

DAC 6 Update: UK Narrows Scope of Mandatory Tax Reporting

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In a surprise u-turn, on 31 December 2020, the UK government took steps to narrow the scope of mandatory reporting under DAC 6. In the UK, only cross-border arrangements falling under the Category D hallmark (broadly, those that (a) have the effect of circumventing the OECD's Common Reporting Standard or (b) obscure beneficial ownership) will be reportable. The change will apply to both historic, and future, cross-border arrangements.

The amendment to the existing legislation is intended as a temporary step. In the coming year, the UK intends to introduce, and consult on, legislation to implement mandatory reporting under the OECD Mandatory Disclosure Rules (the "MDR").

These actions will significantly reduce the number of arrangements that need to be reported to HMRC. Nevertheless, reporting under DAC 6 is already required in some EU member states (such as Germany), and will be required elsewhere in Europe in the coming months. Accordingly, it needs to be considered whether arrangements that would previously have been reportable to HMRC under DAC 6 now need to be reported to other tax authorities.

EU Council Directive 2011/16 (as amended) (known as DAC 6) requires UK intermediaries (or failing which, taxpayers) to report, and HMRC to exchange, information regarding cross-border arrangements which meet one or more specified characteristics (hallmarks) and which concern at least one EU country. Regulations implementing DAC 6 reporting obligations into UK law (the "Regulations") came into force on 1 July 2020.

At the end of the Brexit transition period at 11pm on 31 December 2020, obligations requiring the UK to implement DAC 6 fell away. During the course of last year, the UK government had indicated that DAC 6's UK implementation would be unaffected by, and that the Regulations would remain in force following, the end of the Brexit transition period. However, under the Free Trade Agreement agreed between the UK and the EU on 24 December 2020, the UK is only required to ensure any legislation it implements at the end of the transition period relating to the exchange of information concerning potential cross-border tax planning arrangements offers the level of protection provided for by the "*standards and rules which have been agreed in the OECD...*".

Accordingly, on 31 December 2020, the UK government published legislation (taking effect at the end of the transition period) to narrow the scope of the Regulations in line with the MDR. As a result, only cross-border arrangements (i.e. those concerning the UK or an EU member state) that fall within Category D of Part II of DAC 6 will fall within the scope of UK reporting obligations.^[1] Broadly, an arrangement will be reportable under Category D if the arrangement either: (i) has the effect of undermining reporting obligations under agreements for the automatic exchange of information (e.g. the EU Common Reporting System, or the OECD's Common Reporting Standards); or (ii) involves non-transparent legal or beneficial ownership chains that:

- do not carry on a substantive economic activity;

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- 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; and
- have unidentifiable beneficial owners.

Historic arrangements

For reportable transactions after 30 June 2020, the first UK DAC 6 reporting deadline is 30 January 2021, and for transactions on or before 30 June 2020 where the first step in implementation was taken on or after 25 June 2018, it is 28 February 2021.

The effect of the amending Regulations (which has been confirmed by HMRC) is that the narrower reporting obligation will not only apply to future arrangements, but will also apply to historic arrangements for the period prior to 31 December 2020. Accordingly, only those arrangements which fall within a hallmark under Category D would need to be reported to HMRC.

Practical impact

The amendments to the Regulations have reduced the scope of disclosures to HMRC under DAC 6. Nevertheless, a full DAC 6 assessment and hallmark analysis will still be required in respect of EU jurisdictions involved in a transaction, in order to determine whether a DAC 6 filing obligation arises in those member states. Cross-border transactions that would otherwise have been reportable to HMRC may need to be reported to EU tax authorities. It is expected that the exception would be cross-border transactions that were reportable under hallmarks A, B, C and E of DAC 6 solely as a result of a UK nexus. However, it remains to be seen whether EU member states will update their domestic legislation implementing DAC 6 to require reporting of arrangements that concern only the UK and a non-EU jurisdiction. Such amendments would likely raise a number of practical issues, including, for example, questions as to who should bear the reporting obligation where intermediaries in the relevant EU jurisdiction have limited knowledge of the wider arrangements.

From a practical perspective, the UK's divergence from the DAC 6 standard may create additional administrative burdens for those intermediaries and taxpayers with pan-European operations that had planned to coordinate and submit DAC 6 reports in the UK. As the UK's actions were not trailed, these businesses may, at short notice, need to shift the coordination and submission of reports to an EU member state involved in the reportable arrangement. For those businesses that had already begun preparing data for submission using HMRC's XML schema, additional administrative work may be needed to ensure this data can be submitted to other relevant EU member states' databases. It remains to be seen whether (to lessen such burdens) HMRC may be willing to accept submissions on a voluntary basis or whether (if HMRC was so willing) this would be permissible under the laws of relevant EU member states.

Going forward

OECD Mandatory Disclosure Rules

We understand that the UK government will consult on draft legislation to implement the MDR in due course. The MDR were first published in March 2018, and form part of the OECD's recommendations set out in the "*Model Mandatory Disclosure Rules for CRS Avoidance Arrangements and Opaque Offshore Structures*".^[2] They are designed for jurisdictions wanting to implement disclosure obligations on certain intermediaries involved in arrangements intended to circumvent disclosure obligations under the OECD's Common Reporting Standard.^[3]

It is unclear whether such legislation would, in the immediate term, substantively alter the

scope of mandatory reporting obligations provided for under the Regulations (as amended). Looking forward, however, enhanced reporting is fast becoming a popular measure, internationally, for tackling tax avoidance, evasion and non-compliance. Countries outside the EU have introduced disclosure requirements that go beyond the MDR (with Mexico being the latest country to implement a disclosure regime modelled on DAC 6). Given this trend, it is expected that the OECD will further expand the scope of the MDR in the future. Accordingly, despite the reduced scope of the UK's current reporting regime, wider mandatory disclosure obligations may well become standard practice for taxpayers party to, and intermediaries advising on, cross-border arrangements.

Exchange of tax information

Before the end of the transition period, the UK was required to exchange tax information (including information relating to tax rulings and advance transfer pricing agreements, EU Common Reporting Standards, country-by-country reporting and beneficial ownership) with EU member states under the various provisions of Directive 2011/16/EU (the "DAC"). However, it is not yet clear: (i) how reports relating to Category D cross-border arrangements will be shared between HMRC and other tax authorities under the current DAC 6 exchange framework; (ii) whether HMRC will have access to information relating to cross-border arrangements falling within hallmarks A, B, C or E; and (iii) whether HMRC will retain access to other information currently shared under the DAC, given that the UK is no longer part of the EU. The FTA, for example, is silent on such matters.^[4]

Outside of the DAC, there are existing international frameworks that allow for the exchange of tax information between tax authorities. In particular, (a) the OECD provides a platform for the spontaneous exchange of tax rulings and advance transfer pricing agreements and (b) most double tax treaties between the UK and EU member states allow for the exchange of information between the treaty parties on request, in each case where the information is foreseeably relevant to the recipient tax authority. Furthermore, the OECD provides an information sharing platform for jurisdictions that have entered into bilateral agreements to exchange information, should the UK seek to enter into such agreements with EU member states. For the moment, however, it remains to be seen whether existing frameworks will provide sufficient information sharing rights for HMRC.

[1] The Category D hallmarks are contained in Annex IV Part II of the EU Council Directive 2018/822 of 25 May 2018 amending Directive 2011/16/EU at: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:32018L0822>

[2] OECD (2018), Model Mandatory Disclosure Rules for CRS Avoidance Arrangements and Opaque Offshore Structures, OECD, Paris. <https://www.oecd.org/tax/exchange-of-tax-information/model-mandatory-disclosure-rules-for-crs-avoidance-arrangements-and-opaque-offshore-structures.htm>

[3] The CRS was introduced in 2014 as a global reporting standard for the cross-border exchange of financial information.

[4] [https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:22020A1231\(01\)&from=EN](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:22020A1231(01)&from=EN)

Gibson Dunn's lawyers are available to assist with any questions you may have regarding these developments. For further information, please contact the Gibson Dunn lawyer with whom you usually work, any member of the Tax Practice Group or the authors:

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