KPMG Meijburg & Co Tax Lawyers

Political agreement reached on proposal for mandatory disclosure of reportable cross-border arrangements by intermediaries

On March 13, 2018, the European Council reached political agreement on the proposal for amending the Directive on administrative cooperation in the field of taxation (Directive 2011/16/EU or DAC). This is the latest in a series of EU initiatives in the field of the automatic exchange of information in tax matters. The revised Directive (DAC 6) introduces an obligation on intermediaries to disclose potentially aggressive cross-border tax planning arrangements and also provides the means for tax administrations to exchange information on these structures. The enhanced transparency requirement is a response to recent revelations on harmful tax practices and the use of offshore companies (the 'LuxLeaks', 'Panama Papers' and the 'Paradise Papers') and the disclosure rules proposed by the OECD in BEPS Action 12.

1. Proposal in short

DAC 6 introduces an obligation for intermediaries to disclose potentially aggressive tax planning arrangements to their tax authorities. The tax authorities must then exchange this information automatically with other tax authorities within the EU. DAC 6 does not dictate what penalties should be imposed, but leaves it to the Member States to implement effective, proportionate and dissuasive penalties.

2. What is a reportable cross-border arrangement

DAC 6 targets aggressive tax planning arrangements. It does not contain a definition of the term 'arrangement'. The concept of 'aggressive tax planning' is also not defined. However, an annex to DAC 6 lists a number of 'hallmarks' that are a strong indication of tax avoidance or abuse. A cross-border arrangement becomes reportable if it meets one or more of the hallmarks. Certain hallmarks can only be taken into account if a "main benefit" test is also satisfied. The main benefit test is drafted along the lines of the principle purpose test in BEPS Action 6 and is satisfied if it can be established that the main benefit or one of the main benefits which, having regard to all relevant facts and circumstances, a person may reasonably expect to derive from an arrangement is the obtaining of a tax advantage (this could also include avoidance of double taxation).

3. Hallmarks

The hallmarks are divided between generic and specific hallmarks and consist of five headings (A through E). Generic hallmarks (heading A) relate to the engagement between the intermediary and the taxpayer and are all covered by the main benefit test. Examples are confidentiality conditions in relation to other intermediaries or the tax authorities and/or fees that are contingent upon the amount of tax advantage derived from the arrangement.

The specific hallmarks that are covered by the main benefit test refer, for example, to:

- acquiring a loss-making company and using its losses to reduce the tax liability; the conversion of income into another category of revenue taxed at a lower level; circular transactions that result in the round tipping of funds (heading B),
- deductible cross-border payments that benefit from a full exemption or from a preferential tax regime at the level of the recipient; situations where the

recipient of the deductible payment is resident in a jurisdiction that imposes corporate tax at the rate of zero percent or almost zero percent (heading C).

Specific hallmarks that do not have to meet the main benefit test include deductible cross-border transactions where the recipient is not resident for tax purposes in any tax jurisdiction or is resident in a jurisdiction included on the EU blacklist. Another example is an arrangement that claims relief from double taxation in respect of the same item of income or capital in more than one jurisdiction. These specific hallmarks are also listed under heading C.

Other examples include specific hallmarks concerning arrangements designed to circumvent rules on the automatic exchange of financial information and beneficial ownership (heading D) and hallmarks concerning transfer pricing, for instance arrangements which involve the use of unilateral safe harbor rules, the transfer of hard-to-value intangibles or – provided an EBIT-test is met – some intra-group cross-border transfers of functions and/or risks and/or assets (heading E).

4. Who has to report

The burden of reporting cross-border arrangements falls primarily on the intermediary. An intermediary is any person who designs, markets, organizes or makes available for implementation or manages the implementation of a reportable cross-border arrangement. This definition is extended to persons who know or could reasonably be expected to know that they have undertaken to provide aid, assistance or advice with respect to a reportable cross-border arrangement. If there is no intermediary, the obligation to disclose shifts to the taxpayer that uses the arrangement. This can be the case, for example, because the taxpayer designs and implements an arrangement in-house, when the intermediary does not have a presence within the EU or where the intermediary cannot disclose the information because of a legal professional privilege.

Where there is more than one intermediary, all intermediaries involved have a filing obligation, unless an intermediary has proof that the arrangement has already been filed by another intermediary.

5. Timing

Intermediaries and relevant taxpayers need to disclose the reportable cross-border arrangements within thirty days beginning on the day they become available for implementation, the day after they are ready for implementation or when the first implementation step has been taken, whichever comes first. The subsequent automatic exchange of information will take place within one month of the end of the quarter in which the information was filed. The information must be communicated for the first time by October 31, 2020.

6. The information to be exchanged

The information that has to be exchanged includes: identification of taxpayer and intermediary; details of the hallmark(s); the date of implementation; the value of the transactions or series of transactions included in the reportable cross-border

arrangement; identification of the Member States involved and identification of any person in the other Member States likely to be affected.

This information is reported to the local tax authorities in each Member State. The local tax authorities will subsequently exchange that information automatically via a central directory on administrative cooperation. The competent authorities of all Member States will have access to that directory.

7. Entry into force

Information on cross-borders arrangements of which the first step was implemented between the date of entry into force (20 days after publication of DAC 6 in the official journal) and the date of application (July 1, 2020) will have to be reported by August 31, 2020.

Member States should implement the proposal by December 31, 2019, at the latest and apply the new legislation as of July 1, 2020. Once DAC 6 takes effect, the reported information will be automatically exchanged one month after the end of the quarter in which the information was filed. The first information will therefore be exchanged by October 31, 2020.

8. Comments by Meijburg & Co

DAC 6 goes beyond the recommendations of BEPS Action 12 and introduces a wide ranging exchange of information. The OECD recently also proposed mandatory disclosure rules, but these are only aimed at discouraging arrangements set up in order to circumvent CRS rules or to disguise the beneficial owners of assets held offshore. The nature of the EU rules currently agreed is much broader.

One of our main concerns, apart from confidentiality and privacy issues, is the fact that a crucial term in the draft proposal – the term 'arrangement' – is not defined at all. The wording of DAC 6 throughout is very broad and not always clear on every point. As a consequence, a wide range of transactions, including transactions that do not meet the definition of aggressive tax planning – such as arrangements set up to avoid double taxation – may potentially fall within the scope of DAC 6. We hope that local tax authorities will come up with clear guidance on the scope of these reporting obligations.

Although DAC 6 will, in principle, apply to all types of taxes levied by a Member State, it will not apply to value added tax, customs duties, excise duties or compulsory social security contributions.

Meijburg & Co
March 2018