KPMG position paper on the European Commission's public consultation on disincentives for advisors and intermediaries for potentially aggressive tax planning schemes (November 10, 2016 - February 16, 2017)

KPMG member firms in the EU[1] welcome the opportunity to respond to the European Commission's public consultation on "Disincentives for advisors and intermediaries for potentially aggressive tax planning schemes", issued on November 10, 2016 (the "Consultation"). Given the importance and complexity of the issues involved, in addition to responding directly to the questionnaire in the Consultation, we are providing further comments and explanations in this paper, as suggested in the final section of the questionnaire under "Additional information".

Introduction

KPMG member firms in the EU support the EU Commissions in its efforts to prevent tax avoidance and evasion. (As explained below we do not consider though that the Consultation should cover evasion.) In addition, KPMG's Global Tax Policy and Regulatory Professionals took an active role at an international level regarding the OECD's Public Discussion Draft on BEPS Action 12 Mandatory Disclosure Rules – which is the genesis of this Consultation - and submitted comments on April 29, 2015.

We note that taxpayers have the right to arrange their affairs in a tax efficient manner according to law. This includes the right of access to expert advice and to legal representation. It is the responsibility of advisers to represent their clients' interests in keeping with their own professional obligations and the relevant laws and regulations in the countries where they operate.

There will inevitably be a degree of tension between, on the one hand, taxpayers' desire to manage their tax liability and, on the other, the legitimate need of governments to raise tax and the expectations of society that everyone pays what is due. We believe that any modern tax system should help ensure the ethical behaviour of advisors, taxpayers and tax authorities and should be able to respond to arrangements that achieve 'unacceptable' outcomes.

In order to provide a framework to assist our professionals in making judgments about the advice they give, KPMG member firms, on a global basis, have therefore adopted a set of "Global Tax Principles for a Responsible Tax Practice". We also believe that the vast majority of tax advisors in the EU provide a positive contribution by enabling clients to understand and comply with their obligations. Nevertheless, we appreciate that, to the extent there are concerns that tax avoidance schemes are being sold by certain advisers or implemented by certain taxpayers, it is appropriate to consider the potential benefit of a mandatory reporting regime (MDR).

Summary

In summary, we consider that there is a need for further detailed discussions between tax authorities and governments of Member States, advisers, professional bodies and other interested parties before a decision can be taken on whether or not a MDR is needed within the EU and if so what form it should take. In particular:

- we query if it would be expedient to introduce a MDR at this point in time given that there is a significant number of new anti-avoidance measures which have been introduced or are being introduced at the EU level and which may render such a regime unnecessary;

[1] KPMG member firms located in the EU forming part of KPMG's Europe, the Middle East & Africa (EMA) region. For the purpose of this paper we only refer to member firms located within EU Member States.

- under the principle of subsidiarity we consider Member States should be encouraged to consider if they need to implement a regime in accordance with the BEPS Action 12, tailored to their particular laws and circumstances, rather than introducing an EU wide "one size fits all" MDR;
- further consideration should be given to the need for an EU wide MDR which only focuses on cross-border planning if it is considered that this would not be sufficiently addressed through national regimes; and
- as regards a code of conduct or ethical rules on tax planning we consider it would not be appropriate to introduce these as a legislative measure and that it may well be impractical to have one voluntary code adopted by all the different professional bodies giving tax advice through all the Member States. However, we believe guiding principles are crucially important when considering complex issues and recommend that the Commission consider further how to encourage all the relevant professions to adopt a code which works in their own environment, perhaps based on a *pro forma* set of principles.

We expand further on these points below. We also set out some considerations on implementation on the basis that a MDR is introduced and some comments on why we think the form of the Consultation itself is not helpful in addressing the key issues. This latter point makes the need for further dialogue all the more important.

1) **Is it appropriate to introduce a MDR at present**?

The EU has introduced and is introducing a considerable number of measures aimed at preventing what is perceived as avoidance or aggressive tax planning. These include Country by Country Reporting and the exchange of rulings under the Directive on Administrative Cooperation and the Anti-Tax Avoidance Directives (ATAD) I and II. Work is also being carried out on the list of non-cooperative third jurisdictions and related counter measures, to be completed in 2017. At a global level, through the OECD, work is being carried out on Multilateral Instrument (MLI) which will reduce the possibility to use tax treaties to create arbitrage. It is possible that with all these measures in force there will be little scope for the type of tax planning which is the subject of the Consultation, particularly at the cross-border, intra-Member State level. It may well, therefore, be advisable to wait until these measures are in place to see if there is still justification for imposing an administrative burden on both companies, advisors and tax authorities by mandating an EU wide MDR.

However, we do recognise that the alternative argument would be that an MDR is required precisely to see if these other anti-avoidance provisions are effective. Proper consideration therefore needs to be given to assessing the relative balance between the risk of tax being lost and the increased administrative burden and cost of implementing a new disclosure regime across 28 Member States.

2) **Subsidiarity**

According to the principle of subsidiarity, legislative acts should be taken at the member state level unless the matter can only be effectively dealt with by community wide legislation.

A significant part of a MDR will be to alert tax authorities to tax planning which relates entirely to the relevant domestic law. Given that each Member State has different tax laws and principles, there are strong arguments that it would be more efficient for each one to introduce

disclosure rules targeted to their own circumstances. Trying to introduce a “one size fits all” disclosure regime for the whole of the EU could create a number of problems. On the one hand it may not cover all potential types of planning in certain countries, meaning that it would either not be effective or each country would have to have the facility to introduce extra hallmarks and modify the common rules to suit its national law. On the other hand the MDR could be drafted so widely that it would potentially catch all planning in all Member States but this would mean that in many countries some of the hallmarks would be redundant so adding to the complexity and administrative burden of the regime.

We note that the UK, Ireland and Portugal already have regimes which are considered to have worked well in those countries. This suggests they should not now be overturned by a new EU wide rule. The UK applies a number of hallmarks relating to, for example, standardised NIC products, loss schemes for individuals and leasing arrangements. Such hallmarks would be irrelevant in, for example, the Netherlands, which demonstrates the difficulty of applying a uniform EU regime.

It may also be that in some countries there is (relatively) little aggressive tax planning and the resources of the tax authority would be better focused on such matters as transfer pricing rather than policing a disclosure regime which would be likely to have little impact.

Therefore, if it is thought that some form of MDR would be generally beneficial within the EU, the most appropriate route maybe a Recommendation from the Commission that Member States consider implementing the proposals in BEPS Action 12 as they think fit rather than introducing an EU Directive.

Notwithstanding the above, the one area where we can see that an EU wide directive *may* be of use is if it is thought that domestic MDRs would not pick up cross-border tax planning which is nevertheless considered to be aggressive. In such a case there may be merit in having a specific EU MDR regime which only focuses on cross-border arbitrage/mismatches. We note that existing MDRs (e.g. in the UK) do apply to cross-border planning – so it should not be assumed there would be a gap in domestic rules. Nevertheless, we recommend that the Commission consults with tax authorities and advisors in order to determine if this would be an appropriate way forward.

3) Implementation issues

Assuming that a MDR is introduced – whether a general one or one focused on cross-border planning - we would like to make the following points on implementation.

First, we note that there are frequent references to tax evasion in the Consultation. Tax evasion is materially different from tax avoidance/aggressive planning – however that is defined – and is a criminal activity. We would like to emphasise that throughout the EU tax advisers are bound by the rule of law, including anti-money laundering rules and various forms of professional conduct rules. KPMG’s own Global Tax Principles state “We act lawfully and with integrity and expect the same from our people, our firms’ clients, tax authorities and other parties with whom we interact.” Many other advisers will have similar codes by which they operate. Therefore the tax advisory profession is already bound by laws against tax evasion and we believe the vast majority of advisors are vigilant in the fight against evasion. There is therefore no need for a

MDR to apply to evasion. Furthermore, as evasion relies on dishonestly hiding information from the tax authorities it follows that a MDR is not appropriate to tackle such behaviour: if a person fraudulently fails to disclose or misrepresents information in a tax return, it is highly unlikely they would comply with the obligation to disclose under a MDR. Tax evasion should be dealt with, as it currently is, through tax law and other instruments such as anti-money laundering rules and the Common Reporting Standard.

Secondly, consideration needs to be given to the issue of client confidentiality/legal privilege. There are varying rules in Member States which protect or mandate client confidentiality and which apply to various professional bodies. In some countries legal privilege against having to disclose client confidential information only applies to lawyers. In other countries this is extended to all tax advisers. It is true that anti-money laundering laws already override client confidentiality in some cases and this precedent could be extended. The issue will be balancing the need for taxpayers to have access to legal representation with the need to fight tax avoidance. In the UK, for example, lawyers can still claim exemption from disclosure. In France, which does not have a MDR, even anti-money laundering disclosures have to go through a specially elected representative of the legal profession (the Bâtonnier) to help protect client confidentiality. Due to the patchwork of different rules we therefore consider an EU wide MDR would only work efficiently if the disclosure obligation was on the taxpayer, not the intermediary. As a fall back, the intermediary could be required to give notification of the type of planning involved but not to give information about the taxpayer involved (this was the way in which the UK rules originally worked).

Thirdly, unlike the BEPS 12 proposal, the Consultation also suggests the MDR could be used "to ensure tax law compliance by national tax authorities." We do not think this is an appropriate use of the MDR and would create confusion. An advisor is highly unlikely to suggest a taxpayer enter into a transaction which they believe is not compliant with national law including EU state aid rules. Even if they did report such a transaction, if it is the tax authority which is not enforcing the rules correctly, they are not likely to act upon the disclosure. We therefore consider that such matters are better dealt with through existing mechanisms such as the exchange of tax rulings and state aid laws.

Finally, any MDR which is introduced must be proportionate. This means the hallmarks and tests for whether or not a structure is notifiable must be sufficiently targeted so that the regime does not result in taxpayers or advisers having to make a significant number of disclosures of purely commercial transactions or schemes already known to the tax authority. This would put an administrative and cost burden on taxpayers, advisers and tax authorities alike. Furthermore, if there are too many irrelevant disclosures tax authorities may be unable to act on the information received so undermining the whole regime.

4) Comments on the drafting of the Consultation document

We appreciate that the Consultation document itself if a fairly blunt instrument to elicit views from a wide range of participants. Nevertheless we wish to point out that there are a significant number of defects in the drafting which both make it very difficult to answer in places and will reduce the value of responses. We have listed some examples below:

- The definition of “aggressive tax planning” is too generic, in particular because it refers to “taking advantage of ….mismatches between two or more tax systems for the purpose of reducing tax liability.” Read literally, this covers advising on any case where there is different treatment of the same item in two jurisdictions. For example, an adviser may have informed a client that dividends on preference shares are tax deductible in one country while they are exempt as a return on equity in another. The advice here is simply about what two domestic laws say and intend as the tax consequences. However, this is potentially caught by the definition. Consequently any firm which advises on cross-border issues may consider it has to say “yes” to the question about whether or not they are an “intermediary for potentially aggressive tax advice”; but this cannot be the intention behind the Consultation. Furthermore, there is actually not a definition of *potentially* aggressive tax advice which adds to the confusion. Given that an MDR is about gathering information in order to determine if certain planning is aggressive and should be stopped – it is not about actually deciding if it is, *a priori* – we believe the focus should be on defining the characteristics which would make planning *potentially* aggressive rather than having such a catch all defining of aggressive planning. We also note there is no comment box provided for this question so a respondent cannot elaborate on the answer given. In answering the question we have therefore focused on the fact that aggressive planning must “*take advantage*..” of tax rules which we assume means to use them in an inappropriate way – which is something which would be contrary to the KPMG Global Tax Principles. Furthermore, we note that when any MDR comes into force the possibility that cross-border tax mismatches will exist will have greatly reduced as the ATAD I will be in force and it is likely that the ATAD II and MLI will have been approved. We have therefore replied “No” to this question. While we will continue to advise clients objectively on what the law says, including where there are mismatches in policy, we do not consider this is intended to or should be covered by the definition.
- In evaluating potential hallmarks the available answers jump from “of limited use” to “very useful”. We consider this approach to be too simplistic and there should have been an option for “useful”. For example, both confidentiality clauses and premium fees are elements that have traditionally been used in mass marketed schemes. Both are hallmarks listed in the existing UK MDR. However, they are also fairly widely used in other situations – for example where an adviser does not want other parties to be able to rely on advice given, there is particular intellectual property in the advice or it is of a complex nature. Just one example would be where an adviser has realised that certain domestic law is contrary to EU law and a taxpayer is entitled to a refund of tax under EU law. The correct application of EU law to a transaction which has already been carried out cannot be described as aggressive tax planning, but it is quite possible that the adviser would ask for confidentiality or a premium fee. The most appropriate answer to the question about the usefulness of such a hallmark is therefore “useful” – as it is clearly neither “of limited use” nor “very useful”.
- Another potential hallmark refers to “use of entities subject to zero taxation…including hybrid entities..” We consider this is too wide and is conflating two separate issues. Use of entities in a country with zero tax may be for purely commercial reasons (e.g. there is a manufacturing plant there) or because the domestic law of the parent company specifically allows it. The presence of such an entity is therefore “of limited” use in determining if a structure is potentially aggressive. By contrast, if a principle is emerging in international taxation or at the EU level that there should always be symmetry

between a deduction and taxation, it would follow that the presence of a hybrid entity would be “useful” or “very useful” in indicating aggressive planning.

- We note that the hallmark “A general artificial arrangement ….for the essential purpose of avoiding…taxation…” is more of a definition of tax avoidance than a hallmark and is too generic to be used as such.
- A number of questions ask about the likely impact of a MDR – e.g. 5.3, 5.4, and Policy Options in 7. There is no room to comment on potential adverse effects or state “not relevant” as an answer. We have answered these questions on the basis of what we see as the potential benefits provided that any rules are introduced effectively which, as outlined above, we consider means introducing rules at the national level. While we have said that we believe MDR rules could reduce aggressive tax planning in appropriate circumstances we note that if a “one size fits all” approach is adopted it may prove unworkable, in which case it would have no beneficial effect.
- As pointed out in Part 1 above, there is a significant number of other EU anti-avoidance measures which will have come into force by the time any MDR is implemented. However, it is unclear if answers to the questions should be given on the basis that those rules are already in force or on the current state of affairs. The former is the only logical approach but it does appear the Consultation has been drafted on the latter basis.

5) Need for a code of conduct or ethical rules on tax planning

Tax advice is provided by a range of professional advisors in different EU Member States including accountants, lawyers, qualified members of tax advisory bodies and former tax authority officials. In some countries there are no professional rules covering the giving of tax advice. In others, professional rules do exist and in the UK these (the Professional Conduct in Relation to Taxation) apply to a number of the tax professions but not to lawyers.

Given that taxpayers have the right to access tax experts so as to understand their rights and obligations and that they have the right to legal representation, we do not consider it appropriate that legislation should be used to regulate how advisers make judgement calls on complex and inevitably partially subjective issues such as the border between acceptable and non-acceptable planning. The conflict of interest which would arise if such rules were policed by a tax authority is even clearer.

As stated above, KPMG has a set of Global Tax principles and we strongly believe that voluntary guiding principles are a powerful way of addressing these issues. Given the differences in the structure of the tax advisory profession and in local law across the EU, it may be very difficult to create one set of professional rules which would automatically cover all EU tax advisors. However, further consideration should be given to the Commission consulting on producing a recommendation that the various professional bodies introduce a local code of conduct, perhaps based on a *pro forma* set of principles.

6) Conclusion

In conclusion, while we support the Commission in its efforts to tackle unacceptable tax avoidance, we consider that there needs to be significantly more dialogue with all the relevant stakeholders to determine to what extent a MDR would be beneficial to Member States, how the principle of subsidiarity applies and, if an EU wide rule is to be introduced, whether it should be restricted only

to disclosure of cross-border planning which would not be reported under national rules. Without further engagement the risk is that a regime will be proposed which would lead to a considerable administrative cost on tax authorities and taxpayers alike without it having a significant beneficial impact.

We fully support the idea of guiding principles as being a useful framework to assist professionals in making judgement calls in complex situations. Given the differences in the tax advisory profession between different Member States, we consider this is best dealt with by the Commission recommending that all relevant bodies introduce an appropriate code of conduct, rather than trying to craft one EU code.

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February 16, 2017