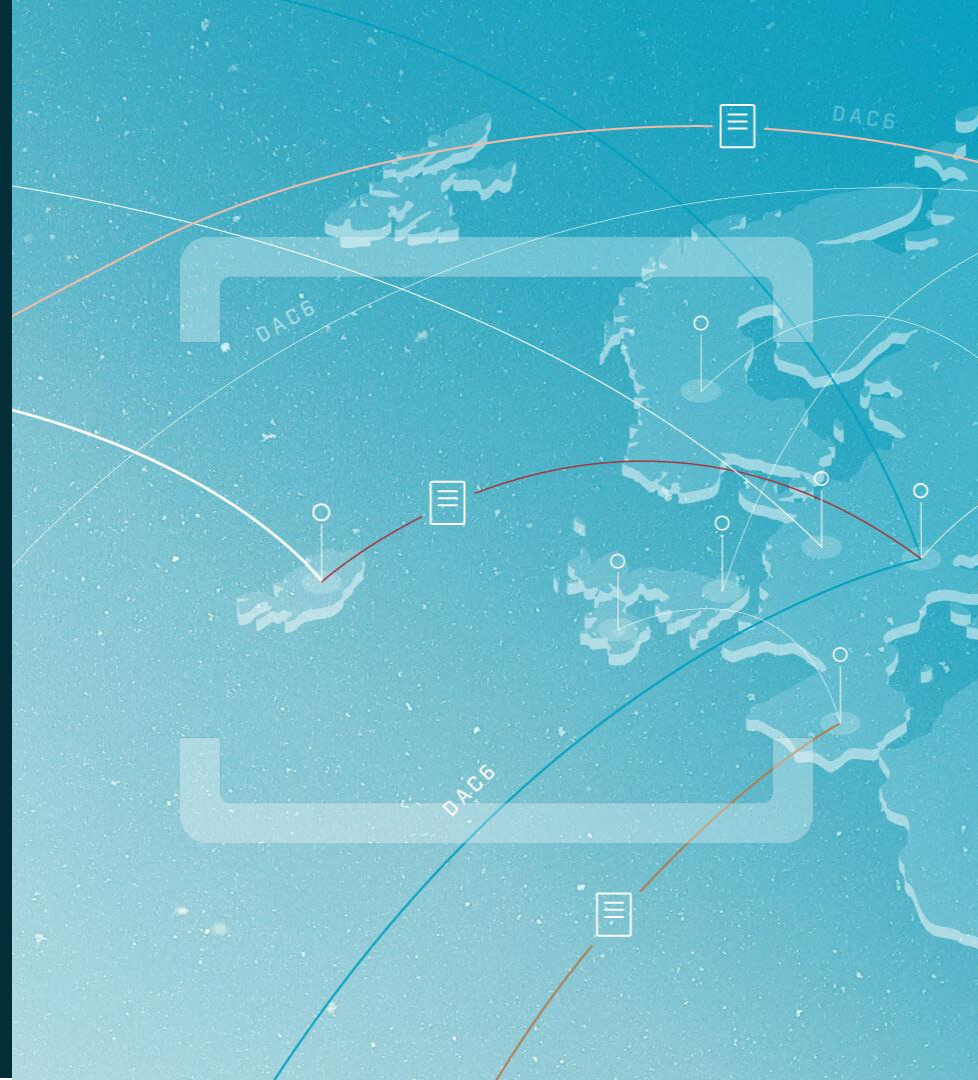




# The MBT and Other DAC6 Limiting Factors

How EU Member States are  
reducing the volume of  
DAC6 reports

26 November 2020



# Your speakers



## **Paul Millen**

Paul is a first mover and foremost thinker on the impact of the MDRs and DAC6 on the financial services industry, having spoken on the topic at prominent tax conferences in Switzerland and abroad and published detailed analyses in leading periodicals since 2018. As the founder of Millen Tax & Legal GmbH, he advises a range of clients, including banks, trust companies, fund managers and single family offices, on an array of US and cross-border tax and legal matters, most notably FATCA and CRS.



## **Anna Szkudlarek**

Anna is a client adviser focusing on regulatory disclosure requirements. By combining a chartered certified accounting qualification with a strong technical background, she can build relationships and prove comprehensive regulatory services such as MDR and DAC6, FATCA and CRS to family offices, service providers and internationally mobile Ultra High Networth Individuals (UHNWIs) in over 80 countries. Anna is a RegTech expert.

# Content of today's presentations

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Welcome remarks & introduction to your speakers

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**What do these limitations mean for your operations?**

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Consequences and key takeaways

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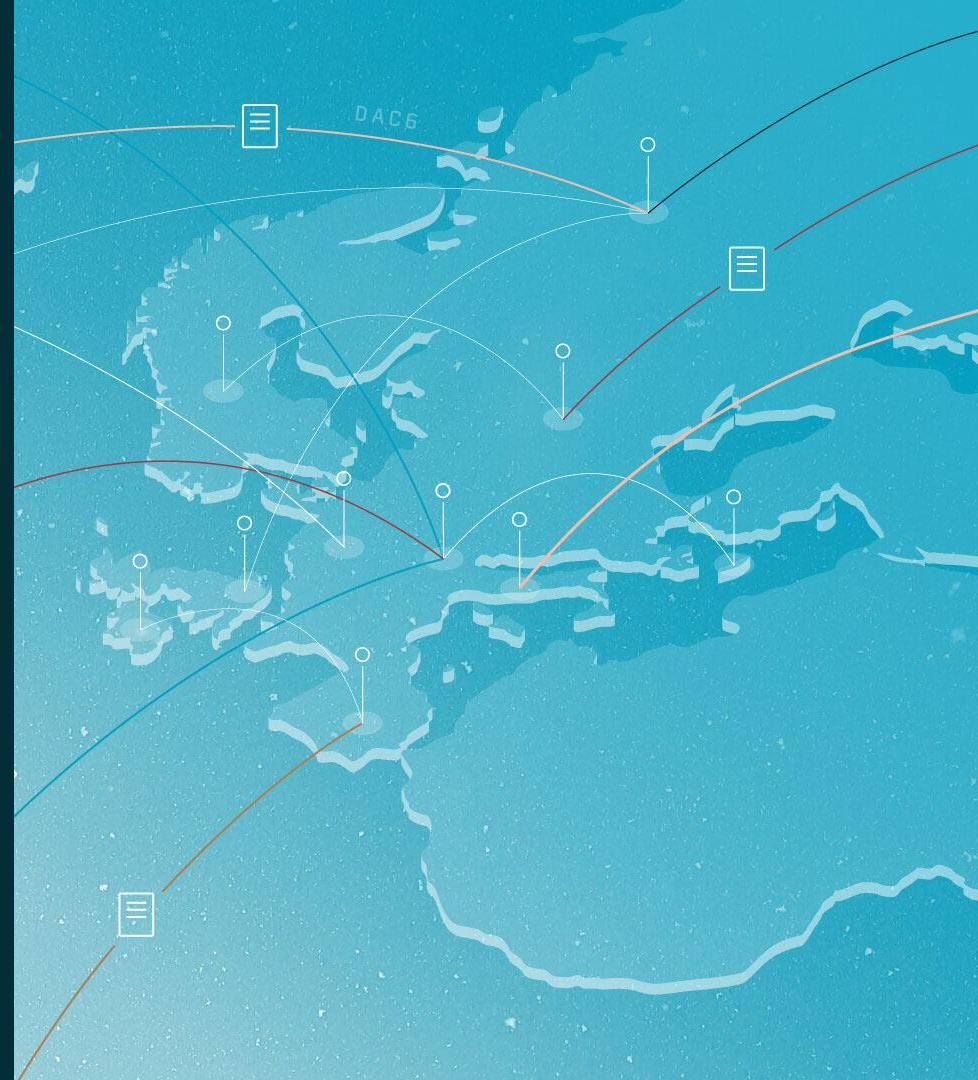
**Q&A**

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**Closing remarks & thank you**

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# What are the Main Benefit Test (MBT) and the DAC6 Hallmarks?



# DAC6 Refresher

- The Amendment to Directive 2011/16/EU on administrative cooperation in the field of taxation (known colloquially as “**DAC6**”) is the **EU’s version of the OECD’s Mandatory Disclosure Rules (“MDRs”)**, which **target CRS avoidance**, coupled with reporting on tax-planning activities regarded as “**aggressive**”
- As of 1 January 2021, a **cross-border “Arrangement” meeting one or more of the DAC6 Hallmarks**—the set of tax attributes deemed indicative of aggressive planning—**plus potentially a tax benefits test, qualifies as a Reportable Cross-Border Arrangement (RCBA)**

- For every RCBA, **EU-connected parties that qualify as “Intermediaries”** with respect to the Arrangement, **or the taxpayers affected by it** (if no EU Intermediary can do so), must report

## Each DAC6 reporting party must:

- Disclose specified information
  - About the transaction and
  - **The parties involved in it**
- To their local competent authority
- **Within 30 days\***
- For exchange on an automatic basis with other EU member states

# The DAC6 Hallmarks

Main Benefit Test		Cross-Border Transactions		AEOI/CRS and Beneficial Ownership	Transfer Pricing
A. Generic	B. Specific	C		D	E
1. Confidentiality clause included	1. Acquisition of a loss-making company	1. (b)(i) Deductible cross-border payments to Associated Enterprises subject (when received) to a zero or almost zero tax rate	1. (a) Tax-deductible payment to an Associated Enterprise with no tax residency	1. Schemes which may undermine CRS (i.e. the automatic exchange of information regime)	1. Use of unilateral safe harbour rules
2. Success fee reflects tax advantage	2. Conversion of income types which are taxed at lower level or tax exempt	1.(c) Deductible cross-border payments to Associated Enterprises subject (when received) to a full tax exemption	1.(b)(ii) Tax-deductible payment to an Associated Enterprise resident in an EU/OECD-blacklisted jurisdiction		2. Transfer of hard-to value intangibles
3. Standardized documentation/ set-up available to more than one taxpayer	3. Circular transactions without primarily commercial function	1. (d) Deductible cross-border payments to Associated Enterprises subject (when received) to a preferential tax regime	2. Depreciation on same asset in multiple jurisdictions	2. Schemes involving non-transparent legal or beneficial ownership chain	3. Restructuring resulting in significant profit shifts (50%) following the transfer of functions and/or risks and/or assets between Associated Enterprises
<b><i>The Main Benefit Test (MBT) must also be fulfilled</i></b>			3. Multiple relief from double taxation		
			4. Transfer of assets with a material difference in the price used for tax purposes		



# What is the Main Benefit Test under DAC6?

**The MBT operates as a second element for roughly half the DAC6 Hallmarks.**

**For these Hallmarks, a cross-border Arrangement must also satisfy the MBT in order to qualify as a Reportable Cross-Border Arrangement (RCBA)**

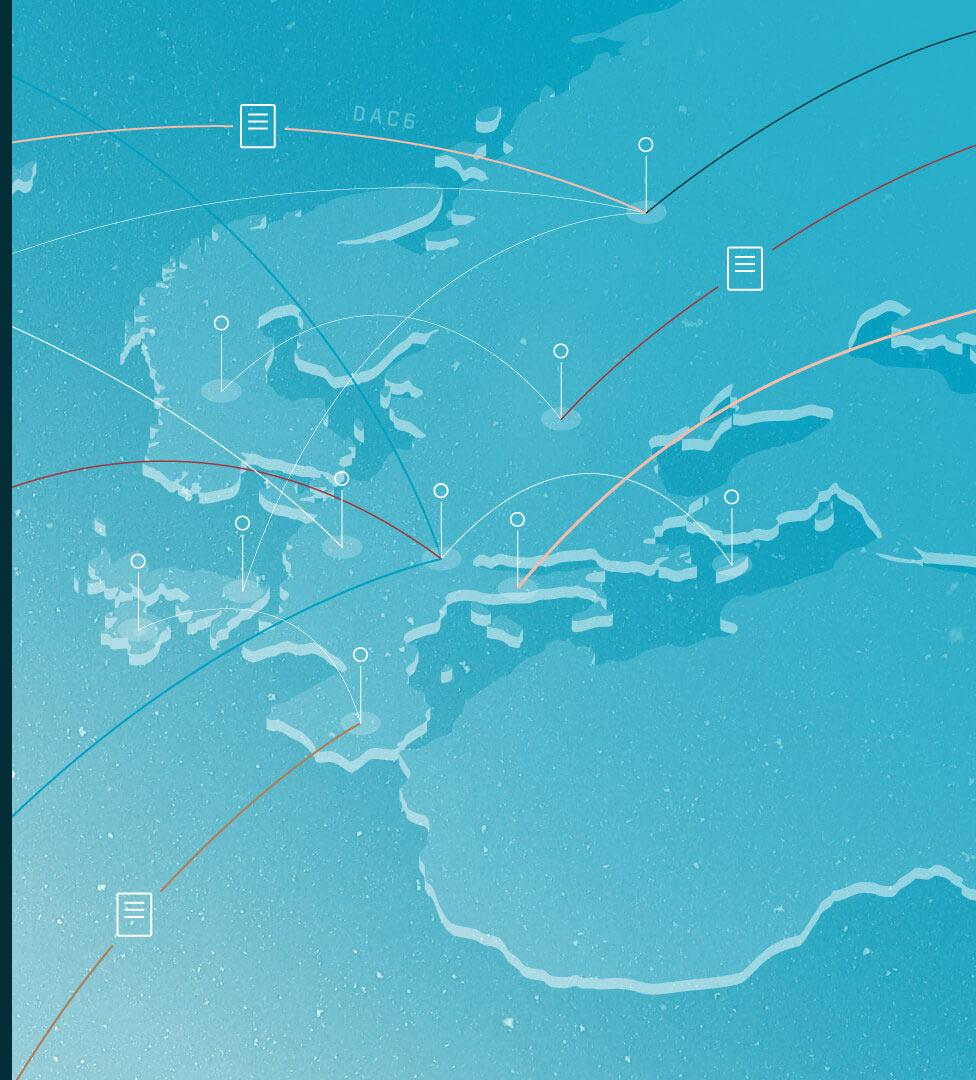
*However, the language in the protocol's text itself is too broad to serve as an effective limiting factor...*

## **DAC6 MBT Definition:**

“The [MBT] 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.**”

Critically, the benefit need not be the sole benefit or even the primary benefit, but **simply a benefit of the Arrangement**

# How are EU Member States limiting DAC6 reporting?





# What counts as a tax benefit?

In their DAC6 guidance, several local tax authorities **specify the types of tax advantages that might be obtained through a cross-border Arrangement:**

- Exemption from taxation
- Eligibility for a tax refund
- Reduction in tax rate or amount of taxable income
- Increase in amount of tax refund
- Deferral of a payment of tax, including withholding levies
- Acceleration of a tax repayment or refund

Some tax authorities also assert that **the MBT applies even where:**

- The tax advantage **concerns indirect taxes, like VAT**
- No tax advantage is **obtained in a DAC6 jurisdiction**
- The tax advantage is the result of a tax-driven arrangement in another jurisdiction that **simultaneously reduces the taxable income** of the EU taxpayer
- The tax advantage is the **stymieing of a tax disadvantage that would otherwise arise in the future** e.g. due to an amendment in the tax code

# Limit via the MBT: The UK & Netherlands Guidance

- In the final regulations released on 1 July, HMRC specifies that tax advantages obtained do not count towards the MBT if they can “**reasonably be regarded as consistent with the principles** on which the relevant provisions that are relevant to the cross-border arrangement are based and the policy objectives of those provisions“
- The Dutch method of enlarging the MBT distills the lawyerly concept into a practical, two-pronged inquiry. All else being equal, the MBT is met only if (i) the Arrangement would **not have been implemented were the anticipated tax benefit not obtainable** or (ii) the Arrangement features **supplemental elements added to obtain the tax advantage in question**

## UK guidance notes example

Tax relief for spending on R&D confers a benefit, but the objective of the legislation intends just such a benefit as an incentive to invest in R&D, and so the MBT is unmet

## Dutch closing thought experiment

If the tax benefit were revoked, would the implementation of the Arrangement have remained the same? If so, the MBT is unmet

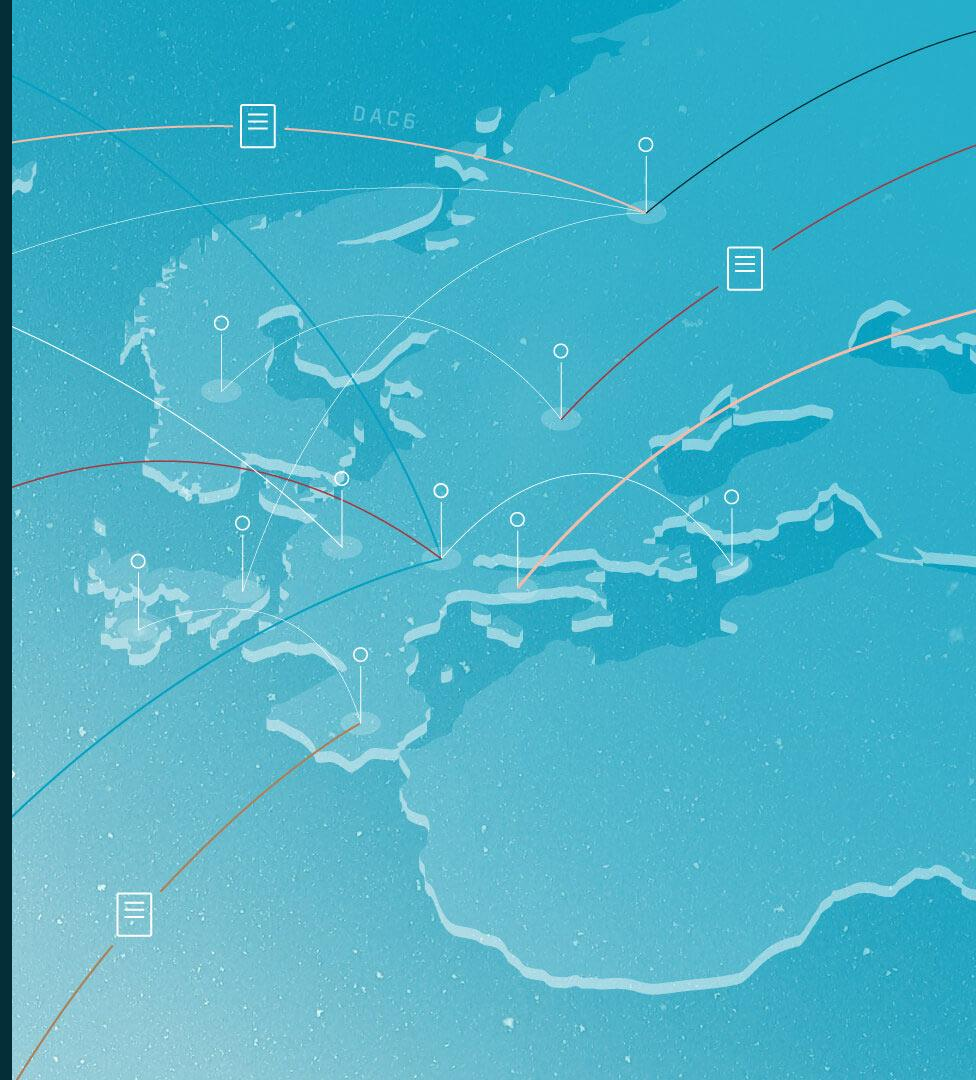
# Limit via the Hallmarks: German & Irish Guidance

- The German DAC6 administrative decree, released as a preliminary draft in March 2020, steps through each of the Hallmarks, refining its interpretation through references to common scenarios and setting out examples specific to the particular Hallmark that are or are not reportable, including appendices with whitelists of commonplace, non-reportable activities
- Helpfully, the guidance also quantifies certain qualitative terms like a “near 0%” tax rate for HMC1b(i) or “a material difference in the price” under HMC4
- The Irish guidance, released on 1 July 2020, deploys a similar approach, limiting the interpretation by providing significant details on the practical application of the specific Hallmark in Ireland, thereby reframing the Hallmark to fit Irish objectives
- Further, in order to staunch the expected flood of RCBAAs under HMA3 (substantially standardized documentation), Appendix II to the guidance provides a catalog of domestic laws which can shelter an Arrangement from reportability so long as it was implemented in accord with one of them

# Limit via the MBT and Hallmarks: Cyprus Guidance

- The Cyprus draft regulations contrast the value of the expected tax advantage to the value the other advantages obtained (e.g. profits) from the Arrangement and produces a mathematical approach of sorts
- In essence, this formula calculates the amount of tax due with the Arrangement in effect and the amount of tax that would have been owed in the absence of the Arrangement and compares the difference to the total value obtained from the Arrangement, presumably using a minimal percentage threshold to define what counts as a “main benefit”
- The Cyprus draft guidance further limits the RCBA for common activities by imitating aspects of the white-/blacklist approach
- While eschewing the whitelist appendices, it follows Ireland’s effort to define each Hallmark in a fashion that is appropriate for (and presumably advantageous to) Cypriot financial firms
- Furthermore, for certain domestic tax regimes, it asserts that they are not “preferential regimes” per HMC1d, so long as the EU Code of Conduct Group (Business Taxation) did not judge them to be a “harmful”

**What do these  
limitations mean for  
your operations?**





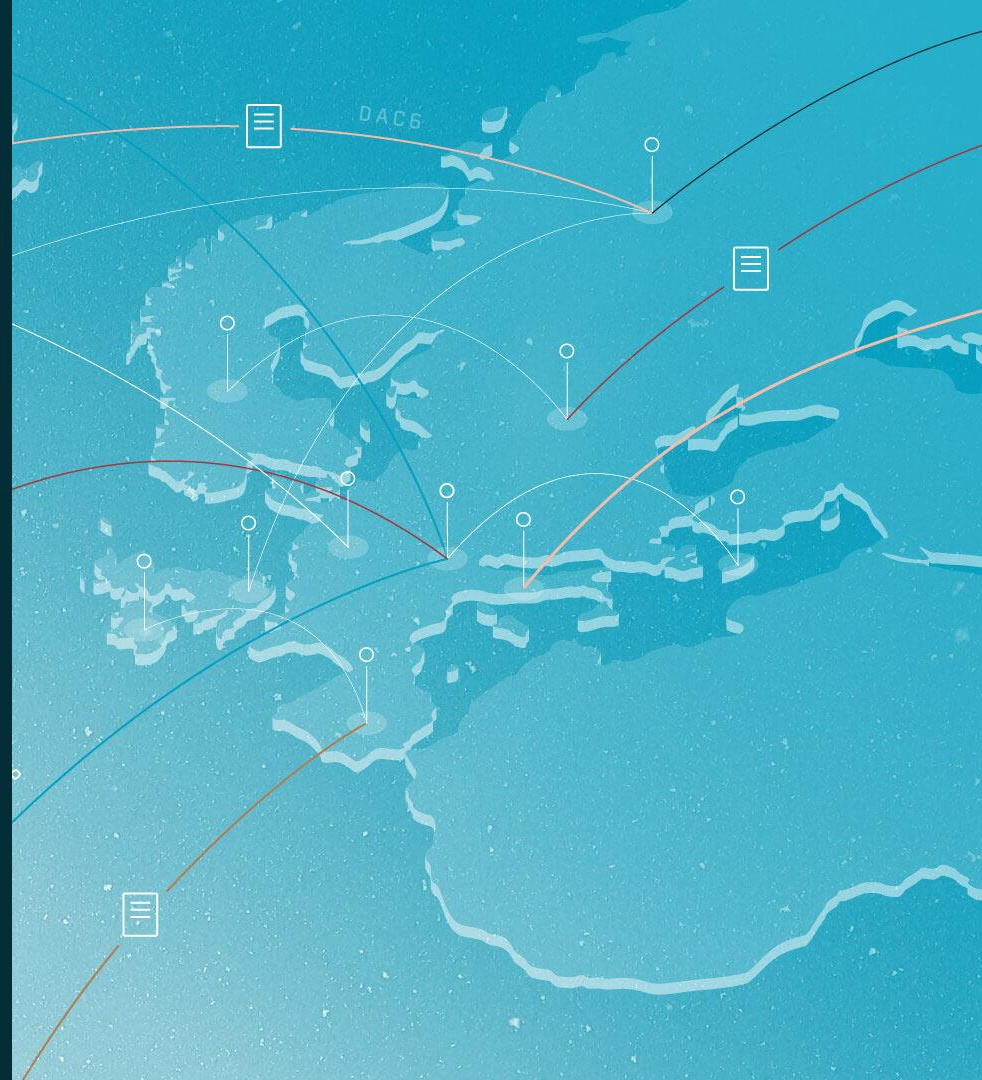
# Consequences and key takeaways

- Elusiveness of a common solution to the risk of excessive reporting volume hindering DAC6'S stated aim of identifying emerging tax-planning schemes in advance of their expansion
- Different approaches to limiting factors a reflection of the different priorities on Intermediary disclosure amongst DAC6 countries
- Further fragmentation of the unified EU DAC6 regimes into multiple local sub-regime, demonstrating potential for DAC6 “competition”
- Significant burden for Intermediaries with operations in multiple EU jurisdictions
- Forum shopping by or of Intermediaries in order to avoid DAC6 reporting, inevitably leading to anti-forum shopping measures
- Recipe for chaos?



## Q&A

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# Upcoming webinars

## DAC6 in Cyprus

*16 December 2020 at 2pm - 3pm CET*

- The Cyprus DAC6 law and accompanying guidance notes
- The treatment of industries in the Cypriot financial center
- The methods by which the Cypriot authorities will limit the scope of Reportable Cross-Border Arrangements
- Key differences in standards and interpretations between Cyprus and other EU member states

## The Specific Impacts of DAC6 on Fiduciaries

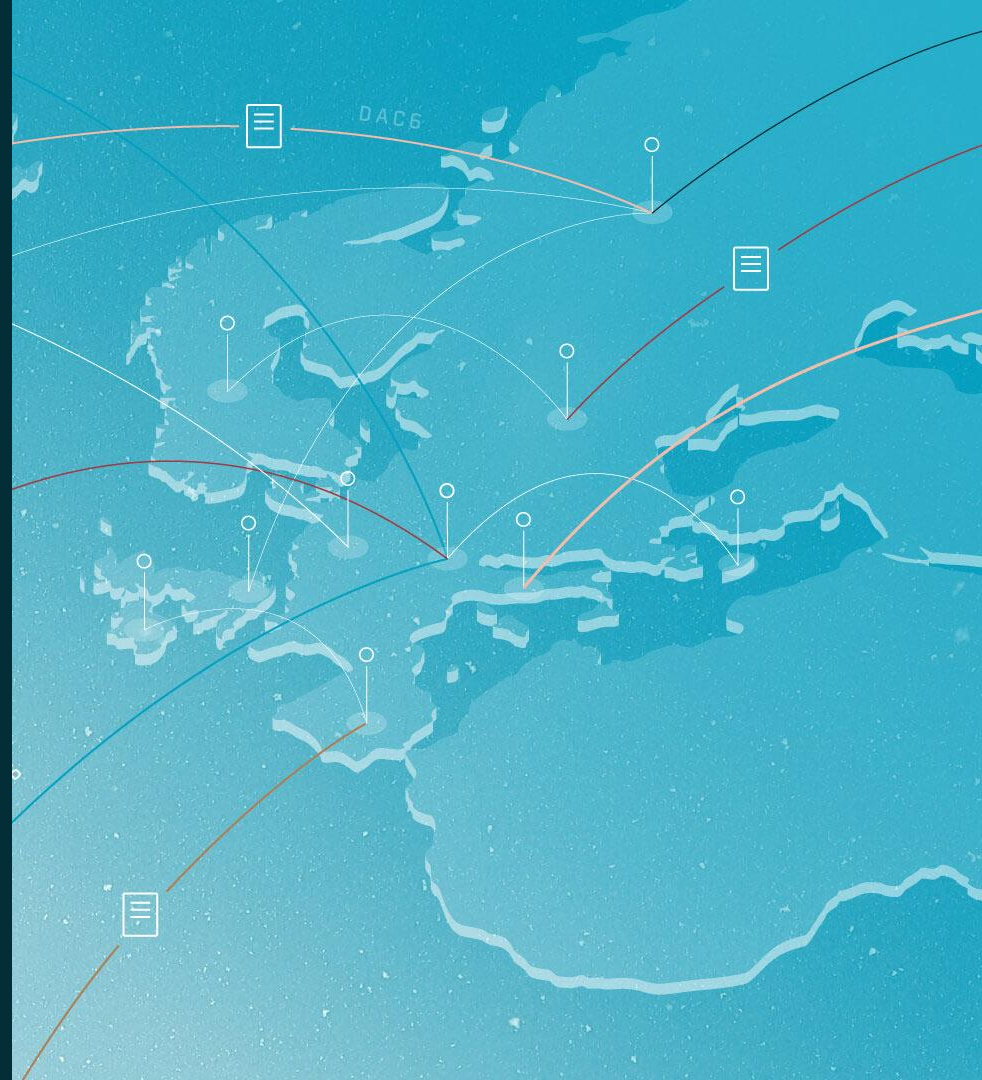
*21 January 2021 at 2pm - 3pm CET*

- The direct and indirect impacts of the DAC6 directive and local rules on the fiduciary industry
- The DAC6 Hallmarks most likely to ensnare fiduciaries and how
- Pitfalls for fiduciaries in the DAC6 landscape, such as the Main Benefit Test and Legal Professional Privilege exemption from reporting
- Advice for fiduciaries on how best to prepare themselves and their clients for DAC6 compliance demands



# Thank You & Stay Safe

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