Tax & Business Lawyers

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NEWSLETTER

THE MOST RECENT ACTS OF THE EUROPEAN INSTITUTIONS REGARDING THE BATTLE AGAINST TAX EVASION

SUMMARY

This Information is intended to provide an update on various developments, at an European level, in terms of the battle against tax evasion and fraud.

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INTRODUCTION

1.

It is recognized that the pressure from various and well-known leaks, widely disclosed and materialized in various headlines and journalistic pieces, political messages and in intense legislative production, at national and international level, have increased the battle against tax evasion and fraud.

This mass production of legal instruments in the battle against tax evasion and fraud should, to a large extent, be applauded, inasmuch required to improve the tax justice, but without prejudice to the need of promoting better comprehensibility and predictability of tax legislation, as well as the need to respect the important principle of proportionality.

Therefore, this Newsletter aims at assisting all readers to follow the recent developments that we deem most relevant, at an European level, regarding measures against tax evasion and tax fraud.

THE EUROPEAN PARLIAMENT'S DRAFT RESOLUTION NO. 2020/2080 (INI)

2.

On March 21, 2023, the European Parliament's Budget and Finance Committee approved the text of the initiative of a European Parliament Resolution *on lessons learnt from the Pandora Papers and other revelations* [2022/2080(INI)] ("Draft Resolution"), still pending approval from the Plenary.

With special emphasis on tax policy, this Draft Resolution mentions some projected to be called "harmful practices" regarding the income and personal assets taxation.

Said Draft Resolution therefore aims at what it identifies as a "trend" of the Member States of the European Union to "adopt legal frameworks designed to attract high-net-worth individuals, foreign pensioners and highly skilled workers to invest or live in their territory, notably granting them generous tax benefits and exemptions which do not apply to nationals".

The Draft Resolution also expresses concern about "shell companies", applauding the European Commission's initiative with the Unshell Directive Proposal (which we will address below).

In this sense, the Draft Resolution urges the Governments of the Member States to reverse this so-called *trend* and to proceed with the adoption of wealth

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taxes, focusing on the taxation of ownership and succession of financial assets and luxury goods.

In face of the above, and if approved by the Plenary, the Draft Resolution will constitute a political initiative to pressure (i) the introduction of wealth taxes in a more transversal way in the European Union and (ii) the revocation of regimes such as the Portuguese Non-Habitual Residents regime.

3.

Notwithstanding, the projected position of the European Parliament does not seem to observe nor respect the differences and tax autonomy of each Member State, or the needs of some Member States to positively differentiate themselves to promote and attract investment, vital for its development, thus improving the level playing field among the Member States of the European Union.

In this sense, the Draft Resolution mainly has a political nature, which raises interesting issues of tax policy and respect for the tax sovereignty of each Member State, which is crucial for smaller countries such as Portugal.

THE *UNSHELL* DIRECTIVE PROPOSAL

4.

Regarding the Proposal for Council Directive COM(2021)565 final (*Unshell* Directive Proposal) – which foresees rules to prevent the abusive use of shell companies for tax purposes – the European Parliament has approved, hence recommending adoption by the European Council, even though with relevant changes, namely establishing updated criteria to assess shell companies, the respective sanctions and the requirements of the reporting obligations that are intended to be implemented.

With more detail regarding the Proposed Directive, see our Newsletter n.º 06/23.

5.

It is understood that the adoption of measures that make it possible to mitigate the illicit intermediation of companies that do not carry out any effective economic activity will be subject to popular approval, being also applauded from the perspective of strengthening the confidence that citizens, in general, should have in European tax systems.

Notwithstanding, the result of the Proposed Directive in question may be insufficient, or even unfair, given the

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proposed imposition of new and difficult compliance obligations on economic agents, increasing their already high tax compliance burden.

In fact, said Proposal seems to burden and harm the normal carrying out of an activity within the European Union, namely since it appears to mold and model the way in which these activities are carried out. Taxable businesses are forced to conduct their activity across the European Union by the book of the substance indicators foreseen in the Proposal, and shall make efforts to provide elements to justify their reporting obligations, if existent, or even the sharing of business models or other trade secrets to justify the valid economic reasons behind their activity, at the expense of otherwise suffering tax consequences or penalties.

6.

On the other hand, such reporting obligations are supported by legal rules that make use of indeterminate concepts, which will certainly generate concern among economic operators, given the potential different interpretations that those may arise across the European Union.

Given the possible forcing of disclosure of business models or other trade secret information to demonstrate that a given entity does not exist for tax reasons, it appears that the reporting obligations foreseen in the Proposal may be contrary to the principle of legal certainty and to tax privacy.

7.

Finally, in our view, the Proposed Directive places too much power on the Tax Administrations to, in a somehow discretionary way, assess, positively or negatively, the way that certain businesses carry out their activities.

After recent amendments to the Anti-Tax Avoidance and Administrative Cooperation Directives in tax matters, the proposal for an Unshell Directive seems hasty, given that, before the effects of said changes are reasonably known, it is intended to advance measures with an impact on the entire economic and business environment. Thus, its proportionality, in view of the intended purposes, is questionable. It may also motivate a "capital flight" to other jurisdictions, therefore not being the most effective measure to solve the identified problems from an international point of view.

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8.

Therefore, developments that will occur within the scope of discussion and eventual approval of said Directive by the European Council must be monitored, namely the date of entry into force and the measures that are approved to minimize the impact on the business of small and medium companies across the European Union.

DAC 8 PROPOSAL

9.

On December 8, 2022, the Commission published a legislative proposal for the revision of the Council Directive 2011/16/EU (DAC 8), which foresees several relevant amendments.

The main amendment proposed is the introduction of a crypto asset reporting framework, based on the similar regime proposed by the OECD, foreseeing a set of due diligence and compliance rules for crypto asset service providers/platforms, namely for reporting information on operations with crypto assets, including their users, as well as rules to facilitate the exchange of information between the tax authorities of the Member States of the European Union.

After AMLD5, which established mechanisms for reporting these transactions within the scope of legislation against money laundering, and the approval of MiCA, regulation that establishes a legal framework for crypto assets, with rules and requirements for service providers in this area, as well as after the DAC 7 (see below), which establishes reporting rules for digital platforms, the DAC 8 Proposal "closes the circle", by foreseeing the exchange of information, for tax purposes, in the context of transactions with crypto assets.

Finally, it should be noted that the ECOFIN Council reached an agreement, on 16 May 2023, on its position – general orientation – regarding this Directive Proposal.

10.

The DAC 8 proposal also aims to broaden the scope of application of the rules on the exchange of information regarding advanced cross-border rulings that concern high-net worth individuals (these being understood as people who hold a minimum of one million euros on financial assets, assets invested or under management, excluding personal residence).

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Therefore, it will also be important to monitor the legislative process regarding the approval of this Directive Proposal and the transposition that will follow into the national law.

THE DEVELOPMENTS OF DAC 7

11.

In order to regulate the transactions of goods and services through digital platforms, the Council of the European Union also approved Directive 2021/514, of March 22, 2021 (DAC 7), which amended the Directive 2011/16/EU, from 15 February 2011 on administrative cooperation regarding taxation.

The main focus of DAC 7 is to increase transparency and face the multiple tax challenges posed by the digital platforms-based economy, introducing new compliance rules and mandatory automatic exchange of information to be communicated by platform operators to Member States.

12.

The Directive imposes that the legislative, regulatory and administrative provisions must be applied by Member States from January 1, 2023. The Portuguese Council of Ministers approved, on February 16, 2023, the Draft Law n. 64/XV/1 for the transposition of Directive (EU) 2021/514, which is pending approval by the Portuguese Parliament.

For this purpose, the referred Portuguese Draft Law suggests amendments to the General Regime of Tax infractions (RGIT), to the Complementary Regime of the Tax Inspection Procedure (RCPITA), and to the fourth amendment of Decree-Law n.º 61/2013, of 10 May, on administrative cooperation in the field of taxation.

In this context, it is important to monitor the legislative process regarding the transposition of said Directive into Portuguese law.

THE DEVELOPMENTS OF DAC 6

13.

Directive 2018/822, of May 25, 2018 (DAC 6) approved a new paradigm regarding the exchange of tax information, with the introduction of obligations to notify tax administrations of certain cross-border mechanisms with tax impact.

These communication obligations must be complied by any intermediaries that intervene in those mechanisms, whether by way of designing, commercializing, organizing or applying, except if the intermediary is under protection of

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professional privilege, as in the case of Lawyers.

In this case, the intermediary/lawyer, who is prima facie prevented from carrying out the report, must notify the other intermediaries (for example: tax consultants or accountants) involved that he/she will not promote this communication of the mechanism to the Tax Administration.

14.

On 8 December 2022, and under the Case C-694/20, an important Judgment was issued by the Court of Justice of the European Union, which ruled on the Request for a preliminary ruling filed by the Belgian Constitutional Court.

In this process, the CJEU reviewed the provision of DAC 6 which provides for the aforementioned obligation of communication by the intermediary who is protected by professional privilege, to the other intermediaries, of the situation of professional privilege.

15.

In this context, the Court of Justice took the view that this obligation of communication conditions lawyers to provide information, what is not compatible with the Charter of Fundamental Rights of the European Union, namely regarding the inviolability of citizens' correspondence and confidentiality of Client/ Lawyer relations.

The Court of Justice also declared that the limitation to the rights protected in the Charter should be adequate, necessary and proportional to the pursuit of the underlying purpose of battling tax evasion and aggressive tax planning, understanding that the aforementioned disclosure, by a Lawyer, namely without the Client's consent, of his knowledge of a certain mechanism which, however, he/she cannot report due to professional privilege, would be a breach of the mentioned principles that is not adequate, necessary or proportional to the aforementioned purposes.

In view of the above, the Court of Justice decided that the legal provisions of DAC 6, which require the intermediary Lawyer to notify others of the professional privilege impeding a notification from the said Lawyer are invalid.

16.

We appreciate the significant ruling by the Court of Justice, which is commendable as it reaffirms its responsibility to oversee the mandates set forth by European Directives, thereby advocating for the rights and interests of its citizens.

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The verdict rendered by the Court of Justice appears to us to emerge as a logical necessity: Given that DAC 6 acknowledges the sanctity of professional confidentiality, it would not be acceptable for it to disregard this very principle when it involves disclosing to third parties the existence of a client-lawyer relationship, even if it pertains to intermediaries, or if it concerns facts known under that relationship.

Moreover, such a disclosure seemingly stems from a prejudiced stance taken by the lawyer about this situation, almost as if pressuring the other parties into fulfilling the communication obligation.

17.

The Case C-623/22 will be observed with keen interest as the Court of Justice will examine, among other aspects, whether DAC 6 violates the principle of legality in criminal matters, the general principle of legal certainty, and the respect for private life. This scrutiny will focus on the directive's use of undefined concepts in situations subjected to communication requirements, or to the extent that the obligation to share information about the mechanisms interferes with the right to respect the privacy of intermediaries and pertinent taxpayers.

CONCLUSIONS

18.

In light of the foregoing, we must appreciate the ongoing fight against aggressive tax planning and evasion, a priority on the agenda of European institutions. However, it is also crucial to demand a sense of rationality in the decisions that are being made, to ensure the preservation of private autonomy, the sanctity of personal life, legal security, professional privilege, and the predictability of tax rules. This rationality is also vital for fostering a conducive and healthy environment for any company operating within the European Union.

Moving forward, we will continue to closely monitor the latest developments in this arena in the near future.

***

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