



OECD releases final report on mandatory disclosure rules under Action 12

Executive summary

On 5 October 2015, the Organisation for Economic Co-operation and Development (OECD) released its final report on mandatory disclosure rules (Action 12) under its Action Plan on Base Erosion and Profit Shifting (BEPS). The final report, *Mandatory Disclosure Rules* (the Action 12 Report), was released in a package that included final reports on all 15 BEPS Actions.

The Action 12 Report makes a series of recommendations about the design of mandatory disclosure regimes intended to allow maximum consistency between countries while also being sensitive to local needs and to compliance costs. The Action 12 Report focuses in particular on international tax schemes, which are viewed as an area of special concern and the primary focus of the BEPS project. It states that disclosure schemes that are intended to address domestic avoidance might not be sufficient to capture cross-border arrangements and provides recommendations for an alternative approach. The Action 12 Report makes clear that the mandatory disclosure recommendations are not a minimum standard and that countries are free to choose whether or not to introduce such a regime.

EY is hosting a series of webcasts that will provide a comprehensive review of the final BEPS reports and consider the outlook for country action. The Action 12 Report will be addressed in a webcast on Anti-Abuse Measures under BEPS Actions 3, 5, 6 and 12 at 10am EST on 19 November 2015.

Detailed discussion

Overview of Action 12 Report

The Action 12 Report closely follows the discussion draft on Action 12 issued by the OECD on 31 March 2015. (For more information, See EY Global Tax Alert, [OECD issues discussion draft on mandatory disclosure rules under BEPS Action 12](#), dated 3 April 2015.) However, the Action 12 Report includes a discussion of information

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sharing developments, and the potential sharing of information received under mandatory disclosures, that was not included in the discussion draft. Moreover, the Action 12 Report explicitly states that countries are free to choose whether or not to implement a mandatory disclosure regime. Unlike several other BEPS Actions, the recommendations set out in the Action 12 Report do not represent minimum standards. Rather, in the Explanatory Statement accompanying the release of the final reports, the OECD describes the recommendations in the Action 12 Report as “guidance based on best practices for countries which seek to strengthen their domestic legislation relating to mandatory disclosure by taxpayers of aggressive or abusive transactions, arrangements, or structures.”

The Action 12 Report begins with an overview of key features of a mandatory disclosure regime and its interaction with other disclosure rules and compliance tools. It sets out options for the modular design of a mandatory disclosure regime. It includes a discussion of international tax schemes in particular and how these could be covered by a mandatory disclosure regime. Finally, it concludes with a brief discussion of information sharing that was not included in the discussion draft.

Mandatory disclosure recommendations

The Action 12 Report considers the mandatory disclosure regimes that have been implemented in various countries to identify and

evaluate design features that are commonly used. The United Kingdom’s Disclosure of Tax Avoidance Schemes rules are a particular focus of attention because they have been in place since 2004 and are perceived to have had considerable success in reducing aggressive tax avoidance. Other forms of disclosure, such as tax rulings, reporting obligations in tax returns and voluntary disclosure rules are also considered. The Action 12 Report includes comparisons of other types of disclosure regime already in existence. It concludes that mandatory disclosure is most effective for accomplishing the objectives of obtaining information early, allowing the promoters and users of aggressive tax arrangements to be identified and deterring the use of such arrangements.

The existing mandatory disclosure regimes considered in the Action 12 Report are either “transaction-based” or “promoter-based.” The former regime requires tax authorities to identify transactions that taxpayers must report when they enter into them. “Promoter-based” regimes place the onus on promoters to disclose arrangements that display prescribed hallmarks. The design recommendations set forth in the Action 12 Report draw on elements from both kinds of regimes.

Who has to report

The Action 12 Report states that countries will need to choose whether they place the onus for reporting primarily on promoters

or whether to implement dual obligations for reporting by both promoters and taxpayers. However, in the case where promoters have the primary disclosure obligation, it is recommended that this obligation revert to the taxpayer where the promoter is outside the jurisdiction or asserts legal privilege or where the arrangement is developed by the taxpayer alone (i.e., there is no promoter).

Where an arrangement is disclosed by a promoter only, the Action 12 Report recommends that the promoter be required to prepare client lists and that there be a scheme reference number system. These client lists and reference numbers also are viewed as useful tools even when taxpayers are subject to their own disclosure requirement, although the Action 12 Report notes that these tools may not be as essential where a jurisdiction has implemented a dual-reporting obligation for disclosure.

Countries are free to choose their own definition of promoter or adviser, although the Action 12 Report provides examples of definitions from existing legislation that it recommends countries use as a basis for their own definitions. For example, a “promoter” might be defined as a person that is responsible for the design, marketing, organization or management of a scheme, and an “adviser” as one who provides assistance or advice with respect to creating, developing, planning, organizing or implementing the transaction. The Action 12 Report

includes a further note, not included in the discussion draft, that input from relevant domestic stakeholders will be important in establishing the appropriate definition of promoter for a particular jurisdiction.

Threshold conditions

Mandatory disclosure regimes often have a threshold condition. For example, this might be a test of whether obtaining a tax advantage is a main benefit of the arrangement. Alternatively, a de minimis filter can be used (e.g., based on transaction size). The Action 12 Report acknowledges that threshold conditions can be appropriate because they help keep the number of disclosures to a manageable level. However, the Action 12 Report indicates that a de minimis filter would be unnecessary in combination with a main benefit test, because the regime would already be targeting only those schemes designed to generate a tax benefit. However, the Action 12 Report indicates that it may be appropriate to use a main benefit test as a pre-condition, with de minimis filters attached to specific hallmarks, so as to ease the administrative burden.

Hallmarks

In existing disclosure regimes, disclosure is often triggered by an arrangement that includes certain hallmark characteristics. The Action 12 Report recommends that the existence of a single hallmark in respect of a scheme should be sufficient to give rise to a disclosure obligation.

Hallmarks can either be general or specific, and the Action 12 Report recommends that each country's hallmarks should include a mixture of both types. General hallmarks should include a promoter's desire to keep the arrangement confidential or the requirement of a contingent or premium fee. The Action 12 Report indicates that a country may also want to adopt additional generic hallmarks such as one applying to standardized tax products.

In addition, the Action 12 Report recommends that countries use specific hallmarks designed for their local circumstances. Examples of specific hallmarks include leasing transactions, transactions similar to those included on a black list, those involving use of losses or income conversion schemes or transactions with counterparties in low tax jurisdictions. Individual countries are left to design the specific hallmarks most appropriate to their local circumstances and may attach a de minimis filter to individual specific hallmarks.

Countries may choose to adopt a hypothetical approach or purely factual objective tests when determining their generic and specific hallmarks. Unlike in the discussion draft, the Action 12 Report provides examples of factors relevant to the hypothetical application of the confidentiality and premium fee hallmarks. Under a hypothetical test, the confidentiality hallmark would be met if a scheme were sufficiently new and innovative that the

designer of the scheme would have required the details of the scheme to remain confidential irrespective of the existence of actual terms of confidentiality.

Timeframe for disclosure

The Action 12 Report recommends that where the promoter has the obligation to disclose, the timeframe for disclosure should be linked to the availability of the arrangement to users. Note that this timeframe could vary from an arrangement being available for implementation (when a fully-designed proposal has been communicated to a client), to a firm marketing approach being made (as in the United Kingdom, which could be earlier in the process), to an advisor being appointed a "material advisor" (as in the United States). Where there is a disclosure obligation on taxpayers, the Action 12 Report recommends that the timing of disclosure be linked to implementation of the arrangement. In both cases, the Action 12 Report notes the benefits of short timeframes for disclosure.

Penalties

According to the Action 12 Report, mandatory disclosure regimes should be enforced through financial penalties for non-compliance. The Action 12 Report notes that countries may also implement other types of penalties (including non-monetary penalties). In addition, the Action 12 Report recommends that domestic law be explicit about the consequences of reporting under a disclosure regime (e.g., disclosure does not mean that

the tax administration agrees with the proposed tax consequences of the arrangement).

Procedural matters

The Action 12 Report indicates that tax administrations will need to specify the information that must be disclosed. Furthermore, mandatory disclosure regimes will need to be supported by powers that allow the tax administration to inquire into the reasons for a failure to disclose and the identity of promoters and intermediaries and to request follow-up information. The Action 12 Report recommends that tax administrations set up a small unit focused on risk assessment and coordination of action with respect to the disclosures it receives.

International tax schemes

The Action 12 Report acknowledges that cross-border transactions raise particular issues for disclosure regimes because it may not always be clear in one jurisdiction whether a tax advantage has been obtained in another jurisdiction. Therefore, an alternative approach is recommended for the design of a disclosure regime for "international tax schemes."

The Action 12 Report recommends that threshold conditions, such as the main benefit test, should not apply to arrangements with cross-border outcomes. This is because the recommended hallmarks would target only arrangements of particular concern to the tax administration. Special hallmarks should be developed for cross-border outcomes. These hallmarks

should focus on BEPS-related risks posed by cross-border arrangements and should be broad enough to capture different and innovative planning techniques. These hallmarks should be both specific (in that they identify particular cross-border tax outcomes which raise concerns for the reporting jurisdiction) and generic (in that they are defined by reference to their overall tax effects and are capable of capturing any arrangement designed to produce those effects). In contrast to the discussion draft, so as to avoid unnecessary disclosures, the Action 12 Report also states that each tax administration should provide a specific list of tax regimes and outcomes that are not required to be disclosed. It further indicates that as part of the future work on monitoring the outputs from the BEPS project, countries may consider developing additional hallmarks, including model hallmarks to minimize overlapping disclosure obligations with respect to cross-border transactions.

The Action 12 Report recommends that the definition of reportable scheme in the international context should be broad and should include any arrangement that incorporates a material transaction with a domestic taxpayer and that gives rise to a "cross-border outcome." In this regard, an arrangement should be reportable only if it involves a transaction that has a material tax impact on the reporting jurisdiction. The Action 12 Report proposes that transactions should be reportable in a specific country only in

circumstances where a domestic taxpayer or their adviser could reasonably have been expected to be aware of the cross-border outcome of the arrangement. In contrast, the discussion draft would have required disclosure where the cross-border outcome arises within the taxpayer's controlled group or where the taxpayer was a party to the arrangement.

The Action 12 Report suggests that a domestic taxpayer or its advisor be required to disclose any material information that is within its knowledge, possession or control. It further recommends imposing an obligation on a domestic taxpayer, at the time it enters into a material intra-group transaction, to make reasonable inquiries as to whether the arrangement that gave rise to the transaction incorporates a cross-border outcome (as identified under any hallmark) and to notify the tax administration if the group member has not provided relevant information, the information is inadequate or incomplete or there is unreasonable delay in providing the information in respect of these inquiries. The discussion draft did not propose this obligation. Similar to domestic schemes, the Action 12 Report indicates that countries should choose whether the disclosure obligation for international schemes should be imposed on the taxpayer or promoter or both.

The Action 12 Report includes an example involving an intra-group hybrid mismatch arrangement—adapted from an example included in the final report on Action 2—

to illustrate how the recommendations regarding disclosure of international tax schemes could apply. The discussion draft had also included two additional examples (involving notional interest deduction and use of a client list) that are not included in the Action 12 Report.

Information sharing

The Action 12 Report concludes with a brief discussion of information sharing developments generally and under the BEPS Action Plan. It includes cross-references to the Action 5 requirement of compulsory spontaneous exchange of information on rulings and the Action 13 requirement of a three-tier approach to transfer pricing documentation (including a master file, a local file and a country-by-country report). Further, the Action 12 Report provides an update on the Joint International Tax Shelter Information and Collaboration (JITSIC) Network. It notes that the information to be spontaneously exchanged within the JITSIC Network could include information obtained under a mandatory disclosure regime and that the JITSIC Network provides a forum for cooperation among tax administrations with respect to emerging issues that are identified through such disclosure and exchange.

Implications

The OECD's final recommendations under Action 12 are in the form of best practices for countries to consider if they are interested in developing a mandatory disclosure regime. Companies should stay informed about any developments with respect to mandatory disclosure in the countries where they operate or invest. In addition to timing and effective dates, jurisdictions considering implementation of a mandatory disclosure regime may vary other key factors, including:

- ▶ Whether to place the onus for reporting on promoters or to employ a dual-reporting obligation that includes reporting by the taxpayer as well;
- ▶ The type of threshold condition (de minimis level or main benefit test) for reporting; and
- ▶ Whether to include additional general hallmarks and which specific hallmarks to include.

Webcasts

EY is hosting a series of eight tax webcasts that will provide a comprehensive review of the final BEPS reports and consider the outlook for country action:

- ▶ OECD BEPS Project Outcomes: Highlights and Next Steps - 15 October 2015, 10am EDT
- ▶ New Reporting under BEPS Action 13 - 20 October 2015, 10am EDT
- ▶ Digital Economy Developments and BEPS Action 1 - 27 October 2015, 12 noon EDT
- ▶ Permanent Establishment Developments and BEPS Action 7 - 5 November 2015, 10am EST
- ▶ Transfer Pricing and BEPS Actions 8-10 - 12 November 2015, 10am EST
- ▶ Anti-abuse Measures under BEPS Actions 3, 5, 6 and 12 - 19 November 2015, 10am EST
- ▶ Financial Payments and BEPS Actions 2 and 4 - 3 December 2015, 10am EST
- ▶ Dispute Resolution and BEPS Action 14 - 10 December 2015, 10am EST

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