Euro Tax Flash from KPMG's EU Tax Centre

European Commission proposal on disclosure requirements for intermediaries

Automatic exchange of information — Mandatory disclosure — Intermediaries — Aggressive tax planning arrangements

On June 21, 2017, the European Commission published its proposal for mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements. The proposal comes 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.

Background

In the light of recent revelations on harmful practices and the use of offshore companies (the so-called 'LuxLeaks' and 'Panama Papers'), the European Parliament, in its July 2016 resolution on tax rulings, has called on the Commission to introduce tougher transparency requirements for intermediaries. The ECOFIN Council also invited the Commission to consider initiatives on mandatory disclosure rules in line with those proposed by the OECD in Action 12 of the Base Erosion and Profit Shifting (BEPS) initiative.

The Commission's Proposal

While the Commission recognizes that some transactions and structures are used for genuine reasons, it also notes that others may not be legitimate. It therefore considers it necessary for intermediaries to be required to report to the tax authorities on potentially aggressive tax planning arrangements in which they are involved.

Disclosure obligation

Intermediaries are defined as any EU-established or resident person that is engaged by a taxpayer to provide taxation services (including material aid, assistance or advice) involving designing, marketing, organizing or managing the implementation of the tax aspects of a reportable cross-border arrangement.

In the absence of an intermediary (e.g. the obligation is not enforceable upon an intermediary due to legal professional privilege, the intermediary is located outside the EU or because an arrangement is developed in-house), the obligation to disclose falls on the taxpayer – defined as any person that uses a reportable cross-border arrangement to potentially optimize their tax position.

Reportable arrangements

The reporting obligation is limited to cross-border situations, i.e. arrangements that involve more than one Member State or a Member State and a third country. An arrangement is reportable if it satisfies at least one of the features and elements that the Commission considers a strong indication of tax avoidance or abuse – referred to as 'hallmarks' and listed in an Annex to the proposal. Both generic hallmarks (in heading A) and specific hallmarks (in headings B to E) are listed. Hallmarks in A and B can only be taken into account if a "main benefit" test is also satisfied.

The main benefit test is satisfied if the main benefit of an arrangement or series of arrangements is to obtain a tax advantage. The test also refers to "taking advantage of the specific way that the arrangement or series or arrangements are structured". While the drafting is not clear, this may mean that inserting a tax-driven step into an otherwise totally commercial transaction could make it reportable.

Generic hallmarks (in heading A) include arrangements where:

- The taxpayer undertakes to comply with a confidentiality condition (in relation to other intermediaries or the tax authorities);
- The intermediary is entitled to a fee contingent on either the amount of tax advantage derived from the arrangement or on the advantage being obtained;
- Standardized documentation (including standard forms) is used.

Specific hallmarks are classified as follows:

- Heading B. Those that may be linked to the main benefit test: the use of losses to reduce a taxpayer's tax liability, conversion of income into categories that are taxed at a lower level and circular transactions that result in the round-tripping of funds;
- Heading C. Specific hallmarks relating to cross-border transactions: these include cross-border payments between related parties where the receipt is subject to a partial or full exemption from tax or benefits from a preferential regime; where the recipient is in a country which imposes corporate income tax at less than half the average rate in the EU or is on list of countries with harmful tax regimes; and where there is a hybrid mismatch with a third country. It also covers cases where depreciation on the same asset is given in multiple jurisdictions or more than one taxpayer can claim double tax relief irrespective of whether or not the parties are related;
- Heading D. Arrangements designed to circumvent automatic exchange of information with the aim of avoiding the reporting of income to the state of residence; and
- Heading E. Transfer pricing: arrangements that do not satisfy the arm's length principle or the OECD transfer pricing guidelines and arrangements that should be the subject of automatic exchange of information on advance rulings but which have not been reported or exchanged.

The Commission may subsequently update the Annex to include arrangements identified through the operation of the Directive.

Timing

Where an intermediary is involved, disclosure should be made before the scheme is implemented, i.e. within five days beginning on the day after the reportable arrangement has become available to the taxpayer. Where the obligation is shifted to the taxpayer, the timing of disclosure should be within five days beginning on the day after the arrangement (or the first step in a series of reportable schemes) has been implemented.

Exchange of information

The disclosed information will be exchanged automatically every quarter of a year via a central directory on administrative cooperation in the area of taxation. A standard form will be developed and will include the identification of the taxpayers and intermediaries involved, the hallmarks that generated the reporting obligation and details of the arrangement and the relevant domestic tax rules.

National tax authorities of all Member States have access to the directory. However, the exchanged information will not be made available to the public and the Commission will only have access to it insofar as needed for the monitoring of the functioning of the Directive.

Sanctions

The proposal leaves it to Member States to introduce sanctions for failing to comply with the Directive's requirements. However, penalties must be "effective, proportionate and dissuasive".

Next steps

The legal basis for the Commission's proposal is Article 115 of the Treaty on the Functioning of the EU (TFEU), which requires unanimity in the Council. The legislative procedure for amendments to the DAC is consultation, meaning that the Council will adopt the text once the Parliament and any relevant Committees have given their (non-binding) opinions.

The Commission proposes that the provisions of the Directive should apply as of January 1, 2019, and that the first information should be exchanged by the end of the first quarter of 2019. It is also noted that Member States should require intermediaries and taxpayers to disclose by March 31, 2019 any reportable arrangements implemented between the date when political agreement is reached on this proposal and December 31, 2018.

In the Explanatory Memorandum accompanying the proposal, the Commission notes that its benefits could be complemented by the introduction of a similar reporting obligation for auditors. The Commission is therefore considering a future legislative initiative requiring auditors to disclose any potentially aggressive tax planning arrangements they discover in the course of their professional activities.

EU Tax Centre comment

The Commission considers tax transparency to be one of the key pillars for a fair tax system and a properly functioning internal market and this proposal is only the latest in a series of initiatives in this area. A series of instruments have already been introduced, including rules implementing the Common Reporting Standard (CRS) in the EU, the mandatory automatic exchange of information on advance cross-border rulings and on country-by-country reporting (CbCR) and the Directive on Double Taxation Dispute Resolution Mechanisms (DTDRM) in the EU. The proposed rules requiring multinationals to report their tax bills (also CbC) is expected to be discussed in the European Parliament plenary session in the near future, after the Committees responsible failed to reach the qualified majority needed to enter into negotiations with the Council.

Should you have any queries, please do not hesitate to contact KPMG's EU Tax Centre, or, as appropriate, your local KPMG tax advisor.

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