

MiKaDiv and the new mass data interface of the BZSt: Financial institutions in a race against time

At European level, the European Commission is currently working on the FASTER initiative to introduce a standardised digital relief system for foreign withholding tax. Like its neighboring countries Switzerland, Austria, and Denmark, the German tax authority is also adopting a digital reporting and submission procedure for withholding tax processing. The efforts of the German Federal Central Tax Office (BZSt) are highly commendable, although it is a complex undertaking for financial institutions and – as it usually is – the devil is in the details. Ulrich Vogl, Co-Founder and CTO of the withholding tax fintech RAQUEST, and Manfred Artmeier, Head of Growth at RAQUEST, have been dealing with the digitalisation efforts of the tax authorities for some time. We invited both withholding tax experts for an interview to shed light on the intentions of the Federal Central Tax Office (BZSt) and to understand the associated actions and challenges for financial institutions.

Question 1: Digitalisation in taxation has gained momentum. Provided all member states agree, FASTER is set to be implemented across Europe by 2027. The BZSt aims to roll out its digital interface by 2025, and simultaneously making the new reporting procedure MiKaDiv mandatory for custodian banks and domestic payors. What's the impetus behind this push for digitalisation?

Manfred Artmeier: The drive for digitalisation mainly stems from tax authorities' desire to reduce their workload. Presently, there are numerous reclaim submission channels with system breaks causing extra work. However, the primary impetus for digitalisation is the political will at an European level: the "European Capital Market" has to become more attractive again for investors. The FASTER initiative was also fuelled by the Capital Market Union. Behind this is the vision that the European capital market will keep pace with the US market in the future, necessitating the evolution of the tax system. Lobbying from the banking sector further propels the digitalisation efforts – a clear indication that if banks already offer a certain service level to their clients, whether institutional or private investors, they intend to maintain and improve this standard efficiently and digitally in the coming years.

Ulrich Vogl: Generally we welcome all these initiatives contributing to digitalisation in this financial sector. However, we hope for more coordination between the various dynamics in the future – both at the European level and specifically in the German capital market, to enhance their attractiveness to investors and ensure these initiatives are implemented without conflicting interests. Additionally, all

initiatives should provide long-term added value and be "cleanly" established. This includes the OECD's TRACE procedure, the EU's FASTER proposal, MiKaDiv in Germany, or the digital submission mechanisms for tax reclaim submissions in other countries.

Question 2: What does the digitalisation dynamic mean for financial institutions?

Manfred Artmeier: It presents both an opportunity and a risk. The opportunity lies in overall digitalising withholding tax processes, enabling banks to offer their services paperless and cost-effectively in the future. However, the downside is the immense time pressure. Once digitalisation is mandated by the regulator, banks must act swiftly and initially face extra work. Banks have limited IT resources that have to deal other regulatory issues simultaneously or dedicate more focus on more future-oriented topics, such as Open Banking. As a consequence banks could quickly risk being left behind, in the pace of digitalisation, if they lack strong digitalisation partner.

Ulrich Vogl: Digitalisation inevitably signifies greater data availability. This data needs to be collected, maintained, and integrated into the existing bank processes. This, in turn, might require banks to manage the additional workload previously handled by the tax authority. Therefore, the digitalisation dynamic might lead to a shift in work between financial institutions and authorities.

Question 3: With MiKaDiv, coming into effect from January 1, 2025, extensive reporting obligations fall on custodian banks and domestic paying agents. What practical implications arise from this and what impact will this have on financial institutions?

Ulrich Vogl: MiKaDiv – the Reporting Procedure for Capital Gains Tax on Dividends and Depository Certificates – mandates that German paying agents will be obligated, starting from January 1, 2025, to report capital gains on dividends through a digital process to the Federal Central Tax Office (BZSt). This requirement also applies to a foreign bank that pays out this income; in this case, the dividends need to be reported through the German paying agent, following the payment chain. German paying agents must thus develop a format by which they receive the necessary information for reporting from foreign banks. BZSt has not yet provided any detailed technical specifications for this, only content-related requirements. Ultimately, German paying agents, intermediaries and foreign banks must find a solution by 1 January 2025 as to how data exchange will be regulated in the future. Foreign banks in particular must determine in advance how they want to implement this procedure and then approach their custodians. German financial institutions that pay out dividends will have to engage directly with the reporting process to understand which information needs to be reported to the BZSt. In this regard, we appreciate the standardisation efforts of the different parties involved, such as the Association of Foreign Banks, to encourage the standardisation of these processes and data formats from the beginning. Ultimately, this will minimise the risk of each paying agent or intermediary setting up its own procedure, which would not lead to less, but to significantly more work for all parties.

Question 4: MiKaDiv reports are supposed to be submitted electronically directly through the interface to the BZSt. Simultaneously, the BZSt plans to provide a mass data interface for withholding tax reclaims. These are two completely separate and also technically distinct interfaces. How does MiKaDiv fit into the overall concept, and what function does the BZSt's mass data interface serve in the withholding tax reclaim process?

Ulrich Vogl: Generally tax reporting via the MiKaDiv interface is the prerequisite for being able to reclaim withholding tax at all via the BZSt's mass data interface. The obligation for German paying agents to issue a tax certificate will be replaced by the German MiKaDiv procedure, so that in future, tax certificates will only be issued for investors whose tax residence is Germany. For all those who are not tax-resident in Germany, only a digital report will be issued. This will result in a so-called order number, which will be needed to reclaim withholding tax. Starting from 2025, the identification number received via the MiKaDiv interface must be provided to the BZSt's mass data interface for reclaims; otherwise it will no longer be possible to reclaim withholding tax from abroad in future. To summarise, MiKaDiv thus replaces the previous tax certificate procedure in the future and is also the necessary prerequisite for being able to reclaim at all – in the end, everyone has to deal with MiKaDiv.

Manfred Artmeier: Provided the BZSt's mass data interface will be implemented in 2024 as we've long hoped, we will have reached an important milestone in Germany and finally realised a market standard in the reclaim system. Other countries in the EU have already implemented this procedure very well in practice – Switzerland is a good example for this. The BZSt's mass data interface supplements a currently impractical arrangement – the withholding tax reclaim via the BOP portal. Currently this procedure represents a significant disadvantage for the German capital market as taxes cannot be reclaimed in bulk (in terms of number of units), and there are considerable liability concerns as to whether banks are permitted to offer this service to their customers in this way. We are therefore in favour of implementing a mass data interface, which should be configured in line with standard market practice. In order to contribute our experience in the relevant areas, we have already started a dialogue with associations and the BZSt in the form of a user group so that a practical, investor-friendly interface can be developed.

Ulrich Vogl: It should also be mentioned that we have already received enquiries as to whether it makes sense to technically connect the BOP portal to the individual banking systems while the mass interface is not yet available. This is technically possible, but we would advise against it due to the enormous effort involved in such a transitional solution and for liability reasons.

Question 5: With the decision to only accept refund applications electronically in future, Germany is following the example of Switzerland and Denmark. This procedure will probably become the new standard in many countries. For financial institutions, this means that the tax authorities of many different countries will have to be connected. Is this even feasible?

Manfred Artmeier: Definitely yes! In fact, it makes things much easier for everyone involved. Electronic data transfer is easier, can be processed faster and is more cost-effective – in concrete terms, this means less manpower and less process effort. We therefore strongly believe that the switch to a digital process will result in more claims. Is it feasible for all banks? Also yes. However, for banks it is more a question of prioritising their own internal IT projects. Banks basically have three options for responding to the changes in terms of service: either financial institutions no longer offer the physical procedure of the reclaim service in the countries that are switching to the digital procedure – this would result in a loss of service for customers and each bank would have to check for itself whether there is also a customer promise. Or financial institutions offer a partial service for one or two main markets. The disadvantage of this solution would be the creation of a „patchwork“. Particularly in the case of end customers, banks could run the risk of creating a “patchwork” solution if, for example, a bank covers two of the customer's three investment markets in terms of service and the customer has to look for another service provider for reclaims from the third market. The third option for banks is to implement a holistic solution with the help of a service provider or tool. We at RAQUEST want to offer financial institutions a central platform for the refund of European withholding taxes in all invest-

ment markets, whether digitally or still on paper. For this reason, we are in various user groups, which gives us direct access to the latest information and developments and enables us to enter into dialog with the executive authority. With our accumulated knowledge, we have already set about implementing a suitable solution.

Ulrich Vogl: If a bank decides to offer withholding tax processing in its service portfolio, a “make” or “buy” decision must ultimately be made internally in advance. In this complex area, customers explicitly demand the third alternative and a “one fits all” solution, which we provide with RAQUEST. With our STTI interface, we have already created the basis for digital data transmission to various tax authorities (such as for the Danish, Swiss and Austrian markets). Banks can connect their systems to the RAQUEST STTI gateway. The gateway also offers standardisation for the various technologies and processes in the markets. If, on the other hand, banks develop their own digital interface, a different software solution must be implemented for each application market. Setting up, implementing and maintaining this „make” solution will be very costly for banks. For example, if the bank has customised ten of these interfaces for different markets, there is a very high probability that something would be changed again in the process chain within a year. The consequence of this would be a perpetual “backsteering” and the reason why many financial institutions will opt for a ready-made product and the „buy” option instead of an in-house solution in the future.

Question 6: A universal interface for all tax authorities would significantly speed up the authorities' digitalisation process process and minimise the workload. What other advantages does the RAQUEST STTI gateway have for financial institutions?

Ulrich Vogl: We have already touched on the advantages of our gateway in the previous question. Our RAQUEST STTI solution is an interface gateway that can be used to map different transmission technologies and formats. We are therefore talking about fast and seamless integration into existing systems and great scalability. It is an out-of-the-box solution for financial institutions, where we take care of all updates (including regulatory updates) and keep the interface up to date as part of a subscription. We also guarantee maximum reliability and security when transferring data, as all data is encrypted end-to-end.

Manfred Artmeier: It should also be emphasised that the RAQUEST STTI is already in use at 23 institutes and is therefore a proven industry standard. So far, we are not aware of any other gateway that has a similar level of coverage in Europe.

Question 7: With regard to the investor: Does digitalisation as a whole make it easier for investors to assert refund claims and does the end of the messenger solution and the change in the law regarding certificates of residence have a direct effect?

Ulrich Vogl: In general, we are seeing increasing digitalisation in all markets, which is to be welcomed. Particularly in the German market and in view of the BZSt's mass data interface, the paperless implementation must be emphasised. In future, all data will be sent digitally to the BZSt interface and will thus be deemed to have been applied for via a digital certificate. Investors will therefore benefit from the fact that refund claims can be submitted and processed faster and more cost-effectively by financial institutions thanks to the digitalisation and products such as RAQUEST. The negative aspect of this changeover, however, is the extensive variety of data that the BZSt would like to collect via the interface. This leads to significantly higher project costs for the banks. In most cases, however, it makes no sense for private investors to process withholding tax reclaims themselves. In the German investment market alone, it is difficult to keep track of all the individual regulations. In addition, every private investor would have to familiarise themselves with each of their investment markets and be familiar with all the relevant double taxation agreements – hardly anyone can do all of this.

Manfred Artmeier: We have roughly estimated that a shrewd private investor has an outlay of at least two vacation days per investment market in which they want to reclaim the withholding tax themselves. You have to be aware whether you invest this time in reclaiming the tax yourself or whether you hand this work over to the banks. This is because the area of withholding tax reclaims is and remains the core business of banks. The end of the messenger solution and the amendment to the German law on the new regulation of limited and gratuitous business assistance in tax matters and on the amendment of other regulations in the area of tax advisory professions should in future allow banks again to apply for residence certificates for their clients, even before the digital reclaim application is submitted. This makes the entire process leaner and even faster thanks to the simplified application for the certificate of residence and the subsequent electronic transmission to the BZSt – a double win!

Question 8: So it makes sense for banks to continue to provide withholding tax refunds for their customers. Does the BZSt have already published the necessary information, so that the institutions can prepare for the new procedure?

Ulrich Vogl: It certainly makes sense for banks to continue providing this service. Banks must slowly adapt to the new circumstances. On the one hand, the technical requirements must first be created for applications via the new mass data interface from 2024 and the necessary data must be integrated into the systems. However, there are no final specifications published for this yet, as the BZSt has only provided a draft so far. A second draft will be presented in a further user group at the beginning of December. We assume that this will then be mostly finalised so that banks can then deal with the specifications in concrete terms and take the necessary steps. In addition, the MiKaDiv procedure will also come into force from 2025 and every financial institution will be involved via its depository, i.e. via the payment chain. Institutions should initiate the necessary preparations now and contact the depository to clarify which components are required for a systemic implementation.

Question 9: That sounds like a long, challenging road ahead for financial institutions. You have already dealt intensively with the requirements. Where do you see the critical points?

Manfred Artmeier: A particularly critical aspect of the BZSt's mass data interface will be the short time window within which banks have to implement the changes. Developing and implementing a test system within these framework conditions will also be an additional challenge. The second major task that is currently emerging is that many financial institutions are undertaking such a changeover for the first time ever. Germany is an important investment market and therefore it is crucial for banks to implement this changeover to ensure that they do not lose customers or suffer a drop in service.

Ulrich Vogl: For the operational process within the financial institutions, this specifically means that claims for income from 2020 must be submitted via the new interface within 2024, as the paper form will already have been abolished by then. If the implementation does not take place on time, there is a latent risk of claims expiring.

Question 10: What is your recommendation for financial institutions to implement and prepare for the new procedures?

Manfred Artmeier: We advise financial institutions to prepare for changes, for example in processes and procedures or systems, and to exert influence in advance. This means exerting influence via associations or in exchange with technology providers such as RAQUEST until the final specifications are available and then implementing the changeover promptly. Financial institutions should also build up knowledge in this complex area as quickly as possible. This means that they should not only build up knowledge internally, but also take advantage of external training opportunities in this area. For example, RAQUEST has set up expert groups for both topics – for the MiKaDiv procedure and the BZSt mass interface – in order to be able to exchange information at industry level.

Ulrich Vogl: You always have to keep in mind that this is about German tax – German banks know their way around. Foreign banks rather less so. Very few or only a few large financial companies have access to a large specialist department with tax experts. It will therefore also be important for smaller and medium-sized foreign financial institutions to find implementation partners with in-depth expertise and tools.

As far as external knowledge building is concerned, RAQUEST offers a webinar specifically for the topic of MiKaDiv and the BZSt mass interface.

The webinar will take place on Wednesday, January 10, 2024 and will be held by our expert and CTO of RAQUEST Ulrich Vogl.



WEBINAR
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and the new German reclaim interface
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