



Update on Withholding Tax in Germany

MiKaDiv postponed until 2027 to facilitate Joint Implementation together with FASTER in Germany

One of the main concerns of affected custodians for German Equities has been having to first implement the domestic Withholding Tax Reform in Germany and then, a few years later, meet the additional requirements of the EU FASTER Directive. The German legislator is now addressing this by (further) postponing the new rules on WHT payment and reporting (“MiKaDiv”) to achieve one joint implementation of the MiKaDiv and FASTER reporting standards in Germany.

Background

German WHT Reform & MiKaDiv

With the Act on the Modernization of Withholding Tax Relief dated June 2, 2021 (“*WHT Reform*”), Germany initiated a comprehensive reform of the German WHT system. The objectives of the Reform include, among others, the prevention of tax abuse and the complete digitization of the WHT workflow for dividends and comparable investment income. The changes therefore affect both the WHT payment and reporting procedure (“*MiKaDiv*”), by implement enhanced requirements to report tax relevant date to German Tax Authorities, as well as the process of WHT relief.

The changes are being implemented in stages: while the electronic WHT relief procedures have been in effect since 2023 (continuously amended to facility bulk reclaims), the revised procedure for WHT payment and reporting (*MiKaDiv*) was originally scheduled to come into effect on January 1, 2025. By Decree of August 27, 2024, the German Ministry of Finance initially provided for a postponement of the effective date to 2026. The Annual Tax Act 2024 now provides for a further postponement and additional changes (see below).

Challenges due to the overlapping scope of the EU FASTER Directive

On May 14, 2024, ECOFIN reached a political agreement on the *Council Directive on Faster and Safer Relief of Excess Withholding Taxes* (“*FASTER*”). Following recent consultations at the European level, we expect the final FASTER Directive to be adopted by the end of 2024/early 2025.

The Directive aims to accelerate and simplify WHT relief across the EU, particularly for cross-border investments, as well as to improve control and tracking capabilities by national tax

administrations. In addition to introducing an electronic EU Tax Residency Certificate (eTRC), the Directive provides for the introduction of two alternative fast-track procedures for WHT relief (Relief at Source, Quick Refund). The fast-track procedures will in the future require, among other things, that so-called Certified Financial Intermediaries ("CFIs") register in national registers and comply with extensive reporting obligations to the competent national tax authorities. The FASTER Directive defines a reporting standard for CFIs, which includes a comprehensive catalog of reportable data on dividend payments, the recipient of the dividend payments, custody chain and other relevant parameters. This reporting standard must be transposed into national law by the Member States by December 31, 2028, at the latest. The new regulations are then to be applied from January 1, 2030.

German Parliament passes Annual Tax Act 2024 with Changes affecting the MiKaDiv/ FASTER implementation

On October 18, 2024, the German Parliament passed the Annual Tax Act 2024. The Act includes, among others, important changes concerning the German WHT Reform and the timeline for implementation in Germany, including a de facto early implementation of FASTER in Germany.

MiKaDiv & FASTER to be Fully Aligned and Implemented by 2027 in Germany

The reporting standard under MiKaDiv and the reporting standard under the FASTER Directive are largely consistent in structure and content. This is partly due to Germany's successful efforts to incorporate elements of its own WHT Reform/MiKaDiv into the final FASTER draft agreed in May 2024. Additionally, Germany managed to ensure that the indirect reporting route under the German MiKaDiv concept, i.e. the information reporting along the chain of custody to the German paying agent in contrast to the direct reporting initially proposed for FASTER, is also recognized under FASTER.

If both reporting standards were implemented separately in Germany, significant bureaucratic burdens would arise for both the tax administration and the financial sector, despite their high congruency and alignment. This is because adjustments to the FASTER reporting standard would be necessary after having implemented the German WHT Reform - at least for cross-border dividend payments.

Therefore, the Annual Tax Act 2024 provides for an adjustment of the MiKaDiv reporting standard to the FASTER Directive to establish one unified reporting standard, which will effectively correspond the standard laid out in Annex II of the FASTER Directive. The due diligence obligations of financial intermediaries in Germany will not be altered by this adjustment.

Even though the legal and technical prerequisites for the CFI register procedure still need to be established, the new MiKaDiv & FASTER reporting standard can already be implemented beforehand in Germany. Consequently, the Annual Tax Act 2024 stipulates that the new MiKaDiv reporting obligations, originally scheduled for 2025, and the German reporting standard adjusted to the FASTER Directive will apply to dividend payments received after December 31, 2026. Germany will thus implement the FASTER reporting standard three years before the latest application date specified in the FASTER Directive.

Further Enhancement of Liability Provisions for the German Paying Agent and (Non-German) Sub-Custodians in the Chain of Custody

Among further amendments specified in the Annual Tax Act 2024, we would like to highlight one amendment with particular relevance for non-German custodians: In addition to the liability of the German paying agent for incorrect or incomplete transmission of relevant information to the Federal Central Tax Office and the resulting tax shortfalls or unjustified tax benefits, (non-German) sub-custodians shall also be liable for incorrect or incomplete data transmission along the custody chain. This implies genuine extraterritorial liability, depending on the structure of the custody chain.

Outlook

The Annual Tax Act 2024 with the amendments passed by the German *Bundestag* still requires the approval of the German *Bundesrat*, which could occur on November 22, 2024.

For affected custodians and financial intermediaries, the next few months will be crucial in determining how quickly the German Tax Administration can adapt its technical requirements for implementing the WHT Reform to the FASTER reporting standard. According to reports, the German Ministry of Finance has already reached out to various banking associations in Germany to establish a working group for this.

In practice, this will likely necessitate a complete overhaul of the previously published technical guidelines for MiKaDiv (including the Communication Handbook, XML Schema, etc.). It is also uncertain whether and when the reporting standards / implementing acts at the European level, which the European Commission has already started to work on, will be harmonized to the extent that they can be considered by the German Tax Administration.

Although the postponement to 2027 provides additional time for technical coordination and implementation, past experiences with MiKaDiv suggest that achieving the targeted implementation of a unified MiKaDiv reporting standard by 2027 will be a significant temporal and technical challenge for all parties affected. Affected custodians and financial intermediaries should use the additional time to prepare for implementation by 2027.

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