

Liisu Lell

**Tax Manager
Deloitte Advisory**

lless@deloittece.com



Amendments to Income Tax Law related to intra-group loans

The Estonian government's plan to introduce corporate income tax on outgoing loans (so-called pledge tax) was rejected by the parliament. Instead, alternative amendments to the Estonian Income Tax Act were adopted by the Estonian Parliament on 19 June 2017 and the Estonian President announced the Law on 29 June 2017. In accordance with the amended law, the Estonian Tax authority will have the right to tax the loans granted by Estonian companies to their parent or sister companies, in case the loan conditions indicate that in substance the loan may be a hidden profit distribution.

In addition, the law obliges to (quarterly) report information on loans granted to the related parties. The first deadline will be February 10, 2018, when the declaration submitted to the Tax and Customs Board must provide data on loans issued on or after July 1, 2017 or where loan amount has been increased or material loan conditions have been changed since July 1, 2017. It also changes the fact that in the case of loans that have been granted for more than 4 years, the burden of proof rests with the taxpayer - that is, at the request of the tax authority the taxpayer will be required within 30 days to prove the 1) ability and 2) willingness to repay the loans issued.

Fighting against the hidden profit distributions has been part of the Estonian Government's action plan for several years. The proposal to introduce the so-called pledge tax was challenged by different business organizations. The amendments adopted instead will provide the tax authority with more information for risk analysis and, hopefully, will also fulfill the broader objective, i.e. prevent the actual cases of hidden profit distributions.

The large intra-group loan transactions where Estonian subsidiaries of multinational groups have granted loans to their foreign parent companies have drawn public attention. In those cases the financial ability of foreign parent company to repay the outstanding loan is usually out of question. However so far the Estonian tax authority has not

been able to prove the unwillingness of paying back the loans.

The amendment is very recent and there is no detailed guidance yet. For the implementation, it is still necessary to specify what kind of loans should be included under the new regulation as well as to 1) compose the respective declaration form and 2) prepare guidelines to implement the new legal provisions. In this regard further cooperation between the professional associations, Ministry of Finance, Tax and Customs Board and tax advisors is inevitable. By amending the Income Tax Act, the state has very clearly indicated its intention to deal with the issue at hand. In the light of these changes it is expected that as a result of risk analysis the tax authority will map the transactions that by their nature refer to the potential hidden distributions of profits. Hopefully, the tax authority's future practice will not damage normal business activities of companies.