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# Tax alert

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### *DAC6 has entered into force. What will change in tax consulting?*

The fight against cross-border aggressive tax planning is a pressing issue in the European Union.

On 25th of June 2018, **Council Directive 2018/822/EL<sup>1</sup> (hereinafter: DAC6)** amending Directive 2011/16/EU on administrative cooperation in the field of taxation entered into force (**hereinafter: directive on administrative cooperation in the field of taxation**). The said Directive regulates the exchange of information between tax authorities in European Union.

The new directive is aimed to fight against aggressive tax planning and strengthen tax transparency.

The Estonian Ministry of Finance also had a role to play in the making of the Directive, as Estonia was the Presidency of the Council of the European Union and at the time one key issue was the fight against cross-border aggressive tax planning<sup>2</sup>. According to the experts of the Ministry of Finance, tax optimization and tax evasion are major problems for European Union's internal market and the success of internationally operating companies cannot be based on unpaid taxes.

What is the problem according to the experts of Ministry of Finance?

It was found that taxpayers and tax consultants, who face tax laws in different countries on a daily basis, have knowledge of tax system gaps and inconsistencies. This advantage over local taxpayers and tax authorities is exploited to develop new and complex cross-border arrangements, which allow optimizing or avoiding tax payment. The solution was to create a regulation that would obligate tax consultants (and in some cases taxpayers) to share information with tax authorities on

which cross-border arrangements are recommended and used for tax evasion. When the new rules come into force tax authorities would also begin to mutually share the information received, so that there would be possibility to regulate the new arrangements through law amendments or tax audit.

The fight against aggressive tax planning has been supported by the Member States, as a proof on 13<sup>th</sup> of March 2018, the finance ministers unanimously agreed on the introduction of a mandatory reporting obligation for cross-border arrangements and was it was adopted by ECOFIN on 25<sup>th</sup> of May.

### *Content of DAC6*

DAC6 is a nightmare for all tax consultants, as it forces each so-called intermediary, including tax consultants, to inform the Tax and Customs Board of potential aggressive cross-border tax planning arrangements at the threat of a penalty. After the tax authorities have received the information, they will regularly exchange information (quarterly) with their colleagues in other Member States through the Common Communications Network (CCN).

It is up to the Member States to lay down penalties against violations of national rules that implement the Directive, but according to the Directive, such penalties should be "effective, proportionate and dissuasive".

According to DAC6 intermediaries is defined as any person that designs, markets, organizes, makes available for implementation or manages the implementation of reportable cross-border arrangement, but also any person who provides assistance or advice with respect to the services mentioned above. To the extent that the intermediary is entitled to legal professional privilege under national law, the disclosure obligation shifts to the taxpayer who benefits from the arrangement. Thus, it is

<sup>1</sup> Council directive (EU) 2018/82 of 25 May 2018 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements.

<sup>2</sup> <https://blogi.fin.ee/2017/07/neli-maksualgatust-mis-on-eestil-eesistumise-ajal-laual/>.

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strived to ensure that the tax authorities would in any case receive the information about the arrangements that can be connected to cross-border aggressive tax planning.

It is worth mentioning that the concept of “aggressive tax planning” is not defined in the DAC6. Instead, in the annex IV of the new Directive („Hallmarks“), reference is made to a number of hallmarks, which are features that could describe a serious threat as tax evasion or tax abuse:

- 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 cross-border arrangements to require being reported to the tax authorities, at least one of the hallmarks specified in the annex IV must be met- i.e. trait or feature, which indicates to the potential risk of tax evasion. Briefly, there is reporting obligation if there is a tax evasion that is reasonably foreseeable as a result of the arrangements.

### *Taking over DAC6, adaptation of standards and the first period for submitting the declaration*

Member States incl. Estonia must transpose the Directive into their national laws and regulations by 31 of December 2019. It is likely that the Tax Information Exchange Act will be amended and upgraded.

The date of application of the DAC6 is 1<sup>st</sup> of July 2020.

It is important for the taxpayers to note, that Estonia as a Member State has to implement measures to require information from intermediaries or any associated taxpayers about cross-border arrangements, where the first step for the arrangement occurred between 25<sup>th</sup> of June 2018 and 1<sup>st</sup> of July 2020. The information about

cross-border arrangements has to be filed by 31<sup>st</sup> of August 2020, after which the information is exchanged between the Member States.

### *Tax Information Exchange Act*

The directive on administrative cooperation in the field of taxation has been transposed into Estonian law with Tax Information Exchange Act, which provides the procedure rules and base for automatic information exchange. The remaining part of the directive on administrative cooperation in the field of taxation (i.e. Information exchanged on self-initiative or at the request) has been transposed into the Taxation Act, which sets the ground rules for international aid.

According to directive on administrative cooperation in the field of taxation, Estonia automatically exchanges information on earned income, board member fees, pension and income derived from immovable property regarding any person who is located in another Member State

### *Prior amendments of directive on administrative cooperation in the field of taxation*

For refreshing the memory, we will recall previous amendments to the directive on administrative cooperation

In 2014, the Directive was amended for providing the exchange of financial accounts information about tax residents in other countries. Banks, insurance companies and other financial institutions must collect and forward the information on accounts related to holding of funds, including settlement and securities accounts to the Tax and Customs Board. Such “accounts” also include life assurance contracts. Information is not collected on individual transactions. In order for financial institutions to be convinced of what client the exchange of information can

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affect, they can ask the client for confirmation of their tax residence. In the context of the exchange of information, a person may be exposed simultaneously to several countries.

The information exchange relates in particular to those who have a residence, set or have an economic interest in the foreign state, i.e. those who might be subject to tax in foreign state. If the client is an Estonian tax resident, information about his accounts is not forwarded to the tax authority.

Financial institutions began to collect information for European Union and OECD countries about their clients from 2016. Estonian Tax and Customs Board transmitted the information received to the tax authorities of the countries concerned in September 2017. For more information about the information exchange, please see the homepage of Ministry of Finance: <http://195.80.113.140/fatca>.

## Automatic exchange of information on binding rulings

In 2017, according to the amendments to the Directive in 2015, the information about binding rulings with a cross-border dimension were automatically exchanged between tax authorities. The exchange of information did not bring any additional obligations to entrepreneurs.

The exchange of information applies to the binding rulings issued as from 2012.

## Information exchange for multinational enterprises

As of 2018, according to the amendments to the Directive in 2016, there is a reporting obligation for multinational enterprises i.e. country by country reporting. Both, information exchange model and automatic exchange of financial accounts information model, have been copied according to the standards from the OECD model.

Annual reporting includes key information on income tax liabilities, profits, share capital, tangible assets, branch of activity (of subsidiaries) and number of employees in multinational enterprises with consolidated revenue of over EUR 750 million. If there are problems with reporting in the country where the parent company of a group is located, the liability for reporting falls on its subsidiaries. The tax authority will forward the report to the countries in whose territory the group operates. For the first time, the groups had to report information concerning the financial year of 2016 by the end of 2017 at the latest.

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