Tax Alert

DAC 6

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What is DAC6?

Background

The Council of the European Union (EU) Directive 2018/822 of 25 May 2018 amended Directive 2011/16/EU regarding the mandatory automatic exchange of information in the field of taxation (the Directive or DAC6). DAC6 entered into force on 25 June 2018.

The Directive reflects the objectives of Action 12 of the BEPS Action Plan and is designed to enhance transparency to prevent aggressive cross-border tax planning.

The Directive and the Law require intermediaries (including EU-based tax consultants, banks, asset managers, corporate administrative service providers, insurance companies and lawyers) and taxpayers to report certain cross-border arrangements (reportable arrangements) to the relevant EU Member State tax authority.

Who is required to report?

- **Intermediaries** who designs, markets, organizes, makes available for implementation or manages the implementation of potentially aggressive tax-planning arrangements i.e. EU-based tax consultants, banks, asset managers, corporate administrative service providers, insurance companies and lawyers;

  and/or

- **Taxpayers**

Scope of taxes covered

All taxes except value-added tax, customs duties, excise duties and compulsory social security contributions.

Reportable arrangements

An arrangement is reportable if:

- it is cross-border; and
- meets at least one of the hallmarks A-E specified in Annex IV of the Law and contained in Appendix I of this tax alert; and
- the main benefit test ("MBT"), where applicable.

What is an "arrangement"?

It includes all types of arrangements, transactions, payments, schemes and structures, whether legally enforceable, and

includes oral agreements. It may also include arrangements comprising more than one step or part.

The meaning of an "arrangement" is broader than that of an "agreement" and it does not depend on the existence of an agreement between the participants of the arrangement.

In the case of a pre-existing arrangement (i.e., first step of implementation had initially been taken before 25 June 2018) which is extended or renewed, this may be considered as a "new arrangement" captured under the timeframes of the Law, in case there is a material change to the arrangement.

However, decisions relating to tax compliance positions shall not automatically render a past/historic arrangement a "new arrangement."

The term "participant" which is crucial in establishing the existence of the "cross-border" element, is a person who actively participates in the arrangement and is substantially related to the arrangement.

In regards to "marketable arrangements", any kind of tax planning scheme that is marketed or promoted should not necessarily be regarded as a marketable arrangement.

Hallmarks A-E of the Law

The hallmarks can be distinguished as hallmarks which are subject to the MBT, and those which themselves trigger a reporting obligation without being subject to the MBT. Please see Appendix I at the end of this tax alert for more detail.

Main benefit test ("MBT")

A tax advantage relates to taxes imposed by EU Member States and thus should have an EU nexus.

A tax advantage may also arise where an arrangement prevents a tax disadvantage which occurs due to an amendment in the tax law.

The MBT is an objective test, implying that there is no need to examine the specific motives or intentions of a person when he/she enters into an arrangement. In determining whether an arrangement results in a tax advantage, a comparison is required between the amount of tax due, having regard to the arrangement, with the amount of tax that would be due under the same circumstances in the absence of the arrangement.

Intermediaries

Intermediaries and relevant taxpayers are exempted from reporting, if sufficient proof of reporting of the same information is provided by the other intermediary/relevant taxpayer.

Also, intermediaries covered under legal professional privilege (LPP) are exempted from reporting. LPP applies only in cases

of lawyers exercising the profession of lawyer and Law Firms, as defined in the Advocates Law, Cap 2. However, the privilege is that of the client and not of the legal professional. Therefore, the client may elect to waive their right to LPP to the extent necessary to allow the legal professional to disclose the information to the tax department. Moreover, legal professionals covered under LPP should notify the rest of the intermediaries/relevant taxpayer of their reporting obligations as per the Law within 10 calendar days from the day on which the reporting obligation would have arisen if the intermediary was not covered by LPP.

Primary intermediaries

"Primary intermediaries" are intermediaries that actively design and advise on tax planning schemes, such as professional tax advisors or other persons specializing in tax law and that they are expected to have a full understanding and knowledge of the details with respect to the cross-border arrangement.

Secondary intermediaries

"Secondary intermediaries" are intermediaries that provide any aid, assistance or advice which may include the provision of tax, legal or other advisory services with respect to planning or structuring transactions, expertise or knowledge, financing, fiduciary and trust services, accounting advisory services and generally any other professional services in the context of implementing a reportable cross-border arrangement. However, the provision of compliance services in relation to historic data, that is not part of the implementation of a reportable cross-border arrangement, e.g., assistance with the completion of a tax return for a client who has previously entered into a reportable cross-border arrangement, would not result to the person providing the services being an intermediary.

"Secondary intermediaries" are not expected to perform additional due diligence to establish whether the service to be provided triggers a reporting obligation. A "secondary intermediary" should perform the normal due diligence for the type of transaction and the client in question. However, if a "secondary intermediary" purposefully failed to perform its normal due diligence or found other ways to be wilfully ignorant by purposefully not asking particular questions, then the test may still be satisfied and they would be considered an intermediary.

Reporting deadlines

The deadline for DAC6 submissions to the Cypriot Tax Department (CTD) is 30 November 2021 for both the transitional period (25 June 2018 – 30 June 2020) and the application period between 1 July 2020 and up to 30 October 2021.

This means that the "live" reporting period (i.e., the application of the 30-day deadline based on specific triggering events) in Cyprus commenced on 31 October 2021.

For the below reportable arrangements, the DAC6 submissions should be submitted by 30 November 2021:

- Reportable cross-border arrangements that were made (i.e., the first step of implementation took place) between 25 June 2018 and 30 June 2020 (i.e., within the transitional period of the Directive) and that was supposed to be submitted by 28 February 2021.

- Reportable cross-border arrangements that were made (i.e., that were made available for implementation or were ready for implementation or the first step in the implementation has been made or for which aid, assistance or advice has been provided by a secondary intermediary) between 1 July 2020 and 31 December 2020 (i.e., within the six-month deferral period of the Directive) and that was supposed to be submitted by 31 January 2021.

- Reportable cross-border arrangements that were made or to be made between 1 January 2021 and 31 October 2021 (i.e., within the normal application period of the Directive) that had to be submitted within 30 days beginning on the day after they were/will be made available for implementation or were/will be ready for implementation or when the first step in the implementation has been/will be made, whichever occurred/will occur first.

- Reportable cross-border arrangements for which secondary intermediaries provided/will provide aid, assistance or advice, between 1 January 2021 and 31 October 2021 (i.e., within the normal application period of the Directive), and had to submit information within 30 days beginning on the day after they provided/will provide aid, assistance or advice.

- The first periodic report for marketable arrangements that was supposed to be submitted by 30 April 2021.

How is information submitted?

- Submission of information for DAC6/MDR purposes is done in the Cypriot Government's Gateway Portal "Ariadni";
- An identification number (the unique reference number for the arrangement), i.e., "Arrangement ID" and a disclosure number, i.e., "Disclosure ID" will be provided which proves that the relevant DAC6 submission to the CTD has been successfully completed.

Proof of DAC6 submission must be provided by a Cypriot intermediary/relevant taxpayer in order to be exempted from the obligation to submit information to the CTD. This must consist of:

a) a copy of the information (i.e., of the DAC6 XML report) submitted to the CTD or to the competent authority of another EU Member State; and
b) a written confirmation of the unique reference number ("Arrangement ID") assigned to the arrangement by the CTD or the competent authority of another EU Member State.

Penalties

Penalties for non-compliance may range from €1,000 up to a maximum of €20,000.

Going-forwards

Determining if there is a reportable cross-border arrangement raises complex technical and procedural issues for taxpayers and intermediaries. Due to the scale and significance of the regime, taxpayers and intermediaries who have operations in Cyprus should review their policies and strategies for monitoring and reporting arrangements so that they are fully prepared for meeting their obligations and relevant deadlines.

Appendix I

Hallmark A *(subject to MBT)*

Hallmark A1 - Confidentiality clauses	Any confidentiality clauses/agreements which are intended to protect commercial or personal data are not captured by this hallmark.
Hallmark A2 – Remuneration in relation to a tax advantage	The key feature of this hallmark is that the intermediary's fee (or other form of compensation) for providing a service in relation to a cross-border arrangement is linked to a tax advantage being obtained. For example, a contingent fee, penalties and surcharges, a percentage of the tax advantage or a success fee.
Hallmark A3 - Standardized documentation and/or structure	This hallmark is intended to capture what is often referred to as "mass-marketed" or "off-the-shelf" arrangements that are primarily tax driven and whereby the finished product requires little or no modification to suit the specific requirements or circumstances of the relevant taxpayer.

Hallmark B *(subject to MBT)*

Hallmark B1 – Acquisition of loss-making entities	It is stated that for the purpose of this hallmark, steps will be contrived where they are pre-planned, artificial and/or complex for no evident commercial reason. The loss-making company being acquired is not considered as a participant. Intragroup acquisitions are also included within the scope of this hallmark.
Hallmark B2 – Conversion of income into capital, gifts or lower-taxed/tax-exempt income	In order to fully assess the applicability of this hallmark, it would be necessary to consider whether there is a conversion of an existing or prospective income stream into capital, gifts or other categories of revenue which are taxed at a lower or other non-taxable/exempt form. Therefore, a comparison test should be made for the tax that would have been payable had the conversion of income not taken place with the amount of tax that is payable (if any). In case employees are granted with share options as part of their remuneration package, any increase in value could be taxed as a capital gain, depending on the jurisdiction of residence. Despite the fact that the remuneration package could have consisted entirely of salary income, share options are a legitimate commercial choice to remunerate employees. In such case, there is no conversion of income into capital, but simply a choice between different options, which are widely used and have an underlying commercial rationale. This applies where the share options do not constitute more than 25% of the total remuneration package. Where arrangements are designed in advance, or do not constitute normal commercial practice, or involve additional artificial steps, which result in making the payments non-taxable or taxable at much lower rates, it is more likely for hallmark B2 to be triggered.
Hallmark B3 – Circular transactions	For this hallmark to be met, there must be a circular transaction resulting in the round tripping of funds (cash or cash equivalents), involving either: • Interposed entities without primary commercial function; or • Transactions that offset or cancel each other (or have similar features). An arrangement is considered to result in "round-tripping of funds" if the jurisdiction from where the funds originate is the same as the ultimate destination jurisdiction. In order to identify whether there is a "primary commercial function" it will be necessary to consider whether the round-tripping of funds serves little or no commercial purpose and has been done primarily to obtain a beneficial tax treatment that would not otherwise be available.

Hallmark C *(some are subject to MBT)*

Hallmark C1 – Deductible cross-border payments between associated enterprises	This hallmark only refers to actual payments and not to "deemed"/"notional" payments or transfer pricing adjustments. Where the payment is made to an entity which is tax transparent in its jurisdiction of incorporation or establishment, such as a partnership, it is considered that the recipient of the payment is the partner/investor. The term "deductible payments" in this hallmark does not extend to acquisitions of depreciable assets or interest that is capitalized into the cost of an asset (e.g., interest used to finance the construction of a building and capitalized into the cost of the building).
Hallmark C1(a) – Recipient not resident for tax purposes in any jurisdiction	This hallmark covers legal persons that have no tax residence in any jurisdiction. It should not cover jurisdictions that do not have the concept of tax residence in their tax regimes, either because a territorial system of taxation is applied, or because they do not charge corporation tax.
Hallmark C1(b)(i) - Recipient tax resident in a jurisdiction that does not impose corporate tax or that imposes corporate tax at a rate of zero or almost zero	For the purpose of this hallmark, "zero or almost zero corporate tax" refers to a nominal rate/headline corporate tax rate below 1% that applies generally in the state of residence of the recipient and not to the effective tax rate applicable to the recipient. Furthermore, where the recipient of payment benefits from an exemption from tax, such as sovereign wealth funds, government entities, etc., the hallmark C1(b)(i) will not apply.
Hallmark C1(b)(ii) - Recipient tax resident in a jurisdiction included in a list of third country jurisdictions which have been assessed by Member States collectively or within the framework of the OECD as being non-cooperative	With respect to the Organisation for Economic Co-operation and Development's (OECD) list, the jurisdictions covered by this hallmark are those which are assessed as "non-compliant." Further guidance is provided with regard to which version of the EU's list of non-cooperative jurisdictions for tax purposes and the OECD's list of non-compliant jurisdictions for the purpose of exchange of information upon request should be relied upon, given that those lists are periodically updated. Accordingly, for the transitional period, the version of the EU's and OECD's lists that should be relied upon is the one in force at the date of the first step of implementation of the arrangement, while for the application period, consideration should be made at the time that the reporting trigger is met (whichever occurs first).

Hallmark C1(c) - Recipient tax resident in a jurisdiction where the payment benefits from full exemption from tax	This hallmark is based on the tax treatment of the payment and not of the recipient. The hallmark applies in those cases where specific payments are made to persons that are subject to tax, but the payments are exempt from tax in the jurisdiction of the recipient.
Hallmark C1(d) - Recipient tax resident in a jurisdiction where the payment benefits from a preferential tax regime	This hallmark is based on the tax treatment of the payment and not of the recipient. A "preferential" regime for the purpose of this hallmark is defined as the regime which has been assessed by the EU Code of Conduct Group (Business Taxation) or the EU State aid rules as a "harmful" preferential regime. Also, the notional interest deduction rules or similar rules on notional interest deduction on equity in other jurisdictions, the intellectual property and tonnage tax regimes, which have been assessed by the EU Code of Conduct Group (Business Taxation) as “non-harmful” preferential tax regimes, are not considered as “preferential” regimes and thus should not fall within the scope of this hallmark.
Hallmark C2 – Depreciation deducted multiple times on the same asset *(not subject to MBT)*	Situations whereby the same depreciation claimed in two jurisdictions is coupled with dual inclusion of income are not within the scope of this hallmark.
Hallmark C3 – Relief from double taxation in respect of the same item of income or capital is claimed in more than one jurisdiction *(not subject to MBT)*	A list of examples is provided in the Guidelines where the same taxation is relieved in two jurisdictions coupled with dual inclusion of income to highlight that such situations fall outside the scope of this hallmark. The application of the dividend income exemption in Cyprus should not be considered as a claim for double tax relief for the purpose of this hallmark and as such this hallmark shall not apply.
Hallmark C4 – Transfer of assets with a material difference in the amount treated as payable *(not subject to MBT)*	The transfer of tax residence does not fall within the scope of this hallmark. The amount that is treated as payable refers to the tax value of an asset. Whenever an asset has no tax value for the transferor and/or transferee, then this hallmark does not apply as there is no “difference.” The accounting value is relevant only if it affects the tax value. Transactions between a head office and its permanent establishment(s) are within the scope of this hallmark but only if an asset has a tax value for both the transferor and the transferee. The hallmark can also be triggered when assets are transferred between unrelated third parties.

Hallmark D

Hallmark D1 – EU legislation or any equivalent agreements on the automatic exchange of financial account information circumvented *(not subject to MBT)*	Hallmark D1 will be triggered where it is reasonable to conclude that an arrangement has, or is designed to have, the effect of undermining the reporting obligation under the national laws implementing Council Directive 2014/107/EU and the Common Reporting Standard or equivalent agreements on the automatic exchange of information on Financial Accounts, including agreements with third countries. For the purpose of this hallmark, "reasonable to conclude" is determined from an objective standpoint by reference to all the facts and circumstances and without reference to the subjective intention of the parties involved.
Hallmark D2 – Non-transparent legal or beneficial ownership chains used *(not subject to MBT)*	Examples of cases of non-identification of beneficial owners are provided in the Guidelines. In relation to trusts, in case the beneficial owners are disclosed or identified, and such disclosure or identification is in accordance with the "Prevention and Suppression of Money Laundering Activities Law" then this hallmark does not apply.

Hallmark E *(not subject to MBT)*

Hallmark E1 – Use of unilateral safe harbour rules	Unlike hallmarks E2 and E3, hallmark E1 should not be taken to concern only arrangements between associated enterprises, but also dealings within the same legal entity (i.e., arrangements between a head office and its foreign permanent establishment). For the hallmark to apply, the use of unilateral safe harbour rules introduced by an EU Member State or a third country should always take place in the context of cross-border intragroup arrangements. Bilateral or multilateral advance pricing agreements concluded between tax authorities are not "unilateral" safe harbours and are therefore out of scope of hallmark E1. Further guidance is provided for Cyprus, according to which: (i) the use of the administrative simplification measure of 2% minimum margin after tax (i.e., margin of 2.29% before tax) on intragroup back-to-back financing transactions by Cypriot tax resident financing companies, as per the Transfer Pricing Circular of 2017; as well as (ii) the use of a return on equity of 10% (after tax) in the case of entities performing functions similar to those performed by regulated financial institutions or other parties engaged in credit-granting activities which are subject to the Regulation (EU) No. 575/2013, are both considered as unilateral safe harbour rules for the purpose of this hallmark.
Hallmark E2 – Transfer of hard-to-value intangibles between associated enterprises	"Rights in intangible assets", such as a license or a contractual right to use the intangible asset, should also constitute "intangibles" for the purpose of hallmark E2. There is also guidance on the categories of assets which can be considered as "intangibles", such as, inter alia, patent rights, know-how, trade secrets and trademarks. Further guidance is provided on the interpretation of the "hard-to-value" element of the hallmark with reference to indicative features or characteristics (e.g., partial development, no commercial exploitation, exploitation in a novel manner, etc.). It is noted that there should be a cross-border transfer of the intangible asset/right to the intangible asset, i.e., from an EU Member State to another EU Member State or from an EU Member State to a third country (or vice versa), for the hallmark to apply. A transaction involving only one person (e.g., transfer of tax residence) should not be considered a "transfer" for the purposes of this hallmark.
Hallmark E3 – Profit shifts following an intragroup cross-border transfer of functions and/or risks and/or assets	The term "transfer" includes changes based on contractual arrangements, as well as changes in the activities or conduct within a multinational group (i.e., not only changes of legal ownership, but also changes in the functions performed or the allocation of risks). There should be a "cross-border" transfer of assets, functions or risks between jurisdictions for the hallmark to apply and the transfer of tax residence is not considered a "transfer" for the purposes of hallmark E3. If the transfer is estimated to reduce the EBIT of the

	transferor by 50% or more during the three-year period after the transfer, this hallmark is likely to apply. The concept of "EBIT" (earnings before interest and taxes) refers to earnings for financial/accounting purposes and not to taxable profits. For the purpose of this hallmark, dividend income is not part of EBIT.

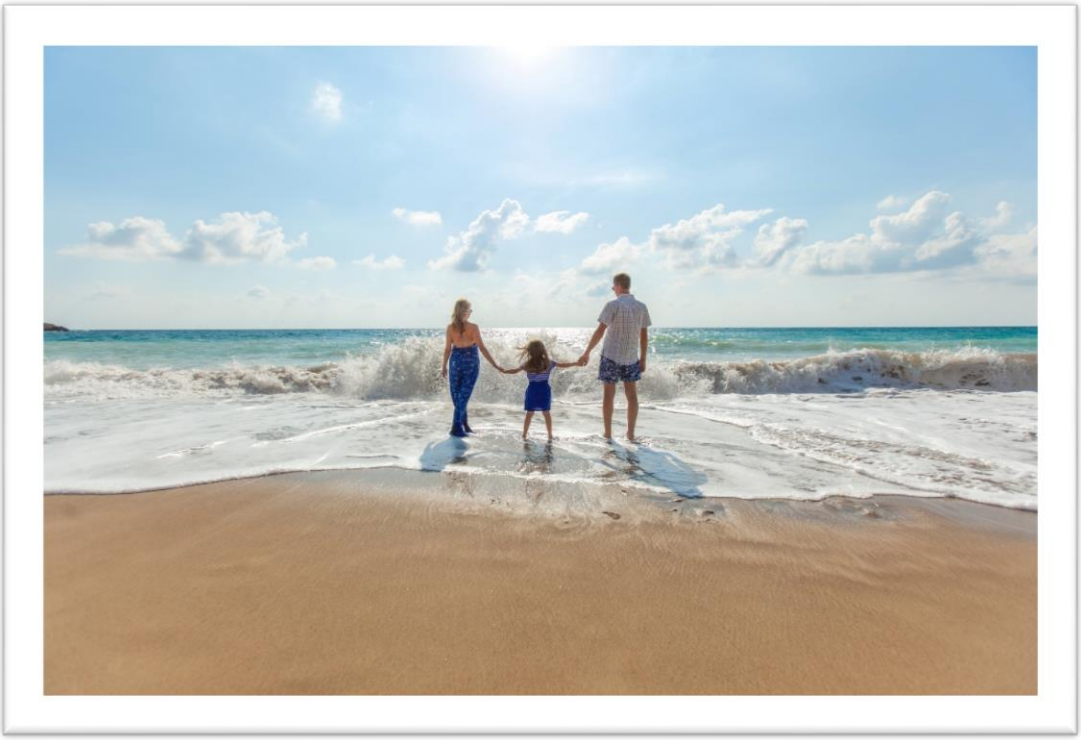
About Cube Audit

Founded in 2015, Cube Audit Ltd is an innovative and progressive professional services firm, incorporated as a Cyprus private limited company. The company is a Certified Public Accountants and Registered Auditors firm and it is authorized by the Institute of Certified Public Accountants of Cyprus (ICPAC) as a Registered Audit and Accounting Company.

We offer a comprehensive range of professional services to both local and international businesses, including Audit and Assurance, Financial Advisory and Business Consulting, Accounting and Financial Reporting, and Taxation.

At Cube Audit, our purpose is to provide tailored, practical and commercially viable advice and solutions to our clients in a diverse range of situations, regardless of complexity, in the areas of audit, accounting, tax and consulting.

Our vision is to be a trusted and respected financial and professional services firm that is built upon integrity, professionalism and a well proven track record.



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