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Harri,

We are pleased to respond to your request for consultation on the subject of Finland's TRACE model and the impending FASTER Directive.

These are the considered comments of the Association and not those of any specific member of the Association. Our commentary is structured as shown below.

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About AQAI

AQAI is an unincorporated, not-for-profit trade association formed currently of 86 members in 27 countries. The members are, for the most part, financial institutions that actively support tax relief at source, notably in the US market under the IRS qualified intermediary (QI) program. Several members of the Association are also Finnish Authorised Intermediaries, and many others will be adopting CFI status in 2030 when FASTER comes into force. As such, the Association is keenly interested to contribute to national and European debates to help improve cross-border tax relief processing. AQAI is a member of the Commission's FASTER Large Working Group.

We are happy to respond to further questions or provide further input on request. Please respond in such cases, to me at chairman@aqai.tax



Ross McGill
 Chairman

Consultative Response

It is clear that the current TRACE model used by Finland will have to be amended to allow for Finland to introduce legislation to give effect to the FASTER Directive.

General concerns

One general concern of a number of members is that any increase in complexity, in TRACE and/or FASTER, particularly where tax relief, quick refund and standard refund are all improved and automated simultaneously, may have the unintended consequence of driving AIs (and CFIs) to selectively register in a pattern that reflects only their existing client base. In some cases, such complexity could also lead to an increase in standard refunds at the expense of the intended relief at source and quick refund models.

Another concern is over the treatment for non-EU investors and US investors in particular. Finnish TRACE is more advanced because it uses an Investor Self-Declaration (ISD) that can be completed by any investor irrespective of their residency. This is similar also to the OECD's Common Reporting Standard which also uses ISDs. FASTER is an outlier because it bifurcates this concept by requiring EU investors to obtain an electronic tax residency certificate from a competent authority (eTRC). While this does not prevent non-EU investors from claiming relief, it does mean that each such jurisdiction will have to demonstrate technical equivalence to an eTRC and FASTER appears to make this an individual judgement of each EU Member State rather than an EU-wide principle.

We also considered whether the Finnish TRACE model meets the requirements set out in FASTER Article 3(22a) (a)-(e) to be considered a “*comprehensive system of relief*”

Does the TRACE model meet the technical requirements of Article 3(31)(a)-(f) to be classified as a “comprehensive system of relief”?

These are the following areas that may need to be strengthened to better conform with the FASTER Directive:

- a. The Investor Self-Declaration will probably need a statement that satisfies Article 11(2)(b) – to confirm that they have not engaged in linked transactions.
- b. Specific Liabilities and Penalties for the CFIs may need to be defined. Our current understanding of the TRACE implementation in Finland is that the liability is limited to the non-withheld tax and only if the AI is negligent. This may not be sufficient to dissuade bad actors. However, we would note that the marketplace pushed back on the original liability and penalties that Finland had proposed because they did not believe they would be able to accept that liability. It remains to be seen how this impacts voluntary applications to become CFIs under FASTER.
- c. Finland may need to make some domestic Financial Institutions become mandatory CFIs. We believe because the AI regime is still voluntary, we are not sure if any that would fall under the FASTER definition of “large institution” have not already voluntarily become an AI in Finland.

We believe that the rest of the current implementation of TRACE is generally aligned with that of the proposed FASTER Directive from a comprehensive system of relief definitional perspective.

It appears to us, as non-legal commentators, that while Finnish TRACE may qualify as a comprehensive relief at source system, we would recommend that Finland obtain a written determination from the European Commission that the system does so qualify. Articles 3(31)(a) and 3(31)(d) would be of most concern because TRACE applies only to nominee registered shares in the first case (not direct registered shares) and in the

second case Finland does require additional information beyond the ISD when an AI uses the pre-certification mechanism.

National Registers

Finland's implementation of the OECD TRACE package did not adopt the concept of a contractual relationship (AI Agreement) between Vero Skatt and non-resident financial intermediaries as withholding agents (c.f., IRS & US QI Agreement), preferring instead to use a national register.

Finland already has a national register of financial intermediaries authorised to act as withholding agents for the provision of tax relief at source using an Authorised Intermediary Identification Number (AIIN). Finland would need to establish an equivalence between its AIIN and the Certified Financial Intermediary Identification Number (CFIIN) that will be required under FASTER. The Large Working Group (LWG) of the Commission is currently working on draft technical guidelines for the central registry of CFIs.

Electronic Tax Residency certificates (eTRC)

The largest difference between TRACE and FASTER is that Chapter II Article 4(1) of FASTER mandates use of digital tax residency certificates (eTRCs) issued by the tax administrations of Member States, compared to the TRACE use of self-certifications i.e. investor self-declarations (ISDs). The LWG has developed draft technical guidelines for the specifications of eTRCs.

Given FASTER's legislative baseline, Finland will need to develop, test and launch its own eTRC system in order to enable its residents to claim relief in other Member States via Finnish CFIs registered in those Member States. Equally, residents of other Member States will use their own eTRCs, through Certified Financial Intermediaries (CFIs) that have been entered into the national register of CFIs in Finland.

A most important improvement to the TRACE system used by Finland would be the establishment of an equivalence between the TRACE self-certification and the FASTER declaration required under Article 12(1)(a)-(d). While the conduct of due diligence is explicit in Article 12(2) and implicitly includes KYC and AML in Article 12(2)(c), the FASTER Directive's text provides only for situations where a CFI has failed to comply (Articles 18 & 19), such that it is liable for any tax under-withheld as a result of an incorrect issuance of an eTRC. We believe there is an opportunity to change the wording on the Finnish ISD to address these issues that would both meet the required FASTER Articles, but also improve the quality of the TRACE documentation.

Non-EU residency evidence

The FASTER Directive mandates the use of eTRCs for intra-European investors but also allows for an equivalence for tax residency evidence for non-EU investors in Article 12(2)(a).

The largest inbound investment market to the EU and to Finland is the USA where investors typically use the form 6166 or form W-9 to evidence US tax residency. Many Americans invest in the EU via the use of American Depositary Receipts (ADRs) issued by one or more of four Depositary Banks. ADRs are denominated in US dollars and traded on the main US markets.

Article 12(2)(a) of FASTER provides that each Member State can verify eligibility for tax relief based on:

- 1 An eTRC or;
- 2 Proof of tax residence in a third country deemed appropriate by that Member State

Our analysis of the US form 6166 and form W-9, commonly used by all non-US financial institutions to determine tax residency of a US person, is that strictly speaking, they do not conform to Annex I of the FASTER Directive.

Generally, the 6166 fails because it does not have an electronic seal, is not specifically machine readable (although it can be read by a machine), and does not contain a free text section to allow for information under Article 4(2)(g), although the information for Annex I(1) and Article 4(2)(h) is only required if the registered owner is not claiming a treaty benefit in the EU. It is also questionable whether one considers the US Tax Year as the covered period under Article 4(3)(a).

For natural persons, the 6166 fails because it does not have the Date of Birth or the Address of the taxpayer. For legal entities, the 6166 fails because it does not have the address or any other registration number (such as the EUID or LEI) other than the US Taxpayer ID Number (TIN).

Other than the US, most countries adopt a physical certificate of residence and some also require an attached physical “apostille”. The OECD TRACE and OECD CRS frameworks both have a self-certification which can be provided digitally.

Having seen certificates of residence from many other countries we doubt that any would meet the current requirements under FASTER. However, we argue that Article 12(2)(a) could be relied upon if Finland were to establish that a form 6166 or a form W-9 (or electronically signed digital substitutes thereof) would be considered “appropriate evidence of tax residency” subject to additional checks and balances including for example a validation by the CFI of the registered owner’s US tax identification number (SSN or EIN) against the IRS database.

We received clarification from the Commission working group that: “This [the requirement for technical equivalence of a non-EU ISD to Annex I] does not prevent Member States from accepting ISD or non-standardised TRC from 3rd countries. The last paragraph of 12(2) was included foreseeing a potential extension of the content and technical specifications of the eTRC from the EU to OECD countries.”

We conclude therefore that Finland’s interpretation of TRACE can be aligned with the FASTER Directive given the freedom of the Member State to determine the acceptability of non-standard TRCs (e.g., 6166) and/or digital self-certifications.

Claims for relief

Article 12(1) of FASTER provides for a “declaration from a registered owner” that they meet the eligibility criteria for tax relief laid down in Article 12(1)(a)-(d). This highlights an inefficiency in FASTER caused by its bifurcation of the tax residency evidentiary issue from the claim of treaty benefits declaration. The TRACE ISD already contains both the declaration of eligibility and the certification of tax residence. The FASTER Directive appears to separate these two issues.

We would argue that Finland could, adopt a two-stage approach:

- 1 For any registered owner not resident in an EU Member State, Finland could deem the TRACE ISD as “appropriate” under Article 12(2)(a), subject to certain safeguards, and that such ISD also be deemed to meet the requirements of Article 12(1). We would recommend a more detailed analysis of the Finland ISD to determine any improvements that could be made to its wording to meet the certification language of Article 12(1)((a)-(f).
- 2 For any registered owner resident in an EU Member State, the eTRC plus an ISD would meet the standard expected by FASTER.

While only Finland as an EU Member State has adopted the TRACE Model, other Member States will no doubt be struggling with the same question given the importance of non-EU inward investment to each of those markets. This may argue for a broader OECD approach and update to the global model for ISDs.

EUID and LEI

There are 200 million national identity cards issued in the EU/EEA consisting of at least 86 versions of identity cards. There are currently 2,840,015 LEIs issued (of which 1,060,116 have lapsed). While these numbers are significant, outside the EU, LEI adoption is patchy and much less significant. It is expected that one of the impacts of FASTER will be an increased rate of adoption of LEIs in order to support claims of tax treaty benefits.

Notwithstanding the generality of Article 4(2)(b), to allow the use of any functional equivalent of a tax identification number, it may be beneficial to include LEI and/or EUID as specific fields required by entities on Finnish ISDs. This would also allow financial institutions and service providers to provide more effective technological solutions including inline API checks against LEI databases.

Standard Refund

The original texts of the FASTER Directive were based on a principle of making all parts of the tax process more efficient. With respect to standard refunds made directly to a tax administration where tax relief and/or quick refund have been absent or unsuccessful, this took the form of a standardised, digital tax reclaim form, standardised evidentiary material and an upper time limit for refunds to be completed.

Article 11(2) of FASTER, provides that “*Member States may, either fully or partially, exclude certain refund requests from the relief mechanisms set out in Articles 13 and 14.*”

We think that Finland should confirm whether it intends to maintain the full scope of refund requests, as currently applied under TRACE, or whether Finland plans to exercise its discretion to exclude certain refund requests from FASTER?

For example, if domestic exemption claims are to be included in FASTER’s scope for Finland, would the current requirement for pre-approval under TRACE be upheld within FASTER? The pre-approval process could be deemed to be “additional information” under Article 3(31)(d) thus removing Finnish TRACE from the definition of a comprehensive relief at source.

Additionally, it would be useful to clarify that no additional documentation beyond the Beneficial Owner Declaration and eTRC may be requested, thereby requiring Finland to rely solely on this declaration to apply tax relief to domestic exemption claims. Finland can then still exclude certain refund requests under FASTER. Given that domestic exemptions are subject to eligibility criteria that may change annually due to legislative updates, it would be prudent to evaluate whether Finland’s FASTER should encompass the full scope of refund requests.

While this is not a proposal to modify TRACE by excluding certain refund requests, it does raise a broader question of whether Finland should align FASTER’s scope with TRACE or adopt a more selective approach.

The potential for a trend towards standard refunds has been raised in this consultation and some evidence of that trend exists in data provided to us. The original principle of the standard refund process was that it, like the relief at source and quick refund systems, should be digital and be completed with a specific timeframe. Article 17 of FASTER addresses neither of these two issues and further references Articles 12 and 13 to establish that standard refunds should only take place if the claims under those relief mechanisms of those Articles are

excluded. The concern of members is that any significant changes in operational systems needed to adhere to Chapter III would naturally mean that claims for relief at source and quick refund would be foregone for operational reasons leaving the existing standard refund as the only recourse for investors. It is not clear whether claims that merely fail to meet the submission deadlines due to late or invalid documentation, as opposed to those failing for reasons provided in Article 15(2), would be eligible for standard refunds on the basis of Article 13 and 14(4).

Penalties - Effectiveness, Proportionality and Dissuasiveness

We believe that Finland's liability framework is aligned with FASTER Article 3(31)(e). However, with respect to penalties, Article 3 (31)(f) of FASTER mandates that penalties must be (i) effective, (ii) proportionate and (iii) dissuasive. None of these terms is further defined in FASTER and it would be difficult to argue that a penalty that is proportionate is necessarily dissuasive or vice versa.

Finland could lead the way in this area by establishing TRACE definitions for these terms and determining specific dissuasive penalties for particular types of case. In line with the US FATCA Model, failures leading to penalties could be defined as "minor administrative failures" and "substantial non-compliance".

The need for transparent guidance

We are curious to see whether the current BO declaration also offers the possibility to apply special rates. According to Article 12(2)(d) investors should also provide the tax rate to which they are entitled via an ISD. As EU FASTER also grants reduced rates for dividends and interest from both a tax treaty as well as domestic legislation, this might create an additional layer of complexity as certain jurisdictions offer exemptions based on a similarity analysis for funds (e.g., comparable to a domestic fund).

If CFIs would deny benefits because of the penalty risk and risk of under withholding this could create tension between the investors and the CFI applying reduced rates (a claw-back clause between investor and AI would no longer be sufficient). We hope that more guidance will be given on this matter.

Effects of legislative amendments

Any amendments to legislation cause additional work and cost for financial institutions.

One of our members that services large US financial institutions, has seen a shift in U.S. pension funds filing for exemption from RAS/QR towards a Standard Refund. This may indicate that the threshold of €10,000 in dividend entitlements is too low and seems to be forcing all exempt claims into the standard refund process.

Additionally, they have noticed that the introduction of the ISD requirement has led to an initial dip in claims filed through RAS/QR but these claims are slowly improving each year. The shift from using data about the investors to requiring a document from them provided was a hurdle that investors are starting to adapt to.

Possible Adjustments:

- 1) Reducing the requirement for any physical documentation for smaller natural persons (relying on the KYC of the banks/brokers instead) would increase the access for these investors without adding much risk to the process.
- 2) Increasing the threshold for exempt investors would likely increase access for U.S. pension funds"

Responses to specific questions

How could the reporting burden be reduced without undermining the quality of the information, considering the mandatory provisions of FASTER?

- Adding a comment to the Investor Self-Declaration to account for mandatory provisions in FASTER, specifically, the requirement to notify the AI/CFI of any potential linked transactions such as stock loan, repos or swaps.
- Allowing for electronic confirmation of the information on the ISD would reduce the reporting burden without undermining the quality of the information.

Were there negative impacts to TRACE (to the Finnish Capital Markets)?

It is difficult to determine the impact of TRACE to the Finnish Capital Markets, because COVID occurred almost at the same time as the TRACE implementation. COVID prevented some Finnish companies from paying dividends in 2020 which may have had a large impact on the Finnish Capital Markets in 2021 and beyond. It seems clear that fewer registered holders are receiving Relief At Source which typically reduces the return on their investment and negatively impacts demand for Finnish securities.

Impact of FASTER on the Finnish Capital Markets

If FASTER works as those who wrote the Directive hope, it will increase the flow of capital throughout the EU. To the extent that this results in net positive investment to Finland would be difficult to quantify. While it may make Finland more attractive to investors from outside of Finland it may also make other investments in the EU more attractive to Finnish residents so they may reallocate their investments out of Finland and into other EU markets. In the long run, it is likely better for the CMU as a whole but not necessarily for each market.

Impact of FASTER on Finnish residents

Finnish residents should benefit by having more investment options throughout the EU where the investments are economically equivalent from a tax perspective to domestic investments. To the extent that they currently invest throughout the EU, they should find that they will receive tax relief with less effort. The effort will be taken up by CFIs.

Conclusions

The Association membership are concerned that the primary objective of both TRACE and FASTER may be undermined by any disproportionate increase in administration of procedures, technical or legislative changes that do not directly contribute to the purpose of these frameworks.

The implementation of eTRCs by Member States, the frequency of reporting and the ability of Member States to make independent decisions of “appropriateness” separate from other Member States, all appear to create a framework in which CFIs will need to adopt more sophisticated approach to client onboarding and processing of tax relief, quick refund and standard refund claims. The fear is that increasing cost and complexity will drive both CFIs and investors into the standard refund system and away from relief at source or quick refund. In effect, the danger of FASTER is that it replaces one form of complexity and cost with another of a different nature, the effect of which will be “no real change”.

The implementation of the FASTER Directive will also have impacts on the OECD TRACE IP Model. While Finland remains the only adopter of TRACE in the EU, this may be a moot point, although our members argue

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that the OECD should take steps in advance to create greater alignment in areas mentioned in this consultation. This may mean that the OECD TRACE IP Model needs to be updated as well as the Finnish TRACE model.

We remain at your disposal.

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