

Finland publishes official tax guidelines on Mandatory Disclosure Rules

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Executive summary

The Finnish Parliament approved the government bill implementing the European Union (EU) Directive on the mandatory disclosure and exchange of cross-border tax arrangements (referred to as DAC6 or the Directive) on 16 December 2019. The legislation was subsequently ratified by the President of the Republic of Finland on 30 December 2019.

The Finnish legislation entered into force on 1 January 2020 and is effective from 1 July 2020. In accordance with the Directive, the legislation is also retrospectively effective to arrangements where the first step is implemented on or after 25 June 2018.

The Finnish Mandatory Disclosure Rules (MDR) legislation is broadly aligned to the requirements of the Directive.

On 30 April 2020, the Finnish Tax Authorities (FTA) published the official tax guidelines (tax guidance) regarding the interpretation of the Finnish MDR legislation.

The tax guidance is partially based on the explanatory notes of the government bill published by the Finnish Government during the legislative process. It also provides some clarity on the definitions of the terms of the Directive and further explanations and examples on the interpretation of the different hallmarks and other rules introduced with the Finnish MDR legislation.

This Alert addresses the key differences between the final Finnish MDR legislation and the Directive and summarizes certain key clarifications provided by the explanatory notes of the Finnish government bill and the FTA's tax guidance.

On 5 June 2020, the FTA published the MDR reporting schema. Individuals (and e.g., foreign entities under certain circumstances) may file their MDR reports by using a manual form which was then published by the FTA on 24 June.

Detailed discussion

Background

The Council of the European Union Directive 2018/822 of 25 May 2018 amending Directive 2011/16/EU regarding the mandatory automatic exchange of information in the field of taxation (the Directive or DAC6), entered into force on 25 June 2018.¹

The Directive requires intermediaries (including EU-based tax consultants, banks and lawyers) and in some situations, taxpayers, to report certain cross-border arrangements (reportable arrangements) to the relevant EU member state tax authority. This disclosure regime applies to all taxes except value-added tax (VAT), customs duties, excise duties and compulsory social security contributions.² Cross-border arrangements will be reportable if they contain certain features (known as hallmarks). The hallmarks cover a broad range of structures and transactions. For more background, see EY Global Tax Alert, [Council of the EU reaches an agreement on new mandatory transparency rules for intermediaries and taxpayers](#), dated 14 March 2018.

EU Member States were to adopt and publish national laws required to comply with the Directive by 31 December 2019.

The key differences between the final Finnish legislation and the Directive are summarized below. This Alert also highlights some clarifications provided by the explanatory notes of the Finnish government bill and by the FTA in its tax guidance regarding the interpretation of the Finnish MDR legislation.

Scope of taxes covered

The scope of the taxes covered under the final Finnish legislation is fully aligned with the Directive and applies to all taxes except VAT, customs duties, excise duties and compulsory social security contributions.

Reportable arrangements

Under the Directive, an arrangement is reportable if:

- ▶ The arrangement meets the definition of a cross-border arrangement; and
- ▶ The arrangement meets at least one of the hallmarks A-E specified in Annex IV of the Directive.

Under DAC6, cross-border arrangements are defined as arrangements concerning more than one Member State or a Member State and a third country. The hallmarks can be distinguished as hallmarks which are subject to the main benefit test (MBT), and those which by themselves trigger a reporting obligation without being subject to the MBT.

The definition of reportable arrangements included in the final Finnish legislation is aligned with the Directive and the final Finnish legislation does not include any additional hallmarks in addition to the hallmarks of the Directive. Finland has chosen not to extend the reportable arrangements to cover domestic arrangements.

Pursuant to the tax guidance published by the FTA, the term "arrangement" must be interpreted broadly and can cover for example any business transaction, scheme, action, agreement, subsidy, understanding, promise, undertaking, event or other transaction. In practice the concept of "arrangement" will be interpreted through the hallmarks.

According to the tax guidance, a reportable arrangement consists of all the actions needed for fulfilling the conditions of a hallmark or for achieving a potential tax benefit. A reportable arrangement consisting of separate transactions or parts should be reported as a whole and the separate transactions or parts of the arrangement would not, as a starting point, need to be reported separately.

The tax guidance gives an example where a Finnish parent company repeatedly makes certain payments to its subsidiary company located in a jurisdiction that imposes corporate tax at the rate of zero (meeting hallmark C1(b)(i), cross-border payments between associated enterprises made to recipients in low-tax jurisdictions). The tax guidance states that each payment shall not be reported separately but the arrangement should be reported as a whole.

Hallmarks A-E of the Directive

Most elements of the hallmarks included in DAC6 are not expressly defined. The explanatory notes of the final Finnish legislation and the tax guidance published by the FTA provide some clarification on these elements, such as:

► **Hallmark A2 (success fees):** The tax guidance clarifies that services related to assistance with tax returns, withholding tax refund applications or other assistance with paying or refunding of taxes would not in general be deemed to fulfill the conditions for Hallmark A2 even if the fee for these services is dependent on the tax benefit. These services do not concern the designing or implementing of an arrangement but are related to assisting with administrative measures.

However, the tax guidance points out that a withholding tax refund application can be part of a reportable arrangement under another hallmark such as hallmark C3 (Multiple claims of relief for double taxation) in which case hallmark A2 could also be met.

- **Hallmark B1 (acquisition of a loss-making company and discontinuance of main activity):** The tax guidance indicates that the conditions of this hallmark are not met if the main activity of the acquired company continues several years after the acquisition. On the other hand, the hallmark could be met even if the main activity of the company is discontinued before the acquisition.
- **Hallmark B2 (converting income into capital, gifts or other categories of revenue which are taxed at a lower level or exempt from tax):** An arrangement would not normally be regarded as reportable under this hallmark if the intent of the tax legislation is followed, i.e., if the tax legislation allows for the arrangement to be carried out in two or several alternative ways, even if one leads to a more advantageous tax result.
- **Hallmark C1(a) (deductible cross-border payments between associated enterprises to recipients not resident for tax purposes in any jurisdiction):** The tax guidance states that an arrangement shall be reportable under hallmark C1(a), if the recipient of the payment is an entity transparent for tax purposes and the partners/owners of that entity located in the same jurisdiction as the entity are not taxed on the income of the entity.
- **Hallmark C1(b)(i) (deductible cross-border payments between associated enterprises made to recipients in low-tax jurisdictions):** Based on the explanatory notes this hallmark covers cases where payments are made to a country with no corporate tax or a nominal tax rate of zero/almost zero. Almost zero is understood in practice to be less than 1%.
- **Hallmark C1 (c) (deductible cross-border payments between associated enterprises benefitting of full exemption of tax):** According to the tax guidance,

investments in foreign investment funds or in partnerships forming a fund structure would not be covered by the hallmark as the investments are not regarded as deductible payments. The fact that the investment can later be deducted from the redemption price for calculating the capital gain is not relevant in evaluating whether the conditions of the hallmark are met.

- **Hallmark C2 (deductions for the same depreciation on the asset):** The tax guidance indicates that deductions for depreciation claimed both in the location country of a permanent establishment (PE) and in the country of residence of its head office are outside the scope of this hallmark provided that the profits of the PE are subject to tax in both jurisdictions.
- **Hallmark E1 (unilateral safe harbor rules used):** In accordance with the Organisation for Economic Co-operation and Development (OECD) Transfer Pricing Guidelines 2017 (OECD TPG), safe harbors do not include administrative simplification measures which do not involve determination of arm's-length prices (such as e.g., an exemption from documentation requirement), advance pricing agreements or thin capitalization rules. Hence, arrangements concerning these measures would not meet the E1 hallmark and would not be subject to reporting obligations.

The hallmark is intended to cover unilateral safe harbor rules which are not concluded between two or more jurisdictions. Arrangements that do not use safe harbor rules for transfer pricing are outside the scope of this hallmark.

The tax guidance mentions that an arrangement will not be reportable, if the OECD TPG have been applied in the arrangement and the transfer prices are proven as meeting the arm's-length principle in line with the OECD TPG, even if the prices used would also meet the level set by the safe harbor rule in question.
- **Hallmark E2 (hard to value intangibles):** The tax guidance states that the concept of "hard to value intangibles" will have the same meaning as provided for in the OECD TPG. An arrangement will not be reportable if the price of the hard to value intangibles to be transferred can be determined based on reliable comparables. The comparability should be assessed in line with the OECD TPG. Other transfer pricing methods used to determine the value of hard to value intangibles will not be regarded as meeting the criteria for a reliable comparable.

Furthermore, it clarifies that the projections of future cash flows or income expected to be derived from the transferred intangible, or the assumptions used in valuing the intangible may not be highly uncertain. The OECD TPG can be used to interpret the existence of uncertainty and to assess whether the arrangement meets the criteria of the hallmark and is therefore subject to a reporting obligation.

- ▶ **Hallmark E3 (arrangement involving significant profit shifts following an intra-group cross-border transfer of functions, risks or assets between associated enterprises):** Neither the Directive nor the final Finnish MDR legislation define the meaning of “intra-group” transfer. According to the tax guidance the definition of “associated enterprises” included in Finland’s domestic law which is applied for transfer pricing can be used here. Thus, the term “intra-group” would in general mean situations where the ownership limit of 50% is met directly or indirectly.

The tax guidance clarifies that in order to determine if the hallmark E3 is met, annual EBIT (earnings before interest and taxes) forecasts for the next three tax years following the transfer should be prepared.

The tax guidance also confirms that this hallmark will not be deemed to cover tax neutral restructuring transactions such as cross-border mergers or sales of shares in a subsidiary.

Main benefit test

In accordance with DAC6, the MBT 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.

The explanatory notes of the Finnish bill and the tax guidance mention that the “tax advantage” also covers tax advantages realized in non-EU countries.

The criteria of the MBT is not considered to be met if the arrangement concerns tax planning methods which are accepted under case law and tax practice or which are not in contradiction with the tax system or the meaning or purpose of applicable law or regulations.

Intermediaries

Under the Directive, intermediaries with EU nexus have the primary obligation to report arrangements to the tax authority. The Directive gives Member States the option to exempt intermediaries from the obligation to report where

the reporting obligation would breach legal professional privilege (LPP). If there are no intermediaries which can report, the obligation will shift to the taxpayers.

Aligned with the Directive, the final Finnish legislation defines intermediaries by reference to EU nexus. Only intermediaries with nexus to Finland will have a reporting obligation to the FTA.

The final Finnish legislation exempts certain intermediaries (attorneys, public legal aid counsels and lawyers who have been granted permission to represent in a court) from a reporting obligation due to national LPP. However, the exemption only applies to information subject to secrecy and testimony regulations, and the intermediaries subject to LPP are liable to report all other information required by the law on the reportable arrangements. Intermediaries that are exempt from reporting due to LPP are also required to inform other intermediaries or relevant taxpayers of their obligations to report.

Individual professionals employed by a legal entity (i.e., a company or partnership) should not themselves fall within the definition of “intermediary.” Instead, it is the legal entity that provides professional services and is legally responsible for those services to relevant taxpayers that should be regarded as the intermediary in respect of a reportable arrangement. Further, the explanatory notes of the legislation clarify that entities housing tax teams (so-called in-house tax teams) could also be regarded as an intermediary.

DAC6 and the final Finnish legislation define two categories of intermediaries, promoters and service providers. Service providers are defined as any person that knows or could be reasonably expected to know that they have undertaken to provide, directly or by means of other persons, aid, assistance or advice with respect to designing, marketing, organizing, making available for implementation or managing the implementation of a reportable cross-border arrangement.

The tax guidance clarifies that a service provider has a reporting obligation only if the service provider has knowledge of the facts relating to the arrangement and of the legal treatment of the arrangement in order to be able to determine whether it is a reportable arrangement and that the arrangement fulfills some of the hallmarks. The evaluation should be made based on the information received during the engagement and there is no obligation on the service provider to seek further information or carry out special due diligence procedures.

The tax guidance also gives some clarification on interpreting the role of financial institutions as service providers. A financial institution can be a service provider subject to reporting obligations when it actively participates in the planning, implementation or marketing of a reportable arrangement provided that the financial institution is sufficiently aware of the nature of the arrangement as a reportable arrangement. For example, providing a service related to the opening of a foreign bank account may be regarded as assisting with a reportable arrangement, if the bank is aware that this action contributes to the organization of a reportable arrangement.

However, the tax guidance indicates that if the role of a financial institution only covers the provision of payment transactions or other regular banking or insurance product offerings, the financial institution would not in general be deemed to be a service provider for the purposes of MDR.

Reporting deadlines

Under DAC6, for intermediaries (and relevant taxpayers), the trigger events for reporting under the Directive (from 1 July 2020) are when the reportable arrangement is “made available for implementation”; or when the reportable arrangement is “ready for implementation”; or when “the first step of implementation has been made.”

Under the Directive, reporting starts from 1 July 2020 and exchanges between jurisdictions from 31 October 2020. However, reports will retroactively cover arrangements where the first step is implemented between 25 June 2018 and 1 July 2020.

The same reporting trigger events apply in the final Finnish MDR legislation. Also, the time limits for filing the reports follow those of the Directive. These include setting a reporting period of 30-days for the intermediary and relevant taxpayer. In respect of marketable arrangements, in accordance with Article 8ab, Paragraph 2 of the Directive, the intermediary also has an obligation to make a periodic report every three months including all relevant information that has become available since the last report was filed.

Several EU Member States have announced that they will provide in their domestic legislation a deferral of the filing deadlines of DAC6 due to the COVID-19 pandemic. These announcements follow a political agreement reached by the ambassadors of the Member States at the COREPER II meeting on 3 June 2020. Under the amended proposal,

Member States are permitted to grant a six-month extension to the existing deadlines for filing and exchanging information on cross-border arrangements. The amended proposal also provides for the possibility of one further extension for a maximum additional three months but proposes to do so by means of a unanimous decision of the Council. On 24 June 2020, the Council of the EU announced that it adopted these amendments to the Directive.³

On 18 June 2020, The Ministry of Finance announced that Finland will not adopt the extension periods of the amended proposal to the existing deadlines for filing and exchanging information on cross-border arrangements. Hence, the reporting period of 30 days will be applied to reportable cross-border arrangements as from 1 July 2020 and the deadline for retroactively reporting arrangements where the first step is implemented between 25 June 2018 and 1 July 2020 will be 31 August 2020.

Thus, Finnish intermediaries and relevant taxpayers should pay close attention to the filing of their reports with the FTA within the above-mentioned deadlines. The MDR legislation allows MDR reports to be filed under certain conditions with a competent authority of another Member State, but it should be noted that the Finnish filing deadlines should still be followed. A failure to meet the Finnish deadlines could lead to the imposition of penalties.

Penalties

If an intermediary or relevant taxpayer fails to meet the reporting obligations a penalty can be imposed depending on the significance of the breach. The penalties are expected to apply as follows:

- ▶ Penalty of up to €2,000 in the case of a minor inadequacy or mistake in the report or in the mandatory procedures, and when the intermediary or relevant taxpayer with whom the reporting obligation lies has failed to fulfill the FTA's request for correcting the report or procedures.
- ▶ Penalty of up to €5,000 for a material inadequacy or mistake in the report or in the mandatory procedures, or for submitting or completing a report or mandatory procedures only after a request from the FTA.
- ▶ Penalty of up to €15,000 for submitting a materially false report deliberately or with gross negligence, or for failing to submit a report, or a deliberate or gross negligence failure to comply with other enacted obligations.

Next steps

Determining if there is a reportable cross-border arrangement raises complex technical and procedural issues for taxpayers and intermediaries. Taxpayers and intermediaries who have operations in Finland should review their policies and strategies for logging and reporting tax arrangements so that they are fully prepared for meeting their obligations.

Endnotes

1. For background on MDR, see EY Global Tax Alert, [EU publishes Directive on new mandatory transparency rules for intermediaries and taxpayers](#), dated 5 June 2018.
2. DAC6 sets out a minimum standard. Member States can take further measures; for example, (i) introduce reporting obligations for purely domestic arrangements; (ii) extend the scope of taxes covered; (iii) bring forward the start date for reporting.
3. See EY Global Tax Alert, [Council of the EU adopts amendments for deferral of MDR filing deadlines](#), dated 24 June 2020.

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