DAC 6
ARE YOU READY FOR THE NEW EU REPORTING REGIME?

BRYAN CAVE LEIGHTON PAISNER

DAC 6 is a new regime under which intermediaries and/or taxpayers must report to an EU tax authority information about cross-border arrangements with a view to the information being exchanged with other EU tax authorities.

The new regime will go fully live on 1 July 2020, but it will be back-dated to include cross-border arrangements in which the first step was taken on or after 25 June 2018 ("the two year look back period").

Many EU countries have now implemented the Directive (Directive 2018/822) into their local law and are in the process of issuing guidance, but a lack of clarity on the scope of the rules remains.

What is reportable?

An arrangement is reportable if it is "cross-border" and bears one or more of the designated hallmarks summarised in the Table at the end of this note.

Essentially, a "cross-border" arrangement is one which concerns either at least two EU member states, or at least one EU member state and a third country. For these purposes the UK is viewed as if it were still a member of the EU. Once we are through the transitional period for Brexit in the UK we are expecting the UK Government to issue amending legislation to continue the application of DAC 6 to the UK.

Although for some hallmarks a tax advantage must be a main benefit of the arrangement, this does not apply to all of the hallmarks. For a number of the hallmarks the arrangement may be purely commercial or motivated by reasons other than tax. Consequently, this is not just a tax reporting regime.

There is no *de minimis* exemption; DAC 6 applies to high and low value or even, in some cases, to no value transactions.

Examples of transactions which may be reportable in the UK

Main benefit test required	Main benefit test not required
Confidentiality condition to not share information in a tax report or tax opinion for a transaction (including in the context of non-reliance language) (**A1**)	Intragroup cross-border reorganisation where the transferor is projected to lose more than 50% in earnings over the next 3 years (**E3**)
An adviser, bank, trust company or anyone else involved with the arrangement is entitled to a premium fee (or return) or contingent fee (or return) geared to the tax advantage **(A2**)	Liquidation of an SPV holding property after acquisition of the SPV with an associated cross-border transfer of the property where the SPV is not projected to be loss making (**E3**)
Transactions where the client is presented with standardised documents or a structure requiring little or no customisation, e.g. a "plug and play" structure or set of documentation (**A3**)	Transfer of intangibles (IP and/or goodwill) between associated persons where the intangible is "hard to value" (**E2**)
Use of Jersey, Guernsey, BVI in a structure where there is a tax deductible payment (e.g. rent, interest, royalty payment or a payment for services) made cross border between associated persons where recipient is tax resident in a tax haven such as Jersey/Guernsey/BVI (jurisdictions with a 0%, or under 1%, corporate tax rate) (**C1**)	Use of entity in Cayman (or certain other jurisdictions blacklisted by the EU or OECD) in a structure – specifically where there is a tax deductible payment (e.g. rent, interest, royalty payment or a payment for services) made cross border between associated persons where recipient is tax resident in a blacklisted jurisdiction. (Blacklisted by the EU or OECD as non-cooperative) (**C1**)

Who has the obligation to report?

The duty to report will fall primarily on intermediaries involved with the arrangement where the intermediary has an "EU connection".

A person is an intermediary with an EU connection if they are resident in an EU member state or have a permanent establishment (PE) in a member state through which the relevant services are provided or they are incorporated in, or governed by, the laws of a member state or registered with a professional association there.

Where there is no intermediary with a reporting obligation (this could be because there isn't an intermediary with an EU connection or the intermediaries are exempt from reporting because of legal professional privilege), a relevant taxpayer could have a reporting obligation. They will have to report where they are sufficiently connected to the EU. This will be satisfied where they are resident in an EU member state or have a PE in a member state benefitting from the arrangement or (in contrast to the test for an intermediary) they either receive income or generate profits in a member state or carry on an activity there.

Even where the intermediary reports on the arrangement the relevant taxpayer may have a further reporting obligation depending upon local implementation. For instance in the UK this may be because the intermediary does not report all of the reportable information (and the relevant taxpayer needs to "top up" that information in a follow up report) or where an annual reporting obligation applies. The UK also requires ongoing annual information about any continuing tax advantage from the arrangement.

Note that an arrangement will be reportable even where there is no intermediary: if it is devised in-house, it could be reportable.

Could this mean multiple reporting?

This is possible. An "intermediary" is drafted broadly. Under the Directive it could be either:

a "promoter" – any person who designs, markets, organises or makes available for implementation or manages the implementation of a reportable cross-border arrangement; or

a "service provider" – any person who knows or could be reasonably expected to know that they have provided aid, assistance, or advice with respect to designing, marketing, organising, making available for implementation or managing the implementation of a reportable cross-border arrangement.

Consequently, there could be multiple intermediaries with reporting obligations on the same matter. Intermediaries include, for instance, lawyers, accountants and other professionals, as well as banks providing finance for an arrangement and potentially fund managers. Intermediaries could also include in-house teams providing advice for someone else in the group.

However, exceptions mean that multiple reporting may be avoided:

- *Lack of knowledge defence* Unlike a promoter, a service provider is not required to report if it did not know and could not reasonably be expected to know that they have provided aid, assistance or advice in relation to a reportable cross-border arrangement. There is some uncertainty as to the extent to which any intermediary must carry out additional due diligence to establish whether the arrangement is a reportable cross-border arrangement. In the UK HMRC draft guidance provides that a firm does not have to do any more due diligence than they would normally do in the course of a transaction.

- *Legal professional privilege* A lawyer may not be obliged to report if this would breach 'legal professional privilege' but, in such a case, the lawyer would be required to notify any other relevant intermediary or, if none, the relevant taxpayer to whom the arrangement has been made available of their reporting obligation. There are local variances in the legal professional privilege exemption.

- *Reliance* An intermediary can avoid reporting where it has evidence that another intermediary has already reported the information it was required to report.

- *Reporting by the entity in another jurisdiction* Similarly, an intermediary or relevant taxpayer can avoid reporting the same information to multiple member states.

These exemptions are designed to facilitate a single report by one intermediary and prevent multiple reporting, but multiple reporting may still arise for various reasons.

When should I report?

The Directive is being changed to allow for member states to adopt a 6 month deferral for the initial reports. However, the new reporting deadlines do not change the matters that will be reported. The same two year look back period applies and the regime still goes live on 1 July 2020; it just gives more time for reporting for the initial reports.

The UK has announced that it will exercise the 6 month deferral option. Accordingly, in the UK the following reporting deadlines apply:

- For arrangements where the first step in the implementation took place between 25 June 2018 and 30 June 2020 - reporting is due 28 February 2021.

- For arrangements where the trigger for reporting falls between 1 July 2020 and 31 December 2020 – reporting is due within the period of 30 days beginning on 1 January 2021. Reporting could be triggered by any of: arrangements made available (or ready) for implementation, or where the first step in the implementation takes place, or a service provider provides aid, assistance or advice. (Essentially this transitional period creates a second type of "catch-up" reporting in addition to reporting for the two year look back).

- For arrangements where the trigger for reporting arises on or after 1 January 2021 – reporting is due within 30 days as before. This is within 30 days of the earliest of the arrangement being made available for implementation (or ready for implementation) or when the first step to implement the arrangement occurs or, in addition, for service providers, when their aid, assistance or advice has been given.

Given the limited 30 day window to report for live matters from 1 January 2021 it is therefore important to understand when the reporting triggers arise. It is possible that these may arise at different times for different intermediaries, which may make reliance on another's report harder in some cases.

The deadlines above apply for the intermediary or relevant taxpayer (depending upon who has the reporting obligation). In addition, as mentioned above, there is an annual limited reporting obligation on the relevant taxpayer where they are sufficiently connected to the EU.   The taxpayer has to report on any continuing tax advantage from the arrangement.

What needs to be reported?

The information required to be reported includes:

- Identification of the intermediaries and the relevant taxpayers and any relevant associated person (where appropriate)
- Details of the applicable hallmarks
- Summary of the reportable cross-border arrangement
- Date of first step to implement it
- Details of relevant national provisions
- Value of reportable cross-border arrangement
- Member state of the relevant taxpayers and any other member state that may be concerned with it

Consequences of failure to report

There are significant penalties for non-compliance, with local variances. In the UK these are generally likely to be up to £5K and in the worst cases, there is a cap at £1m per transaction. In France, the first offence within 3 years is punished by a 5,000 € penalty, then a 10,000 € penalty per offence up to a cap of 100,000 € per year. In Germany the penalty is a maximum of 25,000 € per violation.

Under the UK rules no penalty will be imposed on a person where they have reasonable procedures in place to identify reportable cross border arrangements and secure compliance with the rules. Many businesses are looking at portals (internally or externally developed) that identify transactions and provide an audit trail for compliance. This is combined with education and training across the business so that all relevant operators (and not just those in tax departments) are able to identify relevant transactions.

How will this impact on a multinational?

DAC 6 means greater transparency of arrangements with EU tax authorities, including greater transparency of fairly commercial transactions. It not only applies to EU groups, it could also apply to multinational groups headed by a non-EU entity. This would be where they are participating in a cross-border arrangement involving the EU. Whether or not the multinational is advised by an EU firm (or an EU office within an international firm) the matter may still have to be disclosed to the EU tax authorities because of a secondary reporting obligation falling on the taxpayer. Where there is a relevant taxpayer with an EU connection (as described above) within the multinational group participating in the arrangement they may have a reporting obligation in the event that an intermediary does not.

What should you be doing now?

Reviewing transactions you have been involved with (either as an intermediary or a taxpayer) for the two year look back reporting. The two year look back reporting applies where the first step to implement the arrangement was taken between 25 June 2018 and 1 July 2020 and reporting is due as discussed above.

Determine for those transactions whether they are reportable, and if so, where, and by whom. There may be many intermediaries on the same matter, including in-house teams.

For live matters which are reportable where the first step was not implemented before 1 July 2020 (which could include arrangements that are not even implemented) work out a system to quickly identify reportable arrangements given the shorter reporting period.

Ideally pursue reporting by one person where this is possible. This is likely to involve taxpayers and intermediaries working out which intermediary is best placed to do the report that others may rely upon. Lawyers will need to navigate their way through any privilege obligations and any resulting notification requirements.

In the UK, where there is a defence against penalties for reasonable procedures, ensure that those procedures are established, including training and education across the impacted business (and not just the tax department).

Hallmark summaries

The following is a summary of the hallmarks and indicates where the main benefit test is required.

The main benefit test is satisfied where the main benefit or a main benefit reasonably expected from the arrangement is the obtaining of a tax advantage. This is an objective test.

Hallmark A		**Main benefit test required?**
Targeting general features of a tax avoidance arrangement		
A1	Confidentiality undertakings being given which could prevent disclosure of how the arrangement secures a tax advantage	✓
A2	Fees are tax based or contingent on or refundable by reference to a tax advantage	✓
A3	Substantially standardised documents and/or structure	✓

Hallmark B		
Targeting specific tax planning structures within a tax avoidance arrangement		
B1	Contrived acquisition of a loss-making company and using or transferring its losses	✓
B2	Converting income into capital or other revenues taxed at a lower rate or exempt from tax	✓
B3	Circular transactions resulting in round tripping of funds	✓
Hallmark C		
Including arrangements which feature tax mismatches between the different jurisdictions involved		
C1	Deductible cross-border payments between associated persons where:	
(a)	Recipient is not tax resident in any tax jurisdiction	✗
(b)(i)	Recipient is resident in a jurisdiction that has no corporate tax or a zero (or almost zero) rate of corporate tax	✓
(b)(ii)	Recipient is resident in a jurisdiction regarded as non-cooperative by EU or OECD	✗
(c)	Payment is tax exempt in recipient's tax jurisdiction	✓
(d)	Payment benefits from preferential tax regime in recipient's tax jurisdiction	✓
C2	Deductions are claimed for the same depreciation on an asset in more than one jurisdiction	✗
C3	Double tax relief is claimed in respect of the same item of income or capital in more than one jurisdiction	✗
C4	Transfer of assets where consideration is treated differently, to a material extent, in the jurisdictions involved	✗
Hallmark D		
Arrangements undermining the common reporting standard and similar		
D1	Arrangement which may have the effect of undermining automatic exchange of financial account information	✗

D2	Arrangement involving a non-transparent legal or beneficial ownership chain	✗
Hallmark E		
Arrangements relating to transfer pricing		
E1	Arrangement involving use of unilateral safe harbour rules from transfer pricing	✗
E2	Transfer of "hard-to-value intangibles" (for the purposes of transfer pricing) between associated persons	✗
E3	An intragroup cross-border transfer of functions, risks and/or assets if transferor's EBIT reduces by more than 50% as a result	✗

If you have any queries about the operation of the DAC 6 regime, please speak to your usual BCLP contact or Alan Sinyor (Alan.Sinyor@bclplaw.com) or Anne Powell (anne.powell@bclplaw.com).

