

Special issue featuring B2 as the “Hallmark of the month”

A hallmark is defined as a characteristic or feature of a cross-border arrangement that presents an indication of a potential risk of tax avoidance, as listed in Annex IV of the Directive.

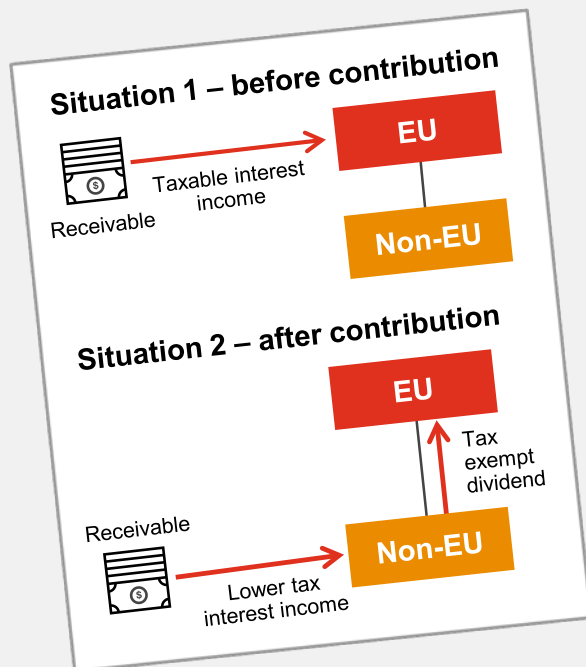
Hallmark B2

An arrangement is reportable under B2 if it has the effect of converting income into capital, gifts or other categories of revenue which are taxed at a lower level or exempt from tax.

Link to the Main Benefit Test (MBT)

Hallmark B2 is linked to the MBT. A cross-border arrangement having the characteristics or features of Hallmark B2 will therefore only become reportable if this test is satisfied. This test will be satisfied if it can be established that the main benefit 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.

Example 1 – Contribution of an interest bearing receivable



An EU parent company transfers an interest bearing receivable into a non-EU subsidiary (via an equity contribution). Amounts corresponding to the interest income are subsequently distributed from the subsidiary to the parent company via tax-free dividend distributions. Former taxable interest income is now converted into tax exempt dividends at the level of the EU parent company.

Could the contribution of the interest bearing receivable be within the scope of hallmark B2?

Assessment questions

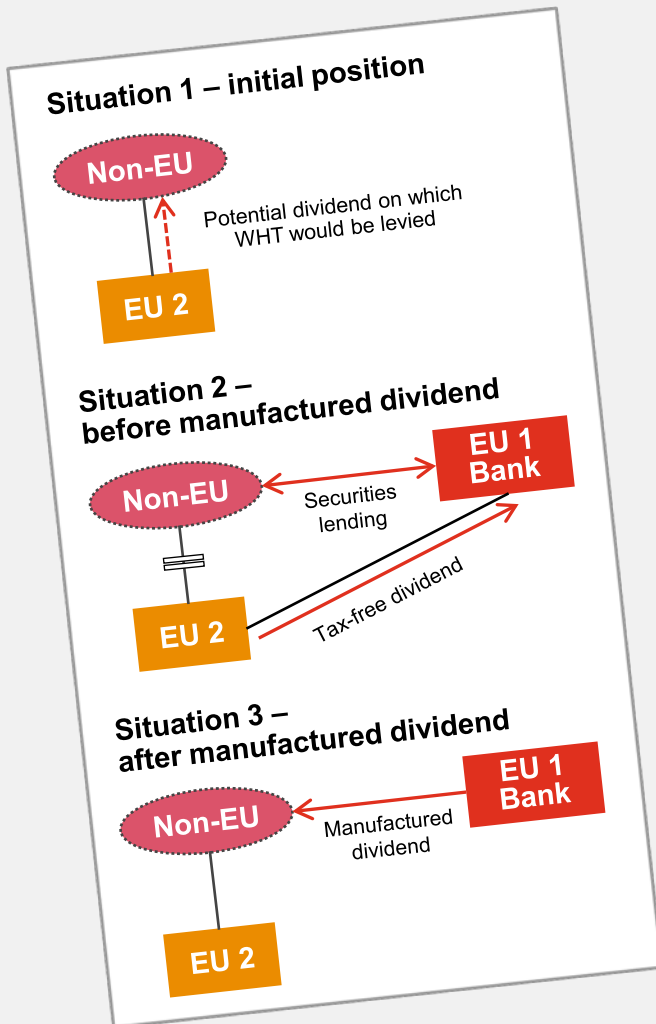
1. Is there an arrangement? **Yes**
2. Is there a cross-border element? **Yes**
3. Is there EU-nexus? **Yes**
4. Is income converted into a category which is taxed at a lower level or exempt from tax? **Yes (if considered from the perspective of parent company): taxable interest income is converted into tax exempt dividends.**
5. Is the MBT satisfied? **MBT could be satisfied.**

Conclusion

Based on the assessment above, hallmark B2 could be met. However, in order for the transaction to be reportable under DAC6, it should be established that this tax advantage is one of the main benefits of the arrangement.

In this context, it must first of all be assessed what the business drivers are for this transaction (e.g. change of Thin Cap Rules or customers/suppliers demanding higher equity at subsidiary level). As a next step, the different tax advantages must be assessed. In view of the latter, it would need to be evaluated whether the transfer of the receivable is a taxable event. In case of latent capital gain on the receivable, this aspect would be of relevance under the MBT. In addition, the question must be raised as to whether the MBT should be applied to the group result or to the individual group companies. This has a considerable impact on the MBT and therefore on the reportability of the arrangement. The MBT is also a concept that may differ from country to country depending on the exact implementation. One element that should be considered is the scope of tax applied by the countries involved.

Example 2 – Securities lending



Conclusion

Hallmark B2 could be met leading to the transaction being reportable under DAC6 if the MBT is satisfied.

Determining the tax advantage within B2

There are arguments to sustain that this hallmark does not cover cases in which a tax advantage obtained due to a 'conversion' of income is explicitly foreseen in the law for the specific transaction/structure (purpose of the law). This is consistent with the (non-binding) EU Commission Recommendations on Aggressive Tax Planning discussed below. Thus, for example, an increase in a participation resulting in the application of the participation exemption may not lead to an obligation to report, if domestic law foresees conditions to grant such an exemption. Certain countries like Germany, the UK and Austria take that approach, but it cannot be ruled out that other Member States take a different view.

Whether a tax advantage for the specific case can be derived from the purpose of the law depends not only on the wording of the provision, but also on the circumstances of the individual case and primarily on the teleology of the legal provision. Furthermore, tax advantages being legitimate from a stand-alone perspective can trigger a

A limited partnership (Non-EU), resident in a non-EU country, owns shares in an EU Company (EU 2). EU 2 is planning to distribute dividends. EU 2 would levy withholding tax (WHT) on the dividend payment.

Just before the distribution of dividend, the EU 1 bank (resident in EU 1) and Non-EU enter into a securities lending transaction with respect to shares in EU 2. The bank can apply a tax treaty between EU 1 and EU 2, effectively lowering the amount of WHT levied by EU 2.

After the distribution of dividend, the bank transfers the shares back to Non-EU. The bank pays a manufactured dividend to Non-EU (minus a securities lending fee).

Could the securities lending arrangement be within the scope of hallmark B2?

Assessment questions

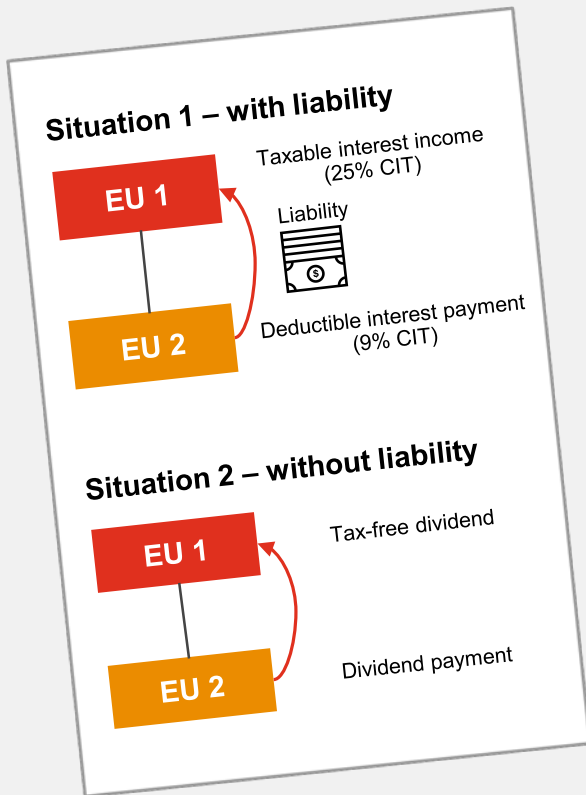
1. Is there an arrangement? **Yes**
2. Is there a cross-border element? **Yes**
3. Is there EU-nexus? **Yes**
4. Is income converted into a category which is taxed at a lower level or exempt from tax? **Yes, as Non-EU receives a tax exempt indirect dividend from the bank minus a securities lending fee (instead of a regular dividend subject to WHT).**
5. Is the MBT satisfied? **Depending on the approach taken in the relevant country, the MBT might be satisfied.**

reporting obligation, if they are achieved by arrangements, which are contrary to the purpose of the law.

This understanding of a 'harmful' tax advantage is based on the definition of 'aggressive tax planning' by the EU Commission, cf. [Commission Recommendation of 6 December 2012 on Aggressive Tax Planning, COM \(2012\) 8806 final](#): 'A key characteristic of the practices in question is that they reduce tax liability through strictly legal arrangements which however contradict the intent of the law. [...] Aggressive tax planning consists in taking advantage of the technicalities of a tax system or of mismatches between two or more tax systems for the purpose of reducing tax liability.'

Please be aware that this Commission Recommendation has a non-binding nature and national tax authorities may not interpret it in the same way.

Example 3 – Debt / equity swap



An EU 1 parent company holds 100% of the shares in an EU 2 subsidiary. The subsidiary has a liability against the parent company, that stems from a loan agreement. The subsidiary has to pay arm's length interest, that is taxable in the hands of the parent company.

The parent company waives its liability. The subsidiary subsequently distributes annual dividend payments (replacing former interest payments). As a result the parent company receives tax free dividends instead of taxable interest income.

Could the waiver of the liability be within the scope of hallmark B2?

Assessment questions

1. Is there an arrangement? **Yes**
2. Is there a cross-border element? **Yes**
3. Is there EU-nexus? **Yes**
4. Is income converted into a category which is taxed at a lower level or exempt from tax? **Yes, the parent company has no taxable interest income in the second situation.**
5. Is the MBT satisfied? **MBT could be satisfied.**

Conclusion

Hallmark B2 could be met leading to the transaction being reportable under DAC6 if the MBT is satisfied. The MBT is, for example, met, if the corporate income tax (CIT) difference between EU 1 and EU 2 is regarded being one of the main benefits deriving from the waiver. The tax treatment of the waiver itself would also be of relevance. However, when determining if the MBT is satisfied the overall conditions and circumstances of the case need to be taken into consideration.

Further remarks

The wording of hallmark B2 is rather broad, with the potential consequence that many common scenarios (e.g. debt waiver) are not excluded from being reportable. In order to understand the scope of hallmark B2, it can be considered that this hallmark has to be interpreted in the light of the meaning and purpose of the Directive.

It remains to be seen how this hallmark as well as the MBT will be implemented in the national legislation and ultimately interpreted by the tax authorities in different Member States.

The meaning of 'converting' income

Whether income is converted into other categories of revenues that are taxed at a lower level or exempt from tax, may need to be evaluated at individual company level. Therefore, this hallmark could potentially also be fulfilled if the conversion of income into tax exempt revenues at the level of one group company, leads to a higher tax burden at the level of another company in the same group. However, the MBT would also have to be met in order to be reportable.

How can PwC help you

Our team combines experts in tax, people, processes, data and technology. By bringing these different skill sets together, we can help you and your organization 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.

Furthermore, we have developed a DAC6 Smart Reporting tool that makes use of technology to ensure DAC6 compliance, while keeping costs under control. Find out more [here](#).

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