UK Mandatory Disclosure Regime (DAC6)

Background

The EU Council Directive 2018/822 (DAC6) provides for the mandatory disclosure by intermediaries, or individual or corporate taxpayers, to HMRC of certain cross-border arrangements and structures that could be used to avoid or evade tax and the mandatory automatic exchange of this information among EU Member States. A cross-border arrangement is reportable if it meets one or more hallmarks.

From January 2013, the EU introduced the Directive of Administrative Co-operation (DAC) and, over time, DAC has evolved to include the automatic reporting of various matters, for example, directors' fees, employment income, insurance premiums, pension income and income and ownership from immovable property.

Member States were required to implement DAC6 into national law by 31 December 2019 and apply the provisions by 1 July 2020. On 8 May 2020, the EU agreed an extension to the deadlines for DAC6 reporting to take into account the upheaval caused by the COVID-19 Pandemic.

The EU extension has allowed some additional time, and so the revised deadlines are as follows:

- Advice given after 1 October 2020 → 30 days;
- Advice given after 25 June 2018 but before 1 October → 30 November 2020.

UK Implementation

The UK government laid the International Tax Enforcement (Disclosable Arrangements) Regulations, SI 2020/25, on 13 January 2020, with a number of changes from last year's draft version. The regulations effectively implement DAC6 into UK law.

Who is an Intermediary?

An intermediary is any person that designs, markets, organises or makes available for implementation or manages the implementation of a reportable cross-border arrangement. An intermediary can be an individual, a company or a trustee.

The definition of an intermediary envisages two types of intermediaries: 'promoters' and 'service providers'. Promoters are those who design and implement the arrangements, whilst service providers are those that provide assistance or advice in relation to the arrangements. The reporting obligation is fundamentally the same, but there is a 'knowledge' defence available to service providers which, if applicable, means that they do not have an obligation to report. There is no equivalent defence for promoters.

An intermediary must meet one of the following conditions:

- it is a resident for tax purposes in the UK;
- it has a permanent establishment (PE) in the UK, through which it provides the services in respect of the arrangement;
- it is incorporated in the UK, or governed by the laws of the UK; or
- it is registered with a professional association relating to legal, taxation; or consultancy services in the UK.

Where information relating to a reportable arrangement is covered by legal professional privilege (LPP), the lawyer is not required to report that information to HMRC. Where a lawyer chooses not to disclose information because of LPP, they must inform other intermediaries or Relevant Taxpayers of their own reporting obligations, as the reporting obligation passes to the other intermediary or Relevant Taxpayer.

What is a Cross-Border Arrangement?

An arrangement is considered 'cross-border' where there is an arrangement concerning either more than one EU Member State or a Member State and a third country where at least one of the following conditions are met:

- not all participants in the arrangement are tax resident in the same jurisdiction;
- one or more participants in the arrangement are simultaneously resident for tax purposes in more than one jurisdiction;
- PE linked to any of the participants is established in a different jurisdiction and the arrangement forms part of the business of the PE;
- at least one of the participants in the arrangement carries on business activities in another jurisdiction without being resident for tax purposes or creating a PE situation in that jurisdiction;
- such an arrangement has a possible impact on the automatic exchange of information or the identification of beneficial ownership.

What is a Reportable Arrangement?

An arrangement will be reportable if it meets at least one of a number of 'hallmarks'. For hallmark categories A, B and certain elements of Category C, an arrangement will only be reportable if it also meets a so-called 'main benefit' test (MBT). This test means that one of the main objectives of the arrangement is to obtain a tax advantage.

A brief summary of the five hallmark categories is set out below:

Categories	General Description	Subject to Main Benefit Test (MBT)?
Category A	Confidentiality – Arrangements where the participant or taxpayer enters into a confidentiality agreement to not	Yes

	disclose how the arrangement could disclose a tax advantage to other intermediaries or tax authorities.	
	Premium Fee arrangements – Arrangements where the intermediary fee is for example based on the tax saved.	Yes
	Standardised documentation – Arrangements involving standardised documentation without substantial customisation.	Yes
Category B	Loss buying – Arrangements involving buying a loss-making company to reduce the tax liability.	Yes
	Conversion of Income to Capital – Arrangements which have the effect of converting income into capital or another type of income that is taxable at lower rates.	Yes
	Circular transactions - Arrangements involving circular transactions with little or no commercial function.	Yes
Category C	Arrangements involving deductible cross border arrangements between associated enterprises where:	
	(a) the recipient has no tax residence, or	No
	(b)(i) the country of tax residence has a zero or close to zero corporation tax rate, or	Yes
	(b)(ii) the country is included in the OECD list as being a non-cooperative jurisdiction.	No
	(c) the payment is exempt in the jurisdiction of receipt.	Yes
	(d) the payment benefits from a preferential tax regime in the jurisdiction of receipt.	Yes
	Arrangements involving deductions in more than one jurisdiction.	No
	Arrangements involving the claiming of relief from double taxation on the same item in more than one jurisdiction.	No
	Arrangements involving the transfer of assets where there is a material difference in the amount treated as payable in consideration for the assets in the jurisdictions involved.	No
Category D	Arrangements which have the effect of undermining the rules, or the absence thereof, on beneficial ownership or any other equivalent agreement on automatic exchange of financial account information. Arrangements 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.	No
Category E	Arrangements concerning transfer pricing (TP), including the use of unilateral safe harbours, or the transfer of hard-to-value intangible assets (IP) when no reliable comparables exist and the projection of future cash flows or income are highly uncertain.	No

The Main Benefit Test

The MBT essentially looks at whether the main benefit or one of the main benefits is a tax advantage having regard to all relevant facts and circumstances.

Grandfathering of Historical Arrangements

Transactions which amount to cross border arrangements but which were already in place at 25 June 2018 do not require to be reported. However, if those transactions continue after 25 June 2018, and any adjustments are made to the original transactions, they will need to be reviewed to determine whether those subsequent arrangements are reportable in their own right.

Multiple Reporting

Where there is more than one intermediary, the obligation to report lies with all intermediaries involved in the arrangement. An intermediary shall be exempt from filing information to the extent that it has proof that this information has already been filed by another intermediary. Where there is more than one Relevant Taxpayer, the Directive puts the primary obligation onto the Relevant Taxpayer who agreed the arrangement and then on to the one who manages the implementation.

Penalties

The penalty for failure to comply with DAC6 is up to £5,000. However, in a number of cases where the £5,000 penalty is inappropriately low, then the penalty can be an initial amount of £600 per day.

Summary

The changes brought by DAC6 will have far-reaching consequences for tax advisors, service providers and taxpayers. Once the rules become fully applicable (i.e. on 1 July 2020), intermediaries and taxpayers will be required to file information with their national tax authority within thirty days of the day after the reportable cross-border arrangement is made available for implementation.

As a transitional measure, where the first step in a reportable cross-border arrangement is implemented between 25 June 2018 and 30 June 2020, the arrangement should be reported between 1 July 2020 and 31 August 2020.

How can Harbottle & Lewis help?

The Harbottle and Lewis tax team is made up of lawyers, chartered accountants, chartered tax advisers and ex-HMRC inspectors and can assist in reviewing structures to identify risk or ensure compliance.

Key contacts:

Gary Ashford
Tax Partner,
CTA (fellow), TEP, ATT
E: gary.ashford@harbottle.com

David Scott
Tax Partner,
E: david.scott@harbottle.com