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Luxembourg Tax Alert

Luxembourg releases the draft law implementing the EU directive (DAC 6) requiring the disclosure of certain cross-border tax arrangements

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On 8 August 2019, the draft law that would implement the EU directive 2018/822, commonly referred to as DAC 6, was introduced to the Luxembourg parliament.

DAC 6, which broadly reflects the elements of action 12 of the OECD BEPS project on the mandatory disclosure of potentially aggressive tax planning, is the fifth amendment to the 2011/16/EU directive on administrative cooperation in the field of taxation.

DAC 6 introduces an obligation to disclose to the tax authorities information on cross-border arrangements that meet certain criteria. It also regulates the subsequent exchange of the information by and between tax administrations of EU member states on a regular basis.

As mentioned in the draft law, information received and exchanged under DAC 6 among tax authorities of EU member states would allow them to react more rapidly to potentially aggressive tax arrangements and to address potential loopholes through conducting appropriate risk assessments and tax audits, or involving legislative reforms aimed at closing such loopholes.

The draft law follows the text of DAC 6 by introducing the same definitions, hallmarks and retaining its scope of application covering cross-border arrangements as well as taxes covered by the amended 2011 directive on administrative cooperation in the field of taxation as transposed under Luxembourg law.

Some of the key elements of the draft law are summarized below concerning, among others, its scope of application, persons who would have to report, reporting deadlines, content of the reporting and potential penalty amounts to be imposed on intermediaries and taxpayers that do not comply with the transparency measures.

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Reporting under a hallmarks-based approach

The obligation to disclose information would concern cross-border arrangements that meet certain criteria, referred as hallmarks.

A cross-border arrangement would mean an arrangement that:

- Involves either more than one EU member state or an EU member state and a third country; and
- Meets one or more hallmarks, understood as elements that indicate potential tax avoidance or abuse.

The five categories of hallmarks have been transposed from DAC 6 directly without any modifications to their wording, although some interpretative comments have been added to the draft law.

The hallmarks, broadly drafted, would cover generic and specific criteria.

Generic hallmarks would target features aimed at promoting arrangements as well as capture arrangements that may be easily replicated and sold to a variety of taxpayers. The commentary to the draft law states that arrangements where documentation and/or structure are for the most part standardized refer to “prefabricated” tax products which could be used as presented or subject to limited modifications. In order to implement such an arrangement, a client would not need significant support of professional council services.

Specific hallmarks would be used to target vulnerabilities in the tax systems. They would cover different topics, including among others:

- Cross-border transactions (for example, deductible cross-border payment made to an associated enterprise located in a jurisdiction that does not impose corporate tax, deductions for the same depreciation on the asset which are claimed in more than one jurisdiction);
- Automatic exchange of information and beneficial ownership;
- Transfer pricing (for example, transfer of hard-to value intangibles).

A “main benefit test” would apply to the generic hallmarks as well as several of the specific hallmarks.

As per DAC 6, the main benefit test will be satisfied if it can be established that the main benefit or one of the main benefits, 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.

The commentary to the draft law quotes OECD BEPS Action 12 report, according to which the main benefit test compares the value of the expected tax advantage with any other benefits likely to be obtained from the transaction and has the advantage of requiring an objective assessment of the tax benefits.

The draft law also clarifies that the main benefit test would have to be met with respect to direct taxes. It would not apply where the tax advantage would be solely linked to value added tax, customs duties, compulsory social security contributions or other taxes, as well as taxes excluded from the scope of the amended 2011 directive on administrative

cooperation in the field of taxation. However, the tax advantage would not necessarily need to be obtained in an EU member state, but could also arise in a third country.

As the disclosure reporting would be aimed at identifying potentially aggressive tax schemes, it would not judge whether a scheme under disclosure would actually be abusive or aggressive. To become subject to reporting, it would be sufficient for a tax scheme to meet at least one of the hallmarks and as such, be identified as potentially aggressive.

Who would have to report?

The reporting obligation would fall on intermediaries but also, in some specific cases, on relevant taxpayers.

An intermediary would be defined as any person who designs, markets, organizes, makes available for implementation or manages the implementation of a reportable cross-border arrangement.

An intermediary would also mean any person that, having regard to the relevant facts and circumstances and based on available information and the relevant expertise and understanding required to provide such services, knows or could be reasonably expected to know that they have undertaken to provide, directly or by means of other persons, aid, assistance or advice with respect to the activities mentioned above.

Following the transposition under Luxembourg law of the amended 2011 directive on administrative cooperation in the field of taxation, a person is defined as (1) a natural person; (2) a legal person; (3) where the legislation in force so provides, an association of persons recognised as having the capacity to perform legal acts but lacking the status of a legal person; or (4) any other legal arrangement of whatever nature and form, regardless of whether it has legal personality, owning or managing assets, which, including income derived therefrom, are subject to any of the taxes covered by this law.

The commentary to the draft law explains that intermediaries would notably include accountants, tax and financial advisors, banks and consultants.

The commentary also indicates that DAC 6 does not in itself impose on the intermediaries and taxpayers any specific duty which would go beyond their existing professional obligations by requiring them to actively pursue information that such an intermediary or taxpayer would not hold in the first place.

For many intermediaries and some of the taxpayers, such current professional obligations cover Anti-Money Laundering requirements.

Lawyers would be granted a waiver from reporting information where doing so would breach their legal professional privilege. However, where such waiver would apply, they would still be required to report information of a general nature to the Luxembourg tax authorities. They would also have an information duty towards another intermediary involved in the transaction or, in the absence of such, towards the relevant taxpayer.

In principle, where there would be more than one intermediary involved in the same reportable cross-border arrangement, the obligation to file information regarding such an arrangement would lie with all the intermediaries simultaneously. The draft law would also foresee the sequence to be followed where there would be more than one taxpayer.

Where no intermediary located in the European Union is involved, the reporting obligation would fall on the relevant taxpayer.

Alongside those reporting obligations, two additional obligations would apply:

- Quarterly update by intermediaries of arrangements qualifying as marketable (meaning cross border arrangements that are designed, marketed, ready for implementation or made available for implementation without a need to be substantially customised).
- Annual reporting on the use of arrangements by relevant taxpayers to the Luxembourg tax authorities. Each relevant taxpayer would be obliged to file information on the use of a previously reported arrangement (either by an intermediary or by itself) via its annual income tax return. This obligation would apply for each of the years for which the taxpayer would use this arrangement.

Timing of the reporting and information to be reported

The mandatory reporting to the tax authorities would be required as from 1 July 2020. As a transitional rule, intermediaries and relevant taxpayers would also be required to disclose information on reportable cross-border arrangements, the first step of which was implemented between 25 June 2018 and 1 July 2020. This information would have to be filed by 31 August 2020.

The commentary to the draft law indicates that information would have to be provided to the tax authorities in sufficient time, which would mean, as far as possible, before such an arrangement is actually effectively put into place.

As from 1 July 2020, the intermediaries would need to communicate on cross-border arrangements within 30 days:

- Following the day on which the arrangement (i) is made available for implementation, or (ii) is ready for implementation; or
- When the first step in the implementation of the reportable cross-reportable arrangement has been made, whichever occurs first.

The reportable information would notably cover:

- Identification of intermediaries and relevant taxpayers, including among others their names, tax residence;
- Details of hallmark(s) that make the cross-border arrangement reportable;
- Summary of the arrangement, including the name by which it is known and an adequate description of the relevant business activities;
- Details of the national provisions of the concerned states that form the basis of the arrangement;
- Value of the reportable cross-border arrangement;

- Identification of the EU member state of the relevant taxpayer(s) and any other EU member state(s) likely to be concerned by the arrangement.

Penalties

The proposed penalty, in line with those already applicable in the context of exchange of information, would amount to up to EUR 250,000. A penalty would apply for failure to report, late reporting, incomplete or inaccurate reporting, as well as a breach of the information duty imposed on lawyers to timely notify other intermediaries or relevant taxpayers.

As indicated in the commentary to the draft law, the intentional nature of an infraction would be taken into account at the time of setting the amount of the penalty.

Comments and next steps

Even though the draft law provides some interpretative comments, more clarity on its key concepts, as well as some practical implementation guidelines, would be welcome. In any event, businesses should already begin to identify transactions potentially affected by DAC 6, as the first reporting should be filed in the summer of 2020.

The draft law now will be debated in the Luxembourg parliament, opined upon by the professional chambers and the Council of State, and possibly amended. A final vote is expected by the end of the year. We will keep you informed on future developments in connection with this draft legislation.

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