

## Estonia publishes draft proposal on Mandatory Disclosure Rules

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### Executive summary

The Estonian Ministry of Finance has published draft legislation, accompanied by explanatory notes implementing the European Union (EU) Directive on the mandatory disclosure and exchange of cross-border tax arrangements (referred to as DAC6 or the Directive). The draft legislation was published on 31 July 2019.

The Estonian draft legislation is subject to the formal legislative process and is likely to be amended before final enactment. If implemented as currently proposed, the Estonian Mandatory Disclosure Rules (MDR) legislation will be broadly aligned to the requirements of the Directive. The draft explanatory notes contain some useful interpretations which clarify the concepts and terms used in the Directive.

The draft legislation is expected to be finalized by the end of 2019.

### 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.<sup>1</sup>

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.<sup>2</sup> 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 are to adopt and publish national laws required to comply with the Directive by 31 December 2019. Estonia will introduce domestic legislation, which is planned to take effect from 1 July 2020.

The key highlights of the draft Estonian MDR legislation are summarized below. As outlined above, if the draft legislation is implemented as currently proposed, the Estonian MDR rules will be broadly aligned to the requirements of the Directive.

### Scope of taxes covered

The scope of the taxes covered under the Estonian draft 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 Estonian draft MDR legislation defines reportable arrangements in the same manner as the Directive. In line with the Directive, domestic arrangements are not included under the reporting requirements.

### Hallmarks A-E of the Directive

Most elements of the hallmarks included in DAC6 are not expressly defined. The draft Estonian legislation also does not provide additional clarification on specific elements of the hallmarks. Estonia plans to implement the hallmarks in the same way as the Directive with no additional hallmarks added.

### 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 same description for the main benefit test is included in the Estonian MDR draft legislation.

### 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.

The draft Estonian MDR legislation defines intermediary by the reference to Estonian nexus.

The draft Estonian legislation exempts Estonian attorneys and auditors from the reporting requirement if it would breach LPP. However, intermediaries that claim LPP are still required to inform other intermediaries or relevant taxpayers of their obligations to report.

The Estonian draft legislation defines an Estonian intermediary as someone who meets at least one of the following conditions:

1. Has tax residency in Estonia
2. Has provided services with respect to a cross-border arrangement through its permanent establishment in Estonia
3. Is incorporated or regulated by Estonian legislation
4. Is registered with a professional association which combines legal or tax advisory service providers

In the draft explanatory notes, it is explained that the obligation to report arrangements to the respective tax authority lies mainly on the persons providing tax advisory, accounting, financial investment advice and lawyers.

### 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.” The same trigger events apply in the draft legislation for Estonia.

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 Estonian reporting deadlines are expected to be fully aligned with the DAC6 reporting deadlines.

### Penalties

The draft Estonian MDR legislation foresees a one-off warning or penalty payment of up to €3,300, whereas it may not exceed €1,300 for the first event and €2,000 for the second event.

In addition, the following fines, established by the *Estonian Taxation Act* are expected to apply for failure to comply with the obligation:

- Fine up to €1,200 for natural persons
- Fine up to €3,200 for legal persons

### 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 Estonia should review their policies and strategies for logging and reporting tax arrangements so that they are fully prepared for meeting their obligations.

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## 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.

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