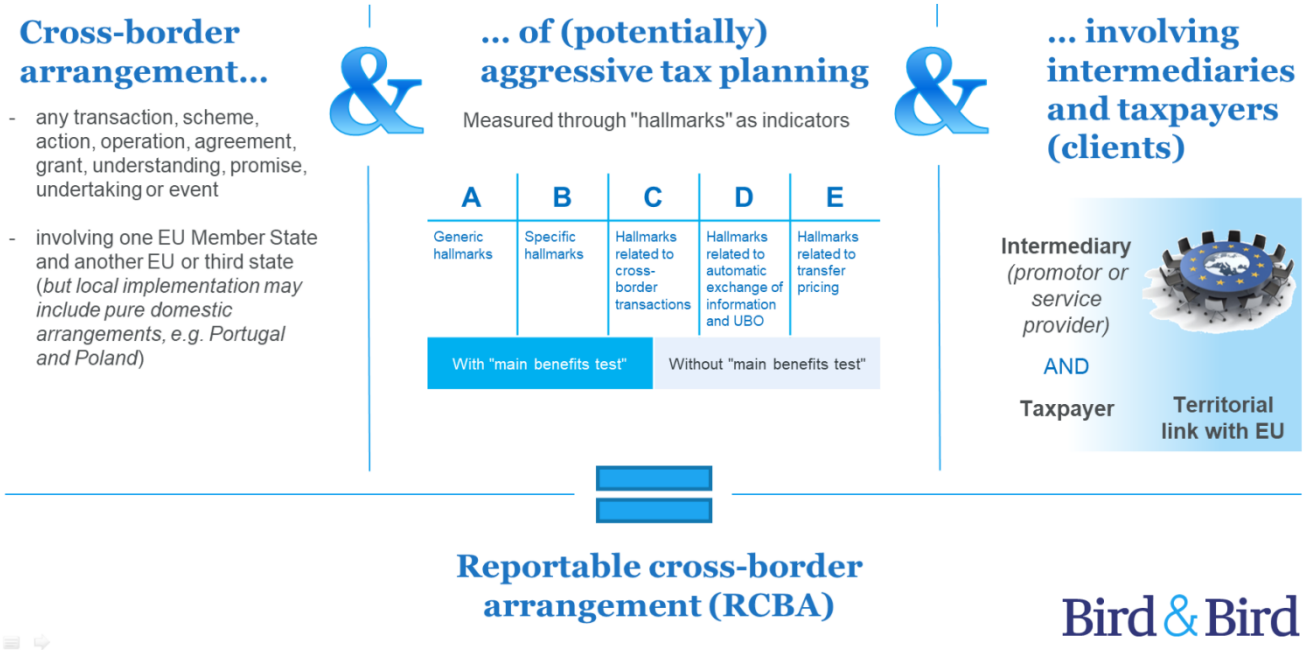
Bird & Bird & DAC6 Briefings: Financial Institutions

May 2020

DAC6 in a nutshell



"DAC6" or the 6th Directive on the Administrative Cooperation between EU Member States aims at improving the functioning of the internal market by discouraging the use of aggressive cross-border tax planning arrangements.

In a nutshell, the directive requires intermediaries (such as financial institutions) – or in certain circumstances the taxpayers themselves (such as the leasing companies) – to report any advice and/or implementation of a cross-border arrangement of potentially aggressive tax planning to the local tax authorities. The presence of such aggressive tax planning is evaluated on the basis of certain objective indicators (called "hallmarks"). Some of these hallmarks only become relevant if one of the arrangement's primary motives is to obtain a tax advantage. Others will just be reportable based on specific indications that the financial institution is (supposed to be) aware of.

For further general information, please consult the first issue of our DAC6 Briefings ("Introduction of a Mandatory Disclosure Obligation") or visit the DAC6 In Focus page on our website. This Briefing builds on the general knowledge of previous issues, with a focus on what these rules mean for financial institutions.

Key hallmarks for financial institutions

Hallmark A.3. targets arrangements with **standardised documentation** or based on a **standardised structure**. The main benefit test must also be met.

Hallmark B.2. targets arrangements that have the effect of **converting income** into capital, gifts or other categories of revenue which are taxed at a lower level or exempt from tax. The main benefit test must also be met.

Hallmark B.3. targets arrangements whereby **funds are being circulated** through various steps with no economic benefit.

Hallmark C.1. targets several **cross-border payments** to associated recipients that are resident in **tax favourable jurisdictions**, **not resident for tax purposes in any tax jurisdiction**, or resident in a **non-cooperative jurisdiction** (according to EU or OECD).

In most cases, a bank will not be informed of any of these arrangements by their customers and the mere execution of a payment instruction is not sufficient to qualify as aid, assistance or advice in regard to the arrangement.

Hallmark D.1. targets arrangements set up to **circumvent the automatic exchange of information** on financial accounts (such as bank accounts, savings accounts and so on).by using products that fall outside the definition of "financial accounts", by using jurisdictions that do not exchange information, by using entities or structures that do not have to report on account holders and by using jurisdictions that are weak in enforcing AML legislation.

Hallmark E.2. targets arrangements involving the transfer of **hard-to-value intangibles** between associated companies. The term "hard-to-value intangibles" covers intangibles or rights in intangibles for which, at the time of their transfer (i) there are no reliable comparables; and (ii) at the time the transaction was entered into, the **projections of future cash flows** or income expected to be derived from the transferred intangible, or the assumptions used in valuing the intangible are **highly uncertain**, making it difficult to predict the level of ultimate success of the intangible at the time of the transfer.

Note: *The above list is certainly not exhaustive for financial institutions, but rather a list of what are likely the most common hallmarks that will have to be monitored.*

How does this translate to banking activities?

Financial institutions will seldom qualify as promotor as they do not render any tax advice and do not actively participate in devising aggressive tax arrangements. Rather, they will qualify as service providers. And even in that capacity, they will quite often not be aware or assumed to be aware of their participation in a reportable arrangement.

So a bank should generally not qualify as an intermediary for **purely routine services** (such as receipt of deposits, money market transactions, commercial loans, custody and management of securities, or consumer credit). However, where the bank is knowledgeable about an arrangement for which it carries out the above activities, it may still be required to file a report.

In the **private banking** and wealth management business, banks should be attentive to cases of exchange of information (*e.g.* use of certain insurance products, foreign investment funds, trust-like entities, use of bearer securities) and conversion of income (when, for instance, advising on the restructuring of private wealth into more tax friendly products). Also standardized mortgage products to claim a tax benefit (*e.g.* a mortgage tax deduction) could fall in scope.

In the **transactional finance** area, banks should be wary of not being drawn into arrangements where a seemingly commercially driven transaction (securitisation, cross-border leasing, group financing structures…) is mainly set up for tax purposes. Banks should in those circumstances look out for standardized documents or structures, the roundtripping of funds or intragroup cross-border payments to targeted jurisdictions.

Finally, international financial institutions may have a reporting obligation in regards to their own (i) intra-group **transfer of intangibles** when shifting around IP on in-house developed innovations (such as banking software) or (ii) group-financing vehicles setup to benefit from tax advantages (such as a notional interest deduction) involving the **roundtripping of funds**.

How can Bird & Bird assist?

- Our international tax team advises clients on whether they have disclosure obligations, and whether or not certain activities contain hallmarks.
- We advise clients on how to manage and coordinate the reporting, if multiple intermediaries (whether or not in various countries) are involved, through DAC6 frameworks. We advise clients on how to manage and coordinate their reporting obligations, especially where multiple intermediaries (across a variety of countries) are involved.
- Please get in touch to find out more about how we can help.

Your key contacts

Brent Springael
Partner

Tel: +32 2 282 60 42
brent.springael@twobirds.com

Zoe Feller
Partner

Tel: +44 203 017 69 50
zoe.feller@twobirds.com

twobirds.com

Abu Dhabi & Amsterdam & Beijing & Berlin & Bratislava & Brussels & Budapest & Copenhagen & Dubai & Dusseldorf & Frankfurt & The Hague & Hamburg & Helsinki & Hong Kong & London & Luxembourg & Lyon & Madrid & Milan & Munich & Paris & Prague & Rome & San Francisco & Shanghai & Singapore & Stockholm & Sydney & Warsaw