

Transfer Pricing Country Profile
(to be posted on the OECD Internet site www.oecd.org/ctp/tp/countryprofiles)

Name of Country: Estonia Date of profile: 6 December 2012

1. Reference to the Arm's Length Principle

Subsection 2 of Article 8 of Estonian Income Tax Act (*Related parties*) stipulates that the difference between the price used in the transaction of related parties (referred as a transfer price) and the value of a similar transaction between unrelated parties (referred as an arm's length price) is taxable according to transfer pricing rules (Article 14 (*Business Income*), Article 50 (*Income tax on dividends and other profit distributions*) and Article 53 (*Taxation of permanent establishment of non-resident legal person in Estonia*) of Estonian Income Tax) if it is not a fringe benefit.

Subsection 4 of Article 50 of Estonian Income Tax Act (*Income tax on dividends and other profit distributions*) and **subsection 4⁶ of Article 53 of Estonian Income Tax Act** (*Taxation of permanent establishment of non-resident legal person in Estonia*) stipulate the arm's length price rule – if the price of a transaction conducted between a resident legal person or a non-resident who has a permanent establishment in Estonia with associated persons is not in accordance with the arm's length price, the tax obligation will occur either on the income which the taxpayer would have derived or the expense which the taxpayer would not have incurred if the transfer price had been in accordance with the arm's length price. A similar provision is contained in **subsection 7 of Article 14 of Estonian Income Tax Act** that regulates taxation of business income of sole proprietor.

2. Reference to the OECD Transfer Pricing Guidelines (if any)

The OECD Transfer Pricing Guidelines (OECD TPG) have no legal status within the Estonian tax system. However, they have been translated into Estonian and, according to **Article 20 of the Regulation no. 53** drafted by MoF (in force since 1.01.2007), taxpayers and tax administrations are encouraged to use the OECD TPG for those situations not covered by the Regulation, as far as the guidance in the OECD TPG is not in contradiction with the Regulation.

3. Definition of related parties

The definition of the concept of related persons is contained in **Article 8 of the Income Tax Act** and according to that persons are deemed to be associated if they have common business interest or if one party has dominant influence over other. This article also includes an illustrative list of related parties:

§ 8. Associated persons

(1) Persons are deemed to be associated if they have a common commercial interest or if one person has dominant influence over the other. The following persons are always deemed to be associated:

- 1) spouses, civil partners, direct or in-law relatives;
- 2) companies belonging to one group as defined in § 6 of the Commercial Code;

- 3) a legal person and a natural person who owns more than 10 per cent of the share capital, total number of votes or rights to the profits of the legal person;
- 4) a legal person and a person who owns, together with other associated persons, more than 50 per cent of the share capital, total number of votes or rights to the profits of the legal person;
- 5) legal persons if more than 50 per cent of their share capital, total number of votes or rights to the profits belongs to one and the same person or associated persons;
- 6) persons who own more than 25 per cent of the share capital, total number of votes or rights to the profits of one and the same legal person;
- 7) legal persons whose management board members or bodies substituting the management board are the same persons;
- 8) an employer and an employee, the employee's spouse, civil partner or direct blood relative;
- 9) a legal person and a member of its management board or controlling body (§ 9), the spouse, civil partner or a direct blood relative of a member of the management or controlling body.

Transfer pricing rules apply to transactions of resident legal persons, non-resident persons operating in Estonia through a permanent establishment and also transactions of sole proprietors with any related persons.

4. Transfer pricing methods

The Regulation no. 53 provides five methods – the CUP, cost-plus and resale price method as well as the profit split method and transactional net margin method (TNMM) – that are the same as those in the OECD Guidelines. There is no compulsory hierarchy or system for applying the methods. It is up to taxpayer which method he chooses, but the choice needs to be appropriate.

5. Transfer pricing documentation requirements

For implementation of transfer pricing rules a resident company is required to submit additional information on the transactions with associated persons, activity of companies belonging to the same group and structure of the group at the demand of a tax authority. The tax authority shall grant the company a term of at least sixty days for submitting such information (**Subsection 7 of Article 50 of the Income Tax Act**).

The requirements for the information as well as the methods for determining the value of transactions are established by **the Regulation no. 53**.

Additional documentation requirements for transactions between related persons are contained in **Article 18** of the Regulation.

These additional requirements are imposed on the following persons and situations:

- resident credit institutions, insurance companies and companies quoted on the stock market;

- in case of transactions with related persons resident in low-tax jurisdictions;
- resident companies and non-resident persons operating in Estonia through a permanent establishment which, when considered with related persons, meet at least one of the following conditions: (1) they hire at least 250 employees, (2) their turnover in the financial year preceding the transaction was at least EUR 50 million or (3) their consolidated balance sheet total is at least EUR 43million¹.

The detailed documentation consists of two parts, namely (1) the main file (i.e. documents which contain unified information about all the members of a group) and (2) documents which contain information about transactions of a particular taxpayer concluded with related persons².

For other taxpayers document requirements are optional as recommendations.

6. Specific transfer pricing audit procedures and / or specific transfer pricing penalties

There are no special transfer pricing audit procedures or transfer pricing penalties.

The law provides for penalties in case of understatement of tax. The amount of penalties depends on the type of action – concerning the evasion of payment of taxes the punishment for legal person would be up to **13 000 EUR (Article 153¹ of the Taxation Act)**, concerning the tax fraud the punishment for legal person would be up to **32 000 EUR (Article 153² of the Taxation Act)**.

In case of obstruction of activities of tax authority (failure to submit a tax return, documents, things or other information by the due date etc) the fine is up to **3 200 EUR (Article 154 of the Taxation Act)**. Intentional submission of wrong information in tax return may also cause criminal proceedings where the fine is up to **16 million EUR (Article 44 of the Penal Code)**

7. Relevant regulations on Advance Pricing Arrangements

None.

8. Link to relevant Government Internet sites

Ministry of Finance of Estonia: <http://www.fin.ee/?lang=en>

Estonian Tax and Customs Board: <http://www.emta.ee/?lang=en>

9. Other relevant information

None

¹ The requirements are based on the Commission recommendation concerning the definition of micro, small and medium-sized enterprises (2003/361/EC) of 6 May 2003.

² The requirements are based on the Code of Conduct on transfer pricing documentation for associated enterprises in the EU (COM(2005)543) of 7 November 2005.

Note

1. Relevant provisions of domestic legislation referring to the Arm's Length Principle.
2. Reference if any to the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations in domestic legislation or regulations.
3. Relevant legislation or regulations containing a definition of related parties or associated enterprises.
4. Relevant legislation or regulations containing guidance on transfer pricing methods including hierarchy among them if any.
5. Relevant regulations if any in relation to transfer pricing documentation requirements.
6. Relevant regulations if any on specific transfer pricing audit procedures and / or specific transfer pricing penalties.
7. Relevant regulations if any on Advance Pricing Arrangements.
8. Addresses of the Internet sites of the relevant authorities in charge of transfer pricing policy, its administration and Advance Pricing Arrangements.
9. Other relevant information, for instance having gone through a peer review, or having new transfer pricing regulations in preparation.