

TAX NEWSLETTER

MARCH 2022

MANDATORY DISCLOSURE REGIME (DAC 6)

On 18 March 2021, the Cypriot Parliament voted for the amendment of the Cypriot Law on Administrative Cooperation in the field of Taxation ('Law N. 205(I)/2012' or the 'Law') implementing the European Union (EU) Directive on the mandatory disclosure and exchange of information on reportable cross-border arrangements (referred to as 'the 'Directive'), known as "DAC6".

The Law entered into effect as of 1 January 2021. However, it has a retrospective effect for reportable cross-border arrangements concluded on or after 25 June 2018, provided that one of the prerequisite triggering events is met.

The Cyprus DAC6 Law requires from intermediaries (including EU based tax consultants, banks, asset managers, corporate administrative service providers, insurance companies and lawyers) and relevant taxpayers to submit information to the CTA, in respect of cross border arrangements that meet at least one of the "hallmarks", as outlined in the Law.

Hallmarks represent the reporting triggers that indicate when information concerning a cross border arrangement must be submitted to the CTA and thus arrangement is classified as reportable.

A reportable cross border arrangement (RCBA) is an arrangement that concerns more than one EU Member State or an EU Member state and a third country. Under the Cypriot MDR Law, an arrangement is reportable if it is cross-border and meets at least one of the hallmarks A-E and the main benefit test (MBT), where applicable. The term 'arrangement' includes all types of arrangements, transactions, payments, schemes and structures, whether legally enforceable, and includes oral agreements. The MBT will be satisfied if it can be established that the main or one of the main benefits which, 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.

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As of 1 January 2022, reportable cross-border arrangements (RCBA) should be filed within 30 days from the day after the RCBA is made available for implementation or the day after the RCBA is ready for implementation or when the first step in the implementation of the RCBA has been made, whichever occurs first.

In order for Intermediaries and taxpayers to be able to file RCBA's can register in the Government Gateway portal "Ariadni" and upon validation, information on RCBA can be submitted.

Penalties on non-compliance vary depending on the type of infringement, with a maximum of €20.000 per arrangement.

CONSULTING REMARKS AND NEXT STEPS

Intermediaries, as well as taxpayers engaging in cross border arrangements, need to continuously monitor their disclosure obligations under DAC6 legislation.

In order to secure compliance with these new requirements and minimize the exposure to monetary as well as reputational damages, affected parties should take a series of holistic and robust actions. The implementation of specific procedures may be essential to ensure compliance with this new chapter in tax reporting obligations.

Our team of Tax experts in HLB Cyprus can help clients to understand DAC6, and the broader tax policy context, and implement effective controls and processes to ensure all reportable cross-border arrangements are proactively identified and managed.

Our team remains at your disposal for any information and/or clarifications required.

Best regards,

HLB Cyprus Tax Team



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Appendix 1

The hallmarks of DAC 6, described in Annex IV, are categorized as follows:

- A. Generic hallmarks linked to the main benefit test
- B. Specific hallmarks linked to the main benefit test
- C. Specific hallmarks related to cross-border transactions
- D. Specific hallmarks concerning automatic exchange of information and beneficial ownership
- E. Specific hallmarks concerning transfer pricing.

For a transaction to meet the disclosure requirements, it must meet at least one of the hallmarks, further discussed below:

Category A: Generic hallmarks linked to the main benefit test

Category A focuses on generic characteristics that can be found in tax avoidance schemes and planning. There are three arrangements that could fall into category A:

- 1. An arrangement where the taxpayer, or participant in the arrangement, enters into a confidentiality agreement regarding not disclosing how the arrangement could create a tax advantage
- 2. An arrangement where the intermediary is entitled to receive a fee for the arrangement, and that fee is (a) fixed relative to the amount of tax advantage of the arrangement, or (b) whether the tax advantage is actually derived from the arrangement
- 3. An arrangement that has substantially standardized documentation or standardized structure and does not require substantial customization for implementation

Category B: Specific hallmarks linked to the main benefit test

Category B focuses on arrangements with characteristics that could lend themselves to tax avoidance. The arrangements that fit this category fall under the main benefit test. There are three arrangements that could fall into category B:

- 1. An arrangement where a participant takes contrived steps in acquiring a loss-making company in order to reduce an entity's tax liability
- 2. An arrangement that converts income into capital, gifts or lower-taxed/tax-exempt income

3. Circular transactions result in the round-tripping of funds - namely, through involving interposed entities without other primary commercial functions or transactions that offset or cancel each other (or have similar features)

Category C: Specific hallmarks related to cross-border transactions

This category of hallmarks only refers to actual payments and not to “deemed”/“notional” payments or transfer pricing adjustments. In addition, where the payment is made to an entity that 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 Guidelines further clarify that 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., the interest used to finance the construction of a building and capitalized into the cost of the building). There are four arrangements that could fall into category C:

- 1) Deductible cross-border payments between two or more associated enterprises where at least one of the following apply:
 - a) The recipient is not a resident for tax purposes in any jurisdiction, or
 - b) The recipient is a resident in a jurisdiction that either:
 - i) has a corporate tax rate of below 1% or does not impose corporate tax
 - ii) is included in a country deemed non-cooperative by either the Member States collectively or within the framework of the OECD
 - iii) Recipient is a tax resident in a jurisdiction where the payment benefits from full exemption from tax
 - iv) the transfer or payment benefits from a preferential tax regime.
- 2) Deductions for the same depreciation on the asset are claimed in multiple jurisdictions
- 3) There is double tax relief in regards to the same item of income or capital.
- 4) Transfer of assets with a material difference in the amount treated as payable

Category D: Specific Hallmarks concerning automatic exchange of information and beneficial ownership

Category D focuses on arrangements that hinder transparency and reporting. The arrangements that fall into this section also fall outside of the scope of the main benefit test. There are two arrangements that could fall into category D:

1. An arrangement that may have the effect of undermining and circumventing the reporting obligations set out in DAC6 or taking advantage of legislation that limits reporting and transparency.

2. An arrangement that involves a non-transparent legal or beneficial ownership chain, with the use of persons, legal arrangements, or structures

Category E: Specific hallmarks concerning transfer pricing

Category E focuses on arrangements that are not at arm's length or contain uncertain pricing or base eroding transfers. There are three arrangements that could fall into category E:

1. An arrangement that involves and incorporates unilateral safe harbour rules;
2. An arrangement involving the transfer of intangibles that do not have a reliable comparable and that the projections of future cash flow are expected to come directly from that intangible, or the ultimate value of the intangible is uncertain at the time of the transfer; and
3. An arrangement involving an intragroup cross-border transfer of functions, risks, and/or assets, if the projected annual earnings before interest cause a more than 50% decrease in earnings before interest and taxes during the next three years.