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DAC6 - New Mandatory Rules Regarding Disclosure and Tax Reporting

By Arun Birla, Hannah Gray & Abigail Hung

What is DAC6?

The new EU Directive on Administrative Cooperation (commonly referred to as "DAC6") imposes obligations on "intermediaries" (and taxpayers in certain situations) to disclose any "cross-border arrangements" involving two EU Member States or a Member State and a third country. The transaction must be disclosed if it meets at least one of the Directive's specified "hallmarks".

The disclosure will be made by the intermediary (or taxpayer) to their Member State's tax authority. There will be a mandatory automatic exchange of information on such reportable cross-border arrangements via a centralised network established by the EU.

The new rules are borne out of the continuing worldwide focus on aggressive tax planning. The purpose of these new provisions is to increase transparency and to ensure EU tax authorities have early access to information regarding tax planning. In addition, the provisions are meant to deter taxpayers from implementing abusive tax schemes.

However, the widely-drafted scope of DAC6 will capture transactions that are not only tax-motivated, but also ordinary transactions that may have a ''potential tax effect'' despite the fact they are not driven by tax planning motives. There is no generic safe harbour for arrangements having an underlying commercial purpose or a de minimis value (although Member States may choose to include certain safe harbours in their domestic legislation).

Member States must adopt and publish national laws to comply with DAC6 by 31 December 2019, and the reporting requirement will be implemented by 1 July 2020. These laws will have retroactive effect with an obligation to report on all transactions since the date of the Directive's implementation on 25 June 2018.

The UK is expected to ratify the Directive despite the impact of Brexit.

Intermediaries and the Reporting Obligation

The responsibility of reporting rests, in the first instance, with the intermediary. An intermediary is broadly defined as an individual or business engaged in the designing, marketing, organising, making available for implementation or managing the implementation of, cross-border arrangements, as well as those who provide aid, assistance and advice (and those who know or could reasonably be expected to know that this relates to a cross-border arrangement).

This will catch tax advisers, accountants, banks and lawyers, although it is unclear whether it will include in-house legal teams.

If there is more than one intermediary involved in the arrangement, all intermediaries are required to report the arrangement, unless they have proof that the required information has already been filed. Disclosure only needs to be made once in respect of each cross-border arrangement.

The disclosure obligations will fall to the relevant taxpayer when external advice is taken from intermediaries, but all intermediaries are based outside the EU (and have no EU connection) or where all EU-based intermediaries are entitled to waive reporting on the grounds of legal professional privilege. An intermediary with legal professional privilege is required to inform the taxpayer (or another intermediary) of their obligation to disclose notwithstanding such waiver.

Intermediaries or, where applicable, taxpayers will be required to report information including (but not limited to):

1. information relating to the identification of the intermediaries and relevant taxpayers;
2. details of the hallmarks that make the cross-border arrangement reportable; and
3. a summary of the reportable cross-border arrangement.

Broadly, the relevant information must be filed with the UK tax authority within thirty days from the first to occur of:

1. the day after the reportable arrangement is ready for implementation;
2. the day after the reportable arrangement is made available for implementation; or
3. the day when the first step of the reportable arrangement has been made.

The penalties for failing to comply will be set by each Member State. The Directive requires the penalties to be effective, proportionate and dissuasive, but it is important to note that beyond potential national sanctions, non-compliance could result in reputational damage for the intermediaries or taxpayers if the tax authorities decide to publish those who have been non-compliant.

"Hallmarks"

DAC6 classifies the hallmarks as "generic" or "specific" hallmarks. The scope of the hallmarks is very wide.

For all generic hallmarks and certain specific hallmarks, the arrangement will only be reportable if an additional "main benefit test" is also met. This means that the reporting requirement will only be triggered where the main benefit or one of the main benefits of the arrangement, taking into account all relevant facts and circumstances, is to obtain a tax advantage (which should be construed widely).

Generic hallmarks look to the nature of the contract between an intermediary and the taxpayer; these hallmarks catch, for example, arrangements where there are certain contingent fees based on tax benefits or confidentiality arrangements.

Specific hallmarks include situations where there are certain uses and transfers of losses, transactions which involve related parties that include exempt taxpayers, exempt or preferentially treated receipts, and taxpayers in non-cooperative jurisdictions and transactions that concern certain transfer pricing issues.

Moving Forward

It is advisable that all parties establish a system of maintaining an internal record of all reportable transactions. Going forward, parties to transactions may want to formally agree on who will have the obligation to report and ensure that doing so will not breach any contractual obligations.

The wide scope of the new rules coupled with the retroactive effect and uncertainty as to how Member States will adopt DAC6 into domestic legislation mean that, going forward, it is prudent for both intermediaries and taxpayers to monitor developments relating to DAC6 closely.

A View from Europe

Italy

Italy has not yet implemented DAC6, nor has any material public or political debate started on the matter.

The Italian cooperative compliance legislation of 2014, which seems to be a rough predecessor to DAC6 (although not practically implemented as yet), included a specific provision implementing a programme to assist taxpayers in distinguishing aggressive tax planning. Known aggressive tax planning schemes would be published online by the Italian Tax Agency.

According to the existing Italian anti-tax abuse legislation, most (if not all) of the cases described in the hallmarks potentially represent a case of tax abuse. Thus, it is probable that the effect of DAC6 will be to radically hinder the organisation, designing and management of aggressive tax planning schemes in Italy.

France

To date, there has been no extensive debate in France about DAC6. However, it is anticipated that France will comply with the Directive in the near future.

Germany

Whilst DAC6 creates an obligation on the EU Member States to interpose DAC6 into national law by 31 December 2019, it does not create any direct immediate obligations vis-à-vis the intermediaries or taxpayers themselves. Germany has not yet transposed DAC6 into German law.

Since the obligation to report on relevant cross-border arrangements initiated from 25 June 2018 applies retroactively, the German legislator may align German domestic legislation closely to the wording of DAC6 in order to reduce the risk of the German law being challenged for creating retroactive obligations (which are typically unpopular).

As mentioned above, now that DAC6 has become effective across EU Member States, intermediaries and taxpayers should be aware of their obligations and should react accordingly, for example, collecting the respective information to be in the position to report to fiscal authorities at a later point in time. It could be possible that the German legislator extends the scope of arrangements to be reported and includes arrangements with tax impact in Germany only as within scope for the purposes of the German law. For those pure German arrangements, the German legislator may choose not to give retroactive effect to any reporting obligations, in order to reduce the risk of the new law being determined unconstitutional.

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If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

London

Arun K. Birla
44.020.3023.5176
arunbirla@paulhastings.com

Jiten Tank
44.020.3023.5133
jitentank@paulhastings.com

Hannah Gray
44.020.3023.5118
hannahgray@paulhastings.com

Abigail Hung
44.020.3321.1004
abigailhung@paulhastings.com

Frankfurt

Uwe Halbig
49 69 90.74.85.105
uwehalbig@paulhastings.com

Milan

Patrizio Braccioni
39.02.30414.210
patriziobraccioni@paulhastings.com

Paris

Allard de Waal
33.1.42.99.04.25
allarddewaal@paulhastings.com