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CCBE Guidance on certain aspects of the Tax Intermediaries Directive

(Directive amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements)

19/10/2018

On 13 March 2018, Member States reached agreement on a Directive for the mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements. The Directive is in the form of an amendment to the Directive on Administrative Cooperation in the field of taxation (the DAC), and introduces an obligation on intermediaries to disclose potentially aggressive tax planning arrangements, and also the means for tax administrations to exchange information on these structures.

Under the Directive, the definition of “intermediaries” is very broad, comprising any person responsible for designing, marketing, organising and managing the implementation of the tax aspects of a reportable cross-border arrangement. In addition, persons who provide, directly or indirectly, material aid or assistance in connection with the arrangement would fall within the scope of “intermediaries”. In case there is no intermediary because a taxpayer designs and implements a scheme in-house, or the intermediary is not within the EU, or is under legal professional privilege/professional secrecy, the obligation to disclose shifts to the taxpayer who uses the arrangement

Once in force, tax intermediaries who provide their clients with complex cross-border financial schemes that could help avoid tax will be obliged to report these structures to their tax authorities. In turn, EU Member States will exchange this information with each other, further increasing scrutiny around the activities of tax planners and advisers. The member states will be required to automatically exchange the information they receive through a centralised database. Member states will be obliged to impose penalties on intermediaries that do not comply with the transparency measures.

Essentially, the Directive is aimed at preventing aggressive tax planning by enabling increased scrutiny of the activities of tax intermediaries. The Directive establishes 'hallmarks' to identify the types of schemes to be reported to the tax authorities. The requirement to report a scheme won't imply that it is harmful, only that it may be of interest to tax authorities for further scrutiny. The proposal broadly reflects action 12 of the OECD's 2013 action plan to prevent tax base erosion and profit shifting

<u>CCBE points</u>

The final text may give rise to a number of difficulties with respect to

I. Hallmarks

II. Privilege/professional secrecy, and

III. (Retroactivity

CCBE delegations may wish to acquaint themselves with these issues.

I: Hallmarks

The Directive establishes 'hallmarks' to identify the types of schemes to be reported to the tax authorities. The provisions regarding hallmarks can be found in Annex I to this paper.

CCBE observations:

(a) The description of the hallmark provides that it is sufficient that the tax advantage is "*one of the main benefits*". This does not appear to be a proportionate requirement, as it appears contradictory that, in taking measures to tackle tax avoidance, the tax advantage does not have to be the "*main advantage*".

(b) The provisions also give rise to uncertainty with respect to the use of "*one of the main benefits*", thus not satisfying the general requirements that laws are required to be clear and certain.

(c) The use of the phrase *"may reasonably expect to derive"* with respect to *"may reasonably expect to derive from an arrangement is the obtaining of a tax advantage"* is very difficult to prove.

(d) Importantly, and in relation to the hallmarks, disclosure will be required where there are cross-border transactions which might involve allegations of mis-priced services or goods or inadequate economic substance in a given jurisdiction ("transfer pricing"). In this case, the hallmark requires disclosure where there is an "*arrangement involving a non-transparent legal or beneficial ownership chain*" with persons, legal arrangements or structures that do not "*carry on a substantive economic activity supported by adequate staff, equipment, assets and premises*". It will be difficult for legal intermediaries to form a view about such matters without undertaking what may be a considerable analysis of an arrangement of which they may only know part.

(e) The same can be said of the hallmark that relates to "*An arrangement involving an intragroup cross-border transfer of functions and/or risks and/or assets, if the projected annual earnings before interest and taxes (EBIT), during the three-year period after the transfer, of the transferor or transferors, are less than 50 % of the projected annual EBIT of such transferor or transferors if the transfer had not been made*." These are matters that simply may not be known to an intermediary.

II: Waiver and professional privilege/professional secrecy

The CCBE refers to the use of "*may*" in Article 8ab paragraph (5) (see Annex II to this paper):

5. Each Member State <u>may</u> take the necessary measures to give intermediaries the right to a waiver from filing information on a reportable cross-border arrangement where the reporting obligation would breach the legal professional privilege under the national law of that Member State. In such circumstances, each Member State <u>shall take the necessary measures to require intermediaries to notify</u>, without delay, any other intermediary or, if there is no such intermediary, the relevant taxpayer of their reporting obligations under paragraph 6.

Intermediaries may only be entitled to a waiver under the first subparagraph to the extent that they operate within the limits of the relevant national laws that define their professions.

(a) Preliminary comment

The CCBE is greatly concerned with the inclusion of an obligation on the part of an intermediary-lawyer to inform a client of the obligation to disclose the particular arrangements. The breach of any obligation of the intermediary is, under the current draft, within the scope of the penalty provisions of the Directive. Including an obligation of notification by a lawyer which can be penalised if breached undermines the protection afforded to legal privilege and professional secrecy elsewhere in the Directive. Including such an obligation would permit third parties (i.e. the tax authorities) to enquire into whether a lawyer has complied with the provision. This presumably would involve an examination of the correspondence between the client and the intermediary, thereby effectively overriding legal privilege/professional secrecy.

(b) What does "may" mean?

It is presumed that Member States agreed this term due to the variety of how privilege/ professional secrecy is applied across different EU Member States. This might also be that not all lawyers are covered for advisory work e.g. we understand that in Denmark with respect to tax, litigation is covered by privilege/ professional secrecy, but not in the case of advisory work.

Incidentally, and for background information, the original Commission proposal provided that "*Each Member State shall take the necessary measures to give intermediaries the right to a waiver from filing information on….."* – the "*shall*" has now been replaced by "*may*".

Delegations will need to check whether conceiving a scheme or implementing a scheme is covered by privilege/professional secrecy or not. This, in the opinion of the CCBE TAX Committee, is the possible explanation for the use of "*may*".

Assuming this activity is covered by privilege/professional secrecy the question is what does "*may*" mean. The CCBE Tax Committee believe that if privilege/ professional secrecy applies then the intermediary must *have the right to a waiver from filing information on a reportable cross-border arrangement where the reporting obligation would breach the legal professional privilege under the national law of that Member State.*

(c) Obligation to inform

The provision provides that in circumstances where the waiver is invoked due to privilege*" In such circumstances, each Member State shall take the necessary measures to require intermediaries to notify, without delay, any other intermediary or, if there is no such intermediary, the relevant taxpayer of their reporting obligations under paragraph 6."*

The CCBE is somewhat opposed to a situation whereby a lawyer would be required to prove, or to keep evidence, that he or she has notified the "*relevant tax payer of their reporting obligations* .." as having to disclose information and keep evidence of this may violate professional privilege/professional secrecy.

Indeed, in the view of the CCBE Tax Committee, the document whereby a lawyer informs his client about the existence of legislation, discusses to which extent said legislation is relevant for the client, and eventually issues advice as to whether or not the taxpayer should comply with said legislation, qualifies as an opinion that should be covered by legal privilege/ professional secrecy.

Ideally, when the directive is transposed, domestic legislation should simply quote that when the intermediary is a lawyer, the reporting is incumbent on the taxpayer. It is assumed that the lawyer has a general obligation to inform his client as part of his overall and continued obligation of information vis a vis his client. We understand that this is the way UK legislation on disclosure of tax avoidance schemes (DOTAS) is construed.

(d) Violating privilege/professional secrecy and sanctions

Violating privilege/professional secrecy is a penal offence in many countries.

Yet, lawyers are not bound by confidentiality in certain cases and under certain modalities regarding anti-money laundering reporting.

CCBE invites delegations to check that legislation regarding legal privilege/professional secrecy which will be put in place for the purpose of implementing "DAC6" will not go beyond what has been put in place for anti-money laundering purposes as, in the view of the CCBE Tax Committee, potentially tax aggressive cross border schemes are in all circumstances less serious and damageable than money-laundering.

(e) What if I do not comply with the requirement to inform the client?

The issue of not complying with the requirement to inform "*the relevant taxpayer of their reporting obligations"* may give rise to other national difficulties. For example, it has been suggested that in Germany, the obligation to advise the relevant taxpayer, and disclose to the authorities that you have advised the relevant tax payer, would mean that you have to report on yourself if you have not informed the relevant tax payer and this could amount to self-incrimination.

(III) Entry into force and the issue of retroactivity (see Annex III to this paper)

The Directive entered into force on 25 June 2018 and Member States have until 31 December 2019 to implement the Directive into their national laws and regulations.

The new reporting requirements will apply from 1 July 2020.

However, it should be noted that, according to the Directive any arrangements entered into as from the date of entry into force (which is 25 June 2018) will need to be reported by 31 August 2020. Therefore, in effect, any arrangement that is entered into from 25 June 2018 onwards is reportable.

This has the practical consequence that intermediaries and their clients will, as from 25 June 2018, need to monitor all tax advice provided with a cross-border dimension and all advice concerning reporting requirements in order to ensure that a future obligation to report can be properly fulfilled. This should be noted by CCBE delegations.

Even though this is not the first time that an EU Directive includes retroactive effects in the field of fight against tax evasion, there is a legal issue though regarding compatibility of this effective retroactivity with EU law and delegations are invited to evaluate to which extent the entry into force of a Directive before it is transposed by Member States into domestic legislation is compatible with the TFEU.

ANNEX

ANNEX to Point I "Hallmarks" – Extract from the Directive regarding Hallmarks

ANNEX IV

HALLMARKS

Part I. Main benefit test

Generic hallmarks under category A and specific hallmarks under category B and under points (b)(i), (c) and (d) of paragraph 1 of category C may only be taken into account where they fulfil the "main benefit test".

That test will be 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.

In the context of hallmark under paragraph 1 of category C, the presence of conditions set out in points (b)(i), (c) or (d) of paragraph 1 of category C can not alone be a reason for concluding that an arrangement satisfies the main benefit test.

Part II. Categories of hallmarks

A. Generic hallmarks linked to the main benefit test

1. An arrangement where the relevant taxpayer or a participant in the arrangement undertakes to comply with a condition of confidentiality which may require them not to disclose how the arrangement could secure a tax advantage vis-à-vis other intermediaries or the tax authorities.

2. An arrangement where the intermediary is entitled to receive a fee (or interest, remuneration for finance costs and other charges) for the arrangement and that fee is fixed by reference to: (a) the amount of the tax advantage derived from the arrangement; or (b) whether or not a tax advantage is actually derived from the arrangement. This would include an obligation on the intermediary to partially or fully refund the fees where the intended tax advantage derived from the arrangement was not partially or fully achieved. 3. An arrangement that has substantially standardised documentation and/or structure and is available to more than one relevant taxpayer without a need to be substantially customised for implementation.

B. Specific hallmarks linked to the main benefit test

1. An arrangement whereby a participant in the arrangement takes contrived steps which consist in acquiring a loss- making company, discontinuing the main activity of such company and using its losses in order to reduce its tax liability, including through a transfer of those losses to another jurisdiction or by the acceleration of the use of those losses.

2. An arrangement that has the effect of converting income into capital, gifts or other categories of revenue which are taxed at a lower level or exempt from tax.

3. An arrangement which includes circular transactions resulting in the round-tripping of funds, namely through involving interposed entities without other primary commercial function or transactions that offset or cancel each other or that have other similar features.

C. Specific hallmarks related to cross-border transactions

1. An arrangement that involves deductible cross-border payments made between two or more associated enterprises where at least one of the following conditions occurs: (a) the recipient is not resident for tax purposes in any tax jurisdiction; (b)

although the recipient is resident for tax purposes in a jurisdiction, that jurisdiction either: (i) does not impose any corporate tax or imposes corporate tax at the rate of zero or almost zero; or (ii) is included in a list of third-country jurisdictions which have been assessed by Member States collectively or within the framework of the OECD as being non-cooperative;

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(c) the payment benefits from a full exemption from tax in the jurisdiction where the recipient is resident for tax purposes;

(d) the payment benefits from a preferential tax regime in the jurisdiction where the recipient is resident for tax purposes;

2. Deductions for the same depreciation on the asset are claimed in more than one jurisdiction.

3. Relief from double taxation in respect of the same item of income or capital is claimed in more than one jurisdiction.

4. There is an arrangement that includes transfers of assets and where there is a material difference in the amount being treated as payable in consideration for the assets in those jurisdictions involved.

D. Specific hallmarks concerning automatic exchange of information and beneficial ownership

1. An arrangement which may have the effect of undermining the reporting obligation under the laws implementing Union legislation or any equivalent agreements on the automatic exchange of Financial Account information, including agreements with third countries, or which takes advantage of the absence of such legislation or agreements. Such arrangements include at least the following:

(a) the use of an account, product or investment that is not, or purports not to be, a Financial Account, but has features that are substantially similar to those of a Financial Account;

(b) the transfer of Financial Accounts or assets to, or the use of jurisdictions that are not bound by the automatic exchange of Financial Account information with the State of residence of the relevant taxpayer;

(c) the reclassification of income and capital into products or payments that are not subject to the automatic exchange of Financial Account information;

(d) the transfer or conversion of a Financial Institution or a Financial Account or the assets therein into a Financial Institution or a Financial Account or assets not subject to reporting under the automatic exchange of Financial Account information;

(e) the use of legal entities, arrangements or structures that eliminate or purport to eliminate reporting of one or more Account Holders or Controlling Persons under the automatic exchange of Financial Account information;

(f) arrangements that undermine, or exploit weaknesses in, the due diligence procedures used by Financial Institutions to comply with their obligations to report Financial Account information, including the use of jurisdictions with inadequate or weak regimes of enforcement of anti-money-laundering legislation or with weak transparency requirements for legal persons or legal arrangements.

2. An arrangement involving a non-transparent legal or beneficial ownership chain with the use of persons, legal arrangements or structures:

(a) that do not carry on a substantive economic activity supported by adequate staff, equipment, assets and premises; and

(b) that are incorporated, managed, resident, controlled or established in any jurisdiction other than the jurisdiction of residence of one or more of the beneficial owners of the assets held by such persons, legal arrangements or structures; and

(c) where the beneficial owners of such persons, legal arrangements or structures, as defined in Directive (EU) 2015/849, are made unidentifiable.

E. Specific hallmarks concerning transfer pricing

1. An arrangement which involves the use of unilateral safe harbour rules.

2. An arrangement involving the transfer of hard-to-value intangibles. The term "hard-to-value intangibles" covers intangibles or rights in intangibles for which, at the time of their transfer between associated enterprises:

(a) no reliable comparables exist; and

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(b) at the time the transaction was entered into, the projections of future cash flows or income expected to be derived from the transferred intangible, or the assumptions used in valuing the intangible are highly uncertain, making it difficult to predict the level of ultimate success of the intangible at the time of the transfer.

3. An arrangement involving an intragroup cross-border transfer of functions and/or risks and/or assets, if the projected annual earnings before interest and taxes (EBIT), during the three-year period after the transfer, of the transferor or transferors, are less than 50 % of the projected annual EBIT of such transferor or transferors if the transfer had not been made.'

ANNEX to point II – Extract from the Directive regarding Recital (8) and Article 8(ab)

II: Waiver and professional privilege/professional secrecy

Recital (8)

To ensure the proper functioning of the internal market and to prevent loopholes in the

proposed framework of rules, the reporting obligation should be placed upon all actors that are usually involved in designing, marketing, organising or managing the implementation of a reportable cross-border transaction or a series of such transactions, as well as those who provide assistance or advice. It should not be ignored either that, in certain cases, the reporting obligation would not be enforceable upon an intermediary due to a legal professional privilege or where there is no intermediary because, for instance, the taxpayer designs and implements a scheme in-house. It would thus be crucial that, in such circumstances, tax authorities do not lose the opportunity to receive information about tax-related arrangements that are potentially linked to aggressive tax planning. It would therefore be necessary to shift the reporting obligation to the taxpayer who benefits from the arrangement in such cases

Article 8ab "Scope and conditions of mandatory automatic exchange of information on reportable cross-border arrangement" (see in particular paragraph 5 highlighted in bold)

1. Each Member State shall take the necessary measures to require intermediaries to file information that is within their knowledge, possession or control on reportable cross-border arrangements with the competent authorities within 30 days beginning:

(a) on the day after the reportable cross-border arrangement is made available for implementation; or

(b) on the day after the reportable cross-border arrangement is ready for implementation; or

(c) when the first step in the implementation of the reportable cross-border arrangement has been made,

whichever occurs first.

Notwithstanding the first subparagraph, intermediaries referred to in the second paragraph of point 21 of Article 3 shall also be required to file information within 30 days beginning on the day after they provided, directly or by means of other persons, aid, assistance or advice.

2. In the case of marketable arrangements, Member States shall take the necessary measures to require that a periodic report be made by the intermediary every 3 months providing an update which contains new reportable information as referred to in points (a), (d), (g) and (h) of paragraph 14 that has become available since the last report was filed.

3. Where the intermediary is liable to file information on reportable cross-border arrangements with the competent authorities of more than one Member State, such information shall be filed only in the Member State that features first in the list below:

(a) the Member State where the intermediary is resident for tax purposes;

(b) the Member State where the intermediary has a permanent establishment through which the services with respect to the arrangement are provided;

(c) the Member State which the intermediary is incorporated in or governed by the laws of;

(d) the Member State where the intermediary is registered with a professional association related to legal, taxation or consultancy services.

4. Where, pursuant to paragraph 3, there is a multiple reporting obligation, the intermediary shall be exempt from filing the information if it has proof, in accordance with national law, that the same information has been filed in another Member State.

5. Each Member State may take the necessary measures to give intermediaries the right to a waiver from filing information on a reportable cross-border arrangement where the reporting obligation would breach the legal professional privilege under the national law of that Member State. In such circumstances, each Member State shall take the necessary measures to require intermediaries to notify, without delay, any other intermediary or, if there is no such intermediary, the relevant taxpayer of their reporting obligations under paragraph 6.

Intermediaries may only be entitled to a waiver under the first subparagraph to the extent that they operate within the limits of the relevant national laws that define their professions.

6. Each Member State shall take the necessary measures to require that, where there is no intermediary or the intermediary notifies the relevant taxpayer or another intermediary of the application of a waiver under paragraph 5, the obligation to file information on a reportable cross-border arrangement lie with the other notified intermediary, or, if there is no such intermediary, with the relevant taxpayer.

7. The relevant taxpayer with whom the reporting obligation lies shall file the information within 30 days, beginning on the day after the reportable cross-border arrangement is made available for implementation to that relevant taxpayer, or is ready for implementation by the relevant taxpayer, or when the first step in its implementation has been made in relation to the relevant taxpayer, whichever occurs first.

Where the relevant taxpayer has an obligation to file information on the reportable cross-border arrangement with the competent authorities of more than one Member State, such information shall be filed only with the competent authorities of the Member State that features first in the list below:

(a) the Member State where the relevant taxpayer is resident for tax purposes;

(b) the Member State where the relevant taxpayer has a permanent establishment benefiting from the arrangement;

(c) the Member State where the relevant taxpayer receives income or generates profits, although the relevant taxpayer is not resident for tax purposes and has no permanent establishment in any Member State;

(d) the Member State where the relevant taxpayer carries on an activity, although the relevant taxpayer is not resident for tax purposes and has no permanent establishment in any Member State.

8. Where, pursuant to paragraph 7, there is a multiple reporting obligation, the relevant taxpayer shall be exempt from filing the information if it has proof, in accordance with national law, that the same information has been filed in another Member State.

9. Each Member State shall take the necessary measures to require that, where there is more than one intermediary, the obligation to file information on the reportable cross-border arrangement lie with all intermediaries involved in the same reportable cross-border arrangement.

An intermediary shall be exempt from filing the information only to the extent that it has proof, in accordance with national law, that the same information referred to in paragraph 14 has already been filed by another intermediary.

10. Each Member State shall take the necessary measures to require that, where the reporting obligation lies with the relevant taxpayer and where there is more than one relevant taxpayer, the relevant taxpayer that is to file information in accordance with paragraph 6 be the one that features first in the list below:

(a) the relevant taxpayer that agreed the reportable cross-border arrangement with the intermediary;

(b) the relevant taxpayer that manages the implementation of the arrangement.

Any relevant taxpayer shall only be exempt from filing the information to the extent that it has proof, in accordance with national law, that the same information referred to in paragraph 14 has already been filed by another relevant taxpayer.

11. Each Member State may take the necessary measures to require that each relevant taxpayer file information about their use of the arrangement to the tax administration in each of the years for which they use it.

12. Each Member State shall take the necessary measures to require intermediaries and relevant taxpayers to file information on reportable cross-border arrangements the first step of which was implemented between the date of entry

into force and the date of application of this Directive. Intermediaries and relevant taxpayers, as appropriate, shall file information on those reportable cross-border arrangements by 31 August 2020.

13. The competent authority of a Member State where the information was filed pursuant to paragraphs 1 to 12 of this Article shall, by means of an automatic exchange, communicate the information specified in paragraph 14 of this Article to the competent authorities of all other Member States, in accordance with the practical arrangements adopted pursuant to Article 21.

14. The information to be communicated by the competent authority of a Member State under paragraph 13 shall contain the following, as applicable:

(a) the identification of intermediaries and relevant taxpayers, including their name, date and place of birth (in the case of an individual), residence for tax purposes, TIN and, where appropriate, the persons that are associated enterprises to the relevant taxpayer;

(b) details of the hallmarks set out in Annex IV that make the cross-border arrangement reportable;

(c) a summary of the content of the reportable cross-border arrangement, including a reference to the name by which it is commonly known, if any, and a description in abstract terms of the relevant business activities or arrangements, without leading to the disclosure of a commercial, industrial or professional secret or of a commercial process, or of information the disclosure of which would be contrary to public policy;

(d) the date on which the first step in implementing the reportable cross-border arrangement has been made or will be made;

(e) details of the national provisions that form the basis of the reportable cross-border arrangement;

(f) the value of the reportable cross-border arrangement;

(g) the identification of the Member State of the relevant taxpayer(s) and any other Member States which are likely to be concerned by the reportable cross-border arrangement;

(h) the identification of any other person in a Member State likely to be affected by the reportable cross-border arrangement, indicating to which Member States such person is linked.

15. The fact that a tax administration does not react to a reportable cross-border arrangement shall not imply any acceptance of the validity or tax treatment of that arrangement.

16. To facilitate the exchange of information referred to in paragraph 13 of this Article, the Commission shall adopt the practical arrangements necessary for the implementation of this Article, including measures to standardise the communication of the information set out in paragraph 14 of this Article, as part of the procedure for establishing the standard form provided for in Article 20(5).

17. The Commission shall not have access to information referred to in points (a), (c) and (h) of paragraph 14

18. The automatic exchange of information shall take place within one month of the of the end of the quarter in which the information was filed. The first information shall be communicated by 31 October 2020.'

ANNEX to point III- Extract from the Directive regarding “entry into force”

Article 2

1. Member States shall adopt and publish, by 31 December 2019 at the latest, the laws, regulations and administrative provisions necessary to comply with this Directive. They shall immediately inform the Commission thereof.

They shall apply those provisions from 1 July 2020.

When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.

2. Member States shall communicate to the Commission the text of the main provisions of national law which they adopt in the field covered by this Directive.

Article 3

This Directive shall enter into force on the twentieth day following that of its publication in the Official Journal of the European Union