AND THE BLAME GOES TO … EU TAX INTERMEDIARIES

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Introduction

In June 2017, the European Commission released the fiercely debated proposal for a directive to introduce mandatory disclosure rules in the area of taxation (Proposal) in the European Union (EU)[1].

The proposed legislation is highly relevant to EU tax professionals but also to enterprises with activities in the EU, implementing tax planning structures that could potentially be regarded aggressive. Specifically, such enterprises may under certain circumstances have own obligation to report information to national tax authorities. In any case, they must be aware that potential tax planning structures they might use shall become reportable and subject to automatic exchange of information among Member States[2], once the Directive is implemented.

Mandatory Disclosure Rules have been examined by the OECD in the framework of the Base Erosion and Profit Shifting (BEPS) Project[3] and in particular in Action 12 (Disclosure of Aggressive Tax Planning). It was concluded that relevant legislation should be straightforward, precise as to identification of the structures triggering disclosure obligations, effective, flexible and limited by the principle of proportionality[4].

Legislative action to this effect at EU level was conceived to respond to Panama Papers leaks. Committed to eliminate such phenomena, the Commission listed one year ago (in July 2016), a number of measures to enhance tax transparency in the EU and improve the function of the Single Market[5]. Amongst others, anti-money laundering legislation, beneficial ownership, whistleblowers' protection and increased oversight of tax advisors' activities were brought forward. As a result, the rules examined herein are promoted as complementary to other legislative measures, already adopted or under consideration.

The specific purpose assigned to these rules is twofold:

(i) to ensure that Member States are promptly informed on aggressive tax planning schemes and can react effectively and

(ii) to discourage tax professionals from involvement with arguable arrangements.

The essence of the new rules lies with the obligatory reporting to Member States' tax authorities of cross-border arrangements involving at least one Member State before implementation, where possible, or following first taxpayer's implementing actions[6]. The obligation is triggered where the arrangements have one or more of the features identified in the Proposal as hallmarks[7]. In particular, there are four categories of hallmarks:

(i) generic,

(ii) specific, linked to the so-called main benefits test,

(iii) specific, related to cross-border transactions and

(iv) specific related to automatic exchange of information in the EU.

1 European Commission, Proposal for A Council 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, COM(2017)335 final, June 2017, available at: https://ec.europa.eu/taxation_customs/business/company-tax/transparency-intermediaries_en

2 The new rules are suggested to be inserted as amendment to the existing Directive regarding Administrative Cooperation (Council Directive 2011/16/EU - DAC). Thus the scope of the DAC shall be expanded.

3 According to the OECD BEPS "refers to tax avoidance strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations." Identifying appropriate actions to tackle BEPS at international level has been the mission of the inclusive framework, consisting of over 100 jurisdictions. Cf. OECD, About BEPS and the Inclusive Framework, available at: http://www.oecd.org/tax/beps/beps-about.htm

4 OECD, Mandatory Disclosure Rules, Action 12 – 2015 Final Report, 2015.

5 European Commission, Fair Taxation: The Commission Sets Out Next Steps To Increase Tax Transparency and Tackle Tax Abuse, Press Release, July 2016.

6 The deadline for the fulfillment of the obligation depends on the reporting subject. In principle. tax intermediaries designing or implementing suspicious arrangements must report them within 5 days from their complete communication to the taxpayer. Nevertheless, taxpayers may proceed with reporting after the first implementing actions.

7 Cf. Annex to the Directive "Hallmarks".

Arrangements with features of categories (i) and/or (ii) fall under the Proposal's scope provided that their principal foreseeable implication is tax-related (main benefits test). Category (iii) includes a set of identified strong indicators of tax avoidance and aggressive tax planning, e.g. arrangements involving entities without tax residence or exploiting mismatches of different national tax laws. Finally, category (iv) refers to features indicating intention to circumvent legislation on automatic exchange of information.

Primary reporting obligation is imposed on EU tax intermediaries[8]. Tax intermediaries are defined very broadly, apparently with a view to catching all professionals that might assist to the realization of the suspicious arrangements[9]. Hence any person (i) responsible towards a taxpayer for the "design, marketing, organization and/or management" of suspicious arrangements or (ii) materially assisting with the above activities may qualify as intermediary under the scope of the rules. It is clarified that where several persons are equally liable to reporting as intermediaries, the main obligation shall lie with the one(s) assigned with the arrangement's design and/or implementation.

However, there are cases of tax intermediaries that either fall outside the scope of the Proposal or can be exempted from the respective obligations. As said above, the new rules are limited to EU tax intermediaries. Consequently, persons that are not sufficiently connected with any EU Member State, under one of the four criteria provided in the Proposal, do not have reporting obligations. Furthermore, persons qualifying as intermediaries but enjoying legal professional privilege in their Member State have the right to waive the discussed obligations. Where no intermediary has reporting obligations, either for one of the above reasons or because the suspicious arrangement is designed and implemented without involvement of tax professionals, the reporting duty falls on the relevant taxpayer.

It is questionable whether the Proposal is fit for the purposes assigned thereto. The most alarming question arising upon its reading refers to the definition of "arrangement". Despite the fact that the Proposal's whole essence is the reporting of arrangements, no clear delimitation of the term is given. Similar question-marks emerge in relation to other core parts of the Proposal. Indicatively, it is arguable when an arrangement is made available by the intermediary to the taxpayer for implementation, thus triggering reporting obligations. Similarly, clarifications are indispensable for the application of the main benefits test. From the above arises a clear and direct risk of tax uncertainty, with harmful implications for the function of the Single Market and its attractiveness to foreign investment. In addition, such measures could be held to undermine existing rules on tax professionals' conduct (e.g. professional codes of conduct) as well as their intrinsic professional ethos.

Another weak point of the Proposal relates to the extent compliance therewith may be enforced. Firstly, it is not clear how Member States (and the Commission) will verify fulfillment of disclosure obligations, especially to the extent they refer to arrangements not revealed otherwise (e.g. through Country-by-country reporting). Secondly, monitoring the success of the regime shall be especially challenging taking into account lack of data on arrangements not disclosed. Most importantly, taxpayers willing to take the risk linked with aggressive tax planning can always address to non-EU intermediaries, not covered by the regime. From this perspective, the regime could drive demand and offer of tax consulting services outside the EU without actually reducing aggressive tax planning in the Single Market.

Additionally, the Proposal risks to undermine the positive implications connected with and expected from cooperative compliance programmes, increasingly adopted around the EU. It has been repeatedly verified that cooperation between tax authorities and taxpayers can enhance significantly tax compliance in a globalizing tax arena[10]. Successful cooperation though pre-requires mutual transparency and trust as well as fair allocation of administrative and compliance burden between the parties. Nevertheless the measures envisaged in the Proposal introduce unbalanced new burdens for taxpayers and their advisers while building on generalizing assumptions as regards the latter.

Concluding, fairness in taxation is not only about fair distribution of tax burden but also – or more – about establishment of fair procedures and respect of taxpayers' rights. Uncertainty over tax obligations and unbalanced allocation of rights and responsibilities are not compatible with fair and effective tax systems. Despite its merits, we are not entirely convinced that the Proposal will be able to reach its said goals, at least at its current form. It might be more prudent to first evaluate the effects of legislation already adopted for the enhancement of transparency and then proceed therewith, if necessary.

8 The proposal explicitly limits the obligations to intermediaries incorporated / residents / registered / based in an EU Member State (art. 1 para. 1 point 21 of the Proposal).

9 According to Working Document accompanying the Proposal, the term is envisaged to include "consultants, lawyers, financial and investment advisers, accountants, financial institutions, insurance intermediaries, agents establishing companies or any other type of person involved in the design of structures potentially leading to tax avoidance". Cf. European Commission, Commission Staff Working Document Impact Assessment (SWD 2017(236)), June 2017.

10 OECD, Cooperative Compliance: A Framework, From Enhance Relationship to Cooperative Compliance, 2013.