Cross-border tax arrangements: be warned!

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We have already discussed Directive (EU) 2018/822 as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements. Although the various European Member States, including Belgium, have yet to transpose the directive into national legislation, the directive entered into force on 26 June 2018. The actual first notification will only have to take place from 2020 onwards.

Intermediaries and taxpayers who are obliged to report must be aware of this new and additional weapon in the fight against tax evasion. It complements the various national anti-abuse tax provisions already in place in the Member States.

What arrangements?

The Directive requires the reporting of potentially aggressive cross-border tax planning arrangements. A cross-border arrangement is one which involves either more than one Member State or one Member State and a third country.

In addition, at least one of the following conditions must be fulfilled:
a) not all of the participants in the arrangement are resident for tax purposes in the same jurisdiction;
b) one or more of the participants in the arrangement is simultaneously resident for tax purposes in more than one jurisdiction;
c) one or more of the participants in the arrangement carries on a trade or business in another jurisdiction through a permanent establishment and the arrangement constitutes part or all of the trade or business of that permanent establishment;
d) one or more of the participants in the arrangement carries on an activity in another jurisdiction without being resident for tax purposes or without creating a permanent establishment therein;
e) such a mechanism is liable to affect the automatic exchange of information or the determination of the ultimate interest.

These arrangements must be primarily, but not exclusively, for the purpose of obtaining a tax advantage (*main benefit test*).

Essential characteristics or hallmarks of the arrangement

In order to minimise costs and administrative burdens for both tax administrations and intermediaries, and to make the directive an effective deterrent, not all arrangements should be reported. This is only the case when the cross-border construction possesses one of the essential characteristics listed in Annex IV to the directive .

There are five categories of essential characteristics or *hallmarks:*
Category A - General essential characteristics associated with the *main benefit test*;
Category B – Specific essential characteristics associated with the *main benefit test*;
Category C – Specific essential characteristics relating to cross-border transactions;
Category D – Specific essential characteristics for automatic exchange of information and ultimate interest; and
Category E – Specific essential characteristics related to transfer pricing.

It is important to note that certain categories may only be taken into account if they comply with the *main benefit test*.

Notifications linked to the main benefit test

Category A covers arrangements with a confidentiality clause, a *success fee* for the intermediary or where a standard, market-ready structure or standardised documents are used.

Category B includes arrangements whereby the taxpayer uses tax losses, income is converted into capital, gifts or other categories that are taxed at a lower rate or not, or resources are pumped around (*round-tripping*) by means of intermediate entities without a primary commercial purpose.

In category C, three arrangements are linked to the *main benefit test*. More specifically, those where deductible cross-border payments are made between two or more related companies and (a) the recipient is - for tax purposes - resident in a jurisdiction that does not levy (or levies at a zero or near zero rate) corporate income tax; (b) the payment enjoys a full tax exemption in the jurisdiction where the recipient is resident for tax purposes or (c) the payment enjoys a favourable tax treatment in the jurisdiction where the recipient is resident for tax purposes.

Mandatory reporting obligation

If an arrangement contains one of the essential characteristics that occur in the other categories of C, D or E, then the arrangement must always be reported. This applies irrespective of whether the main objective is to gain a tax advantage.

Under category C, this is the case for arrangements where the same asset is depreciated in more than one jurisdiction; double taxation is claimed for the same income or capital item in

more than one jurisdiction; transfers of assets take place where there is a material difference between the amount designated in the jurisdictions concerned as the remuneration to be paid for those assets or where the recipient of the cross-border payments is resident for tax purposes in a jurisdiction included in a list of jurisdictions of third countries that have been assessed as non-cooperative by the Member States jointly or in the OECD.

Category D covers those arrangements which are designed to circumvent the automatic exchange of information or where legal or beneficial ownership is non-transparent through the use of persons, legal arrangements or structures.

Finally, category E focuses on transfer pricing arrangements based on unilateral safe-haven rules; transfers are made of intangible assets which are difficult to value or cross-border intra-group transfers where the estimated annual pre-tax earnings before interest and taxes (EBIT) of the transferor(s), in the three-year period following the transfer, are less than 50 % of the estimated annual EBIT of that/those transferor(s) if the transfer had not taken place.

Which intermediary should report?

Any intermediary who conceives, offers, designs, makes available for implementation or manages the implementation of a reportable, cross-border arrangement.

An intermediary is also a person who, bearing in mind the facts and circumstances involved and on the basis of the available information, expertise and understanding necessary to provide such services, has, directly or indirectly, provided any material assistance, other assistance or advice. Any person shall have the right to provide evidence that he or she did not know and could not reasonably have known that he or she was involved in a reportable cross-border arrangement.

In addition, an intermediary must meet at least one of the following additional conditions: be resident for tax purposes in a Member State; have a permanent establishment in a Member State through which the services relating to the arrangement are provided; be constituted in, or subject to, the laws of a Member State or be registered with a professional body in connection with the provision of legal, tax or advisory services in a Member State.

Does the taxpayer have a reporting duty?

Three situations are *de facto* foreseen which the taxable person has to report himself.

The taxable person shall be under an obligation to report if he has at no time engaged intermediaries to carry out the cross-border arrangement. The obligation to report also shifts to the taxpayer when the intermediaries are established outside the European Union. Finally, the taxpayer will also have to take responsibility for the notification if the intermediary in question invokes a legal professional confidentiality and the intermediary operates within the limits of this professional confidentiality.

What needs to be reported?

The following information must be reported:
a) the identification details of intermediaries and relevant taxable persons;
b) the essential characteristics that require the notification of the cross-border arrangement;
c) a summary of the contents of the cross-border arrangement subject to the notification requirement;
d) the date on which the first step towards implementing the reportable cross-border arrangement has been, or will be, taken;
e) the national provisions underlying the reportable cross-border arrangement;
f) the value of the reportable cross-border arrangement;
g) the Member State of the relevant taxpayer(s) and any other Member State likely to be affected by the reportable cross-border arrangement; and
h) the identification of other persons in a Member State who are likely to be affected by the reportable cross-border arrangement, together with an indication of the Member States to which they are linked.

When will the arrangement be reported?

Depending on what occurs first, the intermediary or taxpayer shall be obliged to report the cross-border arrangements of which they are aware, possess or control within 30 days of their becoming aware:
a) the day after the reportable cross-border arrangement has been made available for implementation; or
b) the day after the reportable cross-border arrangement is ready for implementation, or
c) the moment when the first step in the implementation of the reportable cross-border arrangement has been taken.

Intermediaries who have directly or indirectly provided material assistance, other assistance or advice are also obliged to provide information within 30 days of the day after they have directly or indirectly provided assistance, other assistance or advice.

In the case of a market-ready arrangement, the intermediary is obliged to draw up a three-monthly report with an overview of the new notifiers who have also opted for the implementation of this arrangement.

Conclusion

This directive once again increases the pressure on intermediaries involved in cross-border tax arrangements. That much is clear. It remains to be seen how and when Belgium will transpose the directive. In any case, the penalties for arrangements that are not reported will be effective, proportionate and dissuasive. In addition, any intermediary who chooses to ignore the directive and its national interpretation may suffer considerable reputational damage.

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