has a full taxing right on this income;
- The source country has only a limited taxing right. In the jurisdiction of the debtor, foreign investors are granted a "Treaty relief" in the form of a limited tax rate (lower than the tax rate applied to resident taxpayers) or a tax exemption.

Debtors and/or Financial Institutions located in the source country which intervene in cross-border investment income payments are generally required by the domestic tax law to act as withholding agents, deduct a non-resident withholding tax and pass the related investor information up the chain.

Relief and refund procedures:

- The refund procedure is a standard withholding procedure under which relief from withholding tax is obtained through refund of withholding tax, which is requested from the source country's tax authorities by the withholding agent who needs to obtain preliminarily certificates of tax residency per investor.
- The relief of tax at source is a procedure under which the tax benefits are directly claimed by intermediaries and granted upon payment.

1 Create common pan European definitions and standards for withholding tax processing

The EU Code of conduct on Withholding Tax, which is the most recent EU initiative in this field, has appeared to be a list of non-binding recommendations and has not produced any concrete results. There is a need to create common pan European definitions and standards for withholding tax processing, addressing the three aspects.

Technology

Standard technology solutions would help reduce the costs currently associated, for all actors in the process, with the need to build, design, test and maintain multiple systems. Introducing a single digital system based on common law, common definitions, common processes would make it easier to re-balance taxes paid cross-border, while reducing administrative burden and costs.

Tax Forms Information & Data

Relevant tax data required to be transmitted in administration of the relief process should be standardised in order to simplify the data collection, transmission and review process in a truly digitised way. For example, the EBF has identified that tax relief forms have certain core similarities with at least 15 questions repetitive in nature but all conveying the same facts regarding the investor and the tax relief sought.

The wider digital agenda, including e-signature and digital forms

Solutions must be interoperable, standardised, global and available to all parties, and possibly based on machine readable forms.

2 Build a workable EU withholding tax relief at source system while minimising the burden of paper-based tax processing

The EBF welcomes the Commission's objective, stated in the Tax Action Plan of 15 July 2020 (Action 8) and the Capital Markets Union (CMU) Action Plan of 24 September 2020, of alleviating the tax associated burden in cross-border investment and at the same time preventing tax fraud. The EBF will support the Commission in exploring ways to introduce a common, standardised, EU-wide system for withholding tax relief at source. Such system has the potential to reconcile the interest of the Single Market by removing tax obstacles which are tantamount to double taxation and the interest of public finance by ensuring that treaty benefits are properly granted. In the Covid-19 context, both objectives are crucial.

Well-advanced solutions that have been discussed in many fora have possibly been overlooked by the Code of conduct on Withholding Tax published in December 2017, particularly the work of the OECD and its Tax Relief and Compliance Enhancement (TRACE) project which aims to propose a global model for relief of tax at source and is the most advanced work in this area.

Provided that TRACE remains an optional system for Financial Institutions, it may provide a starting point for a welcome level-playing field. The earlier and to some extent parallel work of the Commission – including the work with the Tax Barriers Advisory Group (T-BAG) - should also be referred to.

Until very recently, none of the EU Member States had taken the steps recommended by the OECD. Finland has been the first one to adopt in 2018 a legislation aligned to the OECD TRACE Implementation Package. The reluctance of the other Member States to take action may have been exacerbated over the last few years by the cum-ex files.

There is a need to improve clarity and to raise awareness and understanding about TRACE both in the industry and in the public sector. The Commission should work closely with the OECD notably to help ensure a proper implementation of TRACE in those jurisdictions that are early adopters. There is also a need for a broader industry engagement. The EBF wants to be at the forefront of this initiative.

TRACE in a nutshell

- The OECD TRACE Implementation Package (IP) is a model which suggests that Financial Institutions can enter into Authorised Intermediary agreements with the tax authorities of the source country.
- In their capacity as Authorised Intermediaries, they can then claim withholding tax relief on behalf of customers on a pooled basis.
- Investors have to provide a properly completed standardised Investor Self Declaration to the Authorised Intermediary, which is then required to report investor-specific information to the source country.
- This regime would abolish the need to obtain certificates of tax residency per investor and there would be no requirements to pass confidential investor information upstream.
- The TRACE IP includes an application for an Financial Institution to request authorisation from source countries to act as an Authorised Intermediary and includes a sample contract that could be used between the source country and the Financial Institution. The investor self-declaration forms would enable the investor to benefit from tax relief at source under the regime when presented to a participating Authorised Intermediary.


INVESTOR
FILLS OUT SELF-DECLARATION FORM
AUTHORISED INTERMEDIARY (AI)
REPORTING ON INVESTOR
FILLS OUT AI DECLARATION
INSTRUCTS POOLED TAX RATE
INCOME SOURCE COUNTRY
LOCAL WITHHOLDING AGENT
REPORTING ON AI
WITHHOLDING TAX

3 Alleviate the continuing impacts of COVID 19 and preventing tax fraud

The existing complexities have been exacerbated in the Covid-19 context. The problem primarily arises from the challenges of moving the paper documentation needed to obtain relief at source or to process reclaim submissions, including physical documents with wet ink signatures. A related problem involves the slow-down or cessation of production of needed documents (e.g. certificates of residence) and information due to changed working arrangements in government offices and other organisations. The EBF supports the practical recommendations made in May 2020 by a global coalition of the financial industry.

Concrete, practical solutions recommended by an EBF-led global coalition of the financial industry **MAY 2020**

- Authorising acceptance, by all parties in the chain, of electronic (scanned copy) tax documents and forms, with the further option for documents to be electronically affirmed (e.g. through use of digital signatures).
- Introducing a grace period to allow withholding tax relief to continue based on previously issued certificates of tax residency for investors)
- Having source country tax authorities agree to accept government issued certificates of tax residency in electronic format.
- Eliminating the requirement for withholding tax reclaim forms to be certified by the tax authority of the investor's country of residence.
- Eliminating the requirement for the apostillisation, notarisation, or legalisation of documentation required for the application of withholding tax relief.
- Removing the requirement for non-standard certificates of tax residency (for example, e.g. some jurisdictions require certificates to refer to specific sections of a double taxation treaty, or to be issued using the investment country's template document).
- Extending the period for the filing of withholding tax and information reporting returns by issuers, paying agents, and withholding agents.
- Extending statute of limitation periods by six months, thereby allowing additional time for the submission of withholding tax reclaims.
- Extending deadlines for responding to information and documentation requests issued by tax authorities, whether in the context of audits of withholding tax relief claims or as further substantiation of withholding tax refund claims.
- Issuing clear guidance to clarify the ability of participants in the documentation chain to rely on the parameters recommended above.

#3

NEUTRALISE

VAT distortions and other undue tax disincentives

While considering the introduction of an EU FTT, policy makers and legislators must be aware of the existence of important other taxes and levies that are specific for the banking sector, which already significantly add to the overall tax burden of banks. These are not only specific bank taxes but also non-deductible VAT.

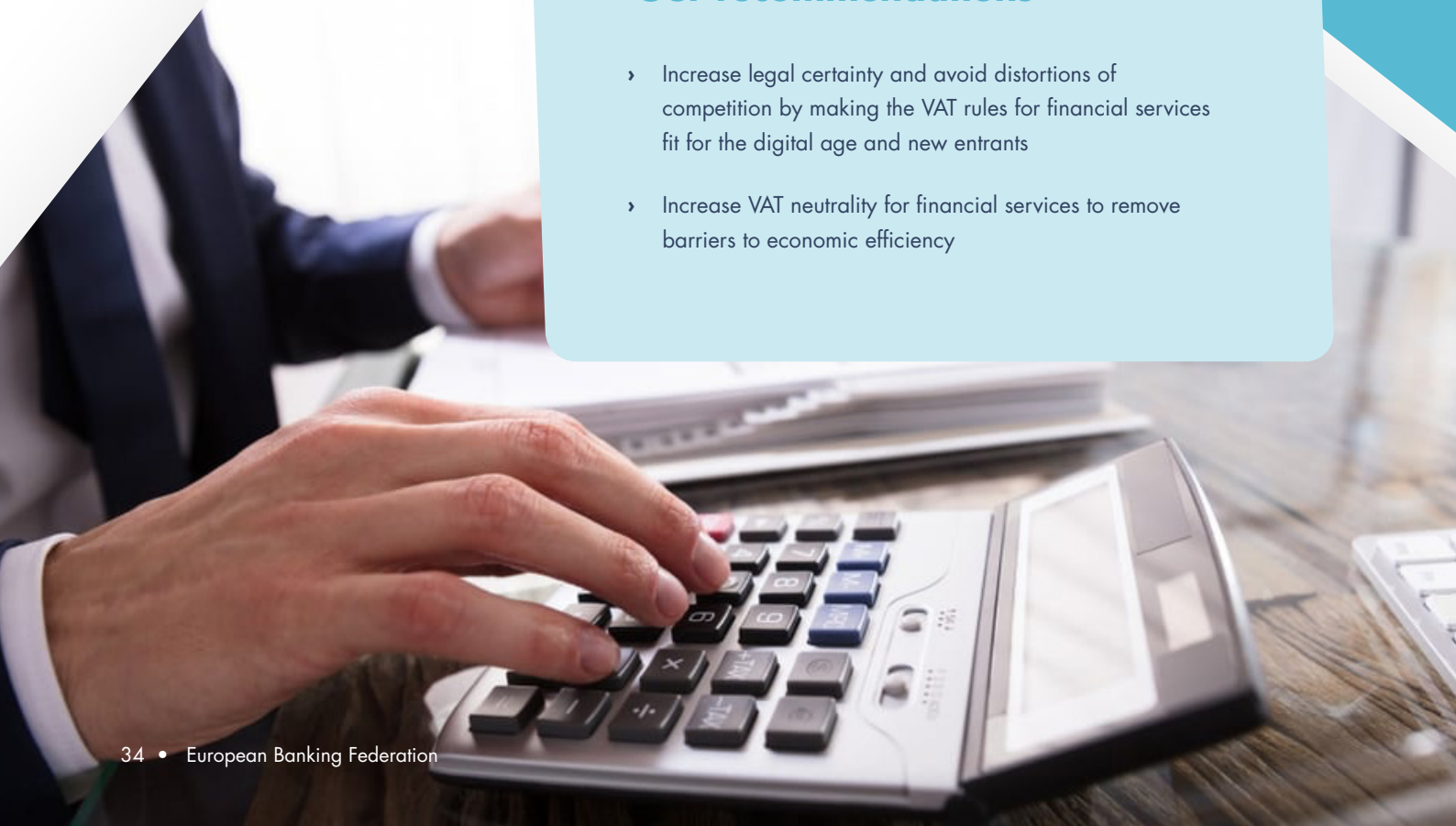
The current VAT system applicable to European banks is characterized by a high level of legal uncertainty and its lack of neutrality due to non-deductible VAT. As early as 2004, the EBF has been at the forefront in advocating for a reform of the VAT regime applicable to financial services. In order to address these concerns, the European Commission submitted in 2007 proposals to modernize the VAT treatment of financial and insurance services, which were discussed in the Council for many years but without reaching agreement among Member States. Consequently, the proposals were withdrawn in 2016 although the problems of non-neutrality and legal uncertainty had not been addressed.

There is still a strong need for a reform of the VAT rules as they apply to financial services.

VAT ON FINANCIAL SERVICES

Our recommendations

- Increase legal certainty and avoid distortions of competition by making the VAT rules for financial services fit for the digital age and new entrants
- Increase VAT neutrality for financial services to remove barriers to economic efficiency



1 Increase legal certainty of the VAT regime

Financial Institutions across the EU continue to face very significant legal uncertainty in respect of the application of European VAT law. Since the adoption of the VAT Directive in 1977, which is the core legislation applicable in the EU, the VAT rules applicable to financial services have never been adapted to the massive developments in the financial services industry.

The problems arising from the lack of legal certainty of the VAT treatment of financial services have been exacerbated by the rise of the digital economy and emerging actors such as fintech entering the financial market as well as increasing regulatory requirements for the financial industry. The result has been costly litigation for taxpayers and tax authorities alike, a cycle of uncertainty and a perception of an unlevel playing field which leads to distorted competition between different market players providing the same financial service.

Due to outdated VAT rules applicable for financial services, there is a high level of legal uncertainty regarding how to treat new forms of financial services, as it is often unclear what the scope of the exemption is, in particular within an increased digitalized environment. Moreover, the rules are interpreted and applied inconsistently by Member States, resulting in distorted competition within the EU.

2 Increase neutrality of the VAT regime

Non-neutrality arises from the VAT exemption regime that is applied to financial services. Exemption means that most services provided by Financial Institutions are not subject to VAT. VAT incurred on expenses by Financial Institutions is, however, only recoverable to the extent that the services supplied are in turn subject to VAT. This is dramatically different from the way that the VAT system was intended to operate and as it applies to other industries.

The lack of neutrality, which restricts banks' right to recover the VAT they have incurred on their own expenses, results in hidden VAT that constitutes a significant additional cost for banks and leads to cascading effects within the chain of supply. Therefore, VAT often thwarts attainment of economic advantages by implementing efficient business models. Any attempt to achieve synergies and to improve efficiency is blocked due to the cascading effect of VAT. Overall, VAT has become a barrier to economic efficiency for banks.

This lack of neutrality results in an increasing loss of competitiveness for European banks in the global marketplace, as hidden VAT cost affects profit margins and prices, giving a significant competitive advantage to non-European providers.

Even within the EU there is an unlevel playing field regarding fintech and other service providers with a full right to deduct input VAT as their "financial" services are often considered VAT liable.

In the light of the above, the EBF strongly supports the new initiative of the Commission to review the VAT rules for financial and insurance services in the light of the existing regulatory and other indirect taxation rules. The EBF would very much welcome new legislative proposals as envisaged in the Commission's Tax Action Plan for a fair and simple taxation in summer 2020.

Example: Outsourcing of Payment Services

Problem:

Payment services are exempt from VAT. The CJEU tends to interprete VAT exemptions strictly, with the effect that outsourced payment services are in most cases VAT liable. Outsourced payment services are being cut up with all operators providing indispensable crucial parts of an overall payment service. On their own the parts become subject to VAT when looked at in isolation because the individual part of the overall payment service is deemed to be a taxable electronic or technical service and not a VAT exempt payment service. The current development of applying VAT on individual parts of payment services, as they are provided by various market players, also by fintech, leads to cumulation of non-deductible VAT as cost for the banks.

Suggestion/solution:

The VAT treatment should follow the nature of the (financial) service. The way in which a service is rendered, whether undertaken manually or automatically via electronic processing, should not be decisive in determining the VAT treatment, and certainly not in the digital age.

Our recommendations

Refrain from introducing an EU FTT, which would limit the efficiency and liquidity of the derivatives, bonds and stock markets in the EU and would reduce the returns for savers

1 Refrain from introducing an EU FTT

The clear lack of global support for a Financial Transactions Tax (FTT) causes potential distortion of competition that could stem from numerous uncoordinated approaches to taxing financial transactions, particularly where Financial Institutions are outside of the FTT-zone.

If the FTT were adopted by a limited number of jurisdictions, Financial Institutions around the world would begin to reduce their exposure to Financial Institutions and businesses within FTT jurisdictions, which are home to some of the largest Financial Institutions and businesses in the world. Such FTT could decrease the interest of performing financial activities inside of the participating jurisdictions and could therefore distort the functioning of the Single Market for capital.

There is an inherent contradiction between the Commission's objective of introducing a uniform and consistent method to tax financial transactions across the EU and the perspective of fragmentation between FTT and non FTT jurisdictions possibly resulting from the enhanced cooperation.

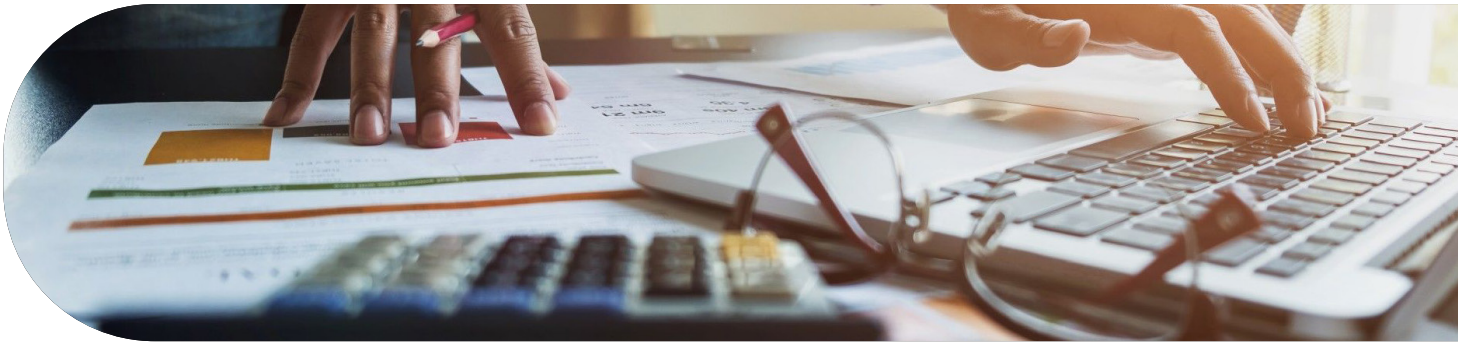
Even if FTT were implemented across all EU Member States, its introduction would be detrimental for EU financial markets as it would increase distortion on the market and encourage entities to relocate their financial activities outside the EU. It would also reduce the value of existing investments in companies which would fall under the FTT.

An FTT would distort asset markets, as types of securities traded more frequently would be taxed much more than assets traded less frequently. This distortion would lead to investors holding certain assets longer than they should in order to avoid the tax. The tax would also decrease liquidity and increases transaction costs.

Ideal tax policy should be economically neutral by taxing income once (ideally at the point of consumption). However, the FTT would be an additional layer of taxation on top of existing capital gains taxes, individual income taxes and corporate taxes.

Deep concern is also expressed about the risk of double taxation where the FTT could operate alongside non-harmonised tax regimes in other jurisdictions.

an EU FTT would be inconsistent with the EU's goal of a single market (Capital Markets Union and Banking Union) and regulatory objectives which have been reinforced to ensure financial stability and harmonization in the EU.



#4

RING-FENCE

banking activities from other highly digitalised businesses when designing new corporate tax rules

Our recommendations

- EU initiatives in the field of corporate taxation should take into consideration banks' operating models and applicable regulations which ensure that banks set up a physical presence and hence have a taxable nexus where they face customers
- There is no ground for bringing financial services into the scope of an EU Digital Tax

The problems of the initiative for an EU Digital Levy aims to tackle are the same that are at the basis of the work performed in the context of OECD BEPS action 1 and the latest OECD pillar 1 blueprint and of the EU DST proposal that was first issued in March 2018.

The situation of banks and other regulated service providers has meanwhile extensively been examined in the context of OECD pillar 1 discussions and, based on the current status of the blueprint, has led to the conclusion by OECD, the Members of the Inclusive Framework and EU member states that banks are to be excluded from the new nexus rule proposed under pillar 1.

A new proposal for an EU Digital Levy should therefore fully align with OECD and Inclusive Framework findings that there are clear policy and technical reasons for excluding banking industry services from the scope of the new taxing right for automated digitized services and consumer facing business which is developed under pillar 1.

Strong consideration should be given in this respect to

- banks' operating model and applicable regulations, which ensure that banks set up a physical presence and hence have a taxable nexus where they face retail customers as well as the high-level compliance of banks under the current rules.
- the fact that any proposal should be based on international consensus and agreement to avoid the potential of unintended tax consequences and disputes between jurisdictions.

An EU Digital levy proposal should consistently reflect this and provide for an equal carve-out for banking services as is provided for in the pillar 1 blueprint. The carve-out of the banking industry should apply to any type of entity that is conducting regulated banking activities. One should consider in this respect the exclusion of regulated financial services provided by regulated financial service providers that already had been laid down in the latest draft directive proposal on the introduction of an EU DST (dd. 28/11/2018).

Finally, we would like to refer to the critical role banks will have to play in the recovery and that it is essential that tax measures produce results consistent with and support the regulation of banks as they do this.

1 Corporate tax rules consistent with banks' operating models and applicable regulations

Banks differ from many other businesses. A "bank" refers to a regulated deposit taking institution licenced to operate in a jurisdiction and its related group subsidiary entities or branches.

Banks are highly regulated with strict rules, standards, funding and capital rules. Banks setup a regulated presence in the locations where they face their retail customers, with careful attention to the formation of legal entities and/or branches, resulting in organizational structures in line with legal requirements, with premises and staff, adequate funding and capital. Accordingly, banks do not have a significant digital footprint in a jurisdiction without a corresponding physical presence.

This regulated presence results in a taxable nexus and a high level of tax compliance: establishing separate/local financial statements, meeting local tax filing requirements, recognising profits in the locations where banks face their customers. These provide a natural barrier to banks using artificial or contrived methods to participate in the economy of a particular jurisdiction without a taxable presence. This means that banks pay tax in the right jurisdictions because their operations in each jurisdiction generally require a taxable presence to be established. These are the reasons why low risks have been identified by BEPS project and in the context of the digitalised economy.

The current tax rules as they apply to banking activities work effectively and ensure a high-level of tax compliance.

Banks are subject to specifically targeted tax rules in jurisdictions including targeted anti-avoidance rules, tailored thin capitalisation rules and additional levies to support risk of failure.

The OECD Report on the Attribution of Profits to Permanent Establishments (2010) is well accepted guidance for banks on the attribution of profit between their head office and offshore branch operations.

Transfer pricing methodologies work effectively to allocate profits to the correct jurisdiction in which multinational banks operate.

Revenue authority guidance and industry practice is well understood and established on profit attribution principles as they apply to banks. Deviation from those principles would cause significant impact to banks and their operations as well as have the potential of conflicting objectives with regulatory law.

As a result, in certain tax jurisdictions where the offshore branch business is not supported, or inadequately supported by capital, an adjustment is required to be made to the offshore branch operation's corporate income tax computation, thereby ensuring that the taxable profits are more closely aligned with those which would be achieved by similar banking activities carried out by a bank in the same or similar conditions.

In addition, banks are subject to extensive tax transparency and tax avoidance mitigation reporting rules, which seek to capture the diversion of profits to low tax jurisdictions by their customers.

Therefore, the existing corporate tax framework adequately captures profits earned by banks, both traditional banking services, including where such services are provided via digital mediums.

As a result, any corporate tax reform applicable to banks should be based on international consensus and agreement. To the extent to which countries implement unilateral measures that impact financial services, there is the potential for unintended tax consequences for global banks. This can include the risk of double taxation and/or disputes between jurisdictions.

Banks's regulatory requirements

- Banks are required by local Regulator to obtain a licence to conduct banking and other financial services. Derogations exists under the EU « passporting » system, but these are generally not relied upon for customer-facing activities.
- Banks must be in compliance with Central Banks requirements.
- They are required to hold loss-absorbing regulatory capital imposed by prudential regulators in respect to their global operations and have prudential limits on intra-group exposure between entities in the group.
- They must maintain buffers of high-quality liquid assets to cope with instability and liquidity shortages
- They must maintain net stable funding ratios.

2 Carving-out banks from the scope of an EU Digital Tax

The carve-out of the banking industry from OECD Pillar One should apply to any type of entity that is conducting regulated banking activities

The EBF welcomes the explicit acknowledgement by the OECD and the Members of the Inclusive Framework in the October 2020 report on the pillar 1 blueprint that the banking industry should not be subject to the new taxing right for automated digitized services and consumer facing business and fully supports their findings that:

- financial regulation governing the banking services industry generally require that appropriately capitalised entities are maintained in each market jurisdiction to carry on business in the market concerned. Due to this factor, the profits from consumer facing business activities (CFB) that arise in a particular market jurisdiction will generally be taxed in that market location; and
- the banking services industry should not generally involve business of the sort that is properly regarded as automated digitized services.

We consider that the carve-out should apply to any type of entity that is conducting regulated banking activities, regardless of whether the taxpayer is a traditional bank or a new or different business model such as a FinTech.

The current Transfer Pricing rules based on the Arms' lengths principle are retained

To the permanent establishment concept, is added a new concept of nexus without physical presence based on the volume of sales in market jurisdictions.

It is complemented with a new formula-based profit allocation applicable to the deemed residual profit

In scope:

- Highly digitalised businesses
- Consumer-facing businesses (which are assumed to generate high profits)

Out of scope: Non-consumer facing businesses (e.g. institutional/ investment banking)

Relevant factors for carve-outs:

- Businesses not generating non-routine profits from intangibles that can be moved to low-tax jurisdictions
- High-level of tax compliance under traditional methods
- Practical difficulties to administer the new approach

An overall carve-out for regulated financial business should be considered for OECD Pillar Two

As regards pillar 2 minimum taxation rules, an overall carve-out for regulated financial business should be considered, as being financially regulated automatically implies strong local substance (apart from costly capital and liquidity requirements) and often comes along with substantial sectoral levies, non-deductible VAT, etc. which are also constitutive of the overall local tax burden of banks.

If minimum taxation rules would apply to banks, such rules should preferably work on the basis of global blending instead of jurisdictional blending. Global blending equally serves the policy objective of GloBE which is to ensure that MNE's do pay a minimum tax on their profits but avoids the additional compliance of jurisdictional blending and may solve possible incompatibilities with EU primary law.

More generally, minimum tax rules should not be overly complex and be manageable from an administrative perspective in order to maximally reduce the additional compliance burden.

EU Digital Tax should fully align with OECD and Inclusive Framework findings that there is no ground for bringing banking industry services in scope of the new taxing right for automated digitized services and consumer facing business which is developed under pillar 1

Any proposal for an EU DST must fully align with OECD and Inclusive Framework findings that there is no ground for bringing banking industry services in scope of the new taxing right for automated digitized services and consumer facing business which is developed under pillar 1. A possible EU DST proposal should consistently reflect this and provide for a similar carve-out for banking services.

Banks utilise data that they obtain from their customers to provide services which in turn are subject to tax. Accordingly, to the extent that there is any monetisation of data by a Bank, this will be reflected in the profits already subject to taxation. Where data is mandated to be exchanged for no value between a bank and third party for no fee, for example under open banking laws, this transaction should not be subject to tax. Where a value-added service in respect to customer data is provided to a third party, the profit should be subject to tax under ordinary principles.

Table of acronyms

AEoI	Automatic Exchange of Information
AML	Anti-Money Laundering
AMLD	Anti-Money Laundering Directive
BEPS	Base Erosion and Profit Shifting
CCCTB	Common Consolidated Corporate Tax Base
CFT	Combating the Financing of Terrorism
CJEU	Court of Justice of the European Union
CRS	Common Reporting Standard
DAC	Directive on Administrative Cooperation (2011/16/EU)
DAC 2	1st Revision of the Directive on Administrative Cooperation (2014/107/EU)
DAC 6	5th Revision of the Directive on Administrative Cooperation (2018/822/EU)
FATCA	Foreign Account Tax Compliance Act
FATF	Financial Action Task Force
FTT	Financial Transaction Tax
KYC	Know Your Customer
OECD	Organisation for Economic Co-operation and Development
PE	Permanent Establishment
QIA	Qualified Intermediary Agreement
T-BAG	Tax Barriers Advisory Group
TEU	Treaty ion European Union
TFEU	Treaty on Functioning of the European Union
TRACE	Treaty Relief and Compliance Enhancement
VAT	Value Added Tax
WHT	Withholding Tax

Roger Kaiser, Senior Policy Adviser
Eduard Hovsepyan, Policy Adviser

Brussels I 56 Avenue des Arts, B-1000, Brussels
Frankfurt I Weissfrauenstrasse 12-16, D-60311, Frankfurt am Main

+ 32 3 508 37 11 I www.ebf.eu I info@ebf.eu I #EBF

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