ALDER & SOUND

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TAX CHALLENGES OF MULTINATIONAL ENTERPRISES

Aalto University, 9 May 2023

WHO ARE WE?

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MOBILE EMPLOYEES & RELATED CORPORATE RISKS

MOBILE EMPLOYEES & RELATED CORPORATE RISKS

DOMESTIC RULES AND TAX TREATIES

Domestic rules and tax treaties

Domestic rules

Taxation is always based on domestic law

Tax liability; registrations; compliance obligations

→ Local legislation and rules must be analysed

Double tax treaties

Double tax treaties can only limit taxing rights; taxing rights are never based on double tax treaties

DTTs divide taxing rights in a specific situation

→ Local interpretation of the DTTs must be analysed

Double tax treaties

DTTs

- Finland has extensive Double Tax Treaty ("DTT") network; Finland has a DTT in force with approximately 80 countries.
- All DTTs concluded by Finland are based on the OECD Model Tax Convention ("OECD Model"). OECD Model Commentary ("OECD Commentary") can be used to interpret the DTTs.
  - All Finland's DTT partners are not members of the OECD, and all DTT partners do not follow guidelines of the OECD Commentary.
  - Thus, interpretation of the applicable DTT may differ in Finland and in the contracting state.
- If there is no DTT in place, operating country's right to tax is based solely on the local tax legislation

EMPLOYEE & EMPLOYER OBLIGATIONS

Employee obligations

Employee's personal tax status

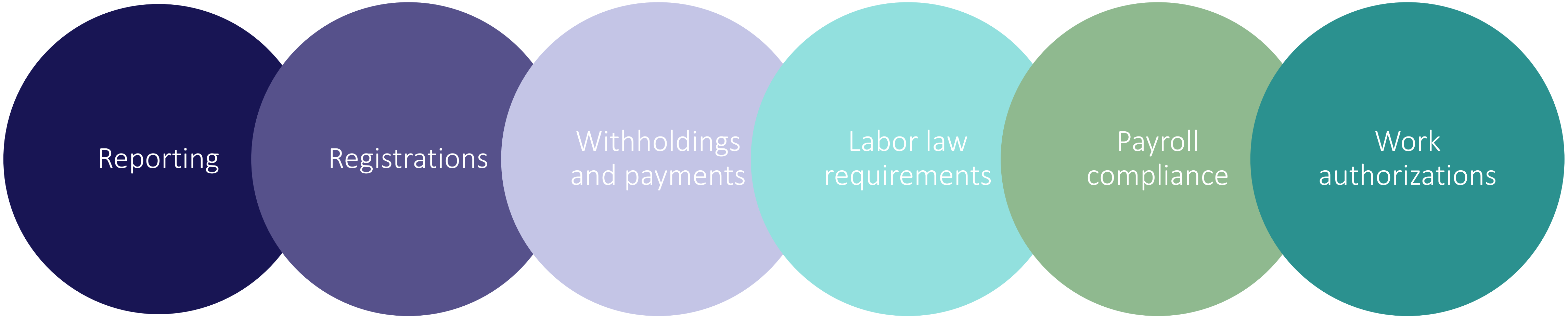
- Domestic legislation sets the base for the individual's status and regulates the taxation rights.
  - In cross-border situations, all working countries' legislations to be considered.
- Double tax treaties between the countries may limit the tax liabilities.
- Double taxation issues and **abolishment on double taxation** based on double tax treaty – exemption or crediting.
- Example: Finnish employee on assignment in Norway for seven months. Family,home and the permanent employment relationship remains in Finland.
  - Tax residency in both of the countries (domestic rules).
  - Tax treaty resident in Finland.
  - Depending on the exact number of days spent (under/over 183) and the company's status in Norway, the salary may become taxable in Norway or not.
  - If both countries impose tax on same income, the country of residency (Finland) will exempt the income taxable in Norway too.

Employee's social security coverage

- Different categories of social security coordination between the countries:
  1. **Full coordination** in EU area
  2. **Partial coordination** with the countries with which Finland has concluded a social security agreement
  3. **No coordination** between the countries – domestic legislation fully applicable
- Level of social security coordination depends on the country combination in question and the overall circumstances.
- Finally the local authorities make the decision of social security coverage.
- Generally, a certificate of coverage is issued by the authorities to prove the applicability of country's SS legislation.

Employer obligations

Regardless of the fact if the employee is liable for tax, social security or any other statutory payments in the country, often the employer has some obligations in the working countries.



PERMANENT ESTABLISHMENTS

Legislative framework – corporate income taxation

Permanent establishment in corporate income taxation

- Foreign business operations of a Finnish company may be subject to tax in the operating countries. Foreign country's right to tax is determined by domestic tax legislation.
- If Finland and the country of foreign business operations have a DTT in place, the operating country has a right to tax the business operations only if the operations qualify as a PE under the applicable DTA.
- The concept of a PE can be seen as a tool to divide taxing rights between two countries.

Permanent establishment in corporate income taxation

- In summary, activities which may lead to a PE according to the DTTs are:
  - Fixed place of business that is used to carry on business activities,
  - Construction and installation activities, and
  - Sales activities.
- Preparatory and auxiliary activities do not constitute a PE. In addition, activities of an independent agent do not constitute a PE.

Permanent establishments in corporate income taxation

The risk of a PE in corporate income taxation depends on local tax legislation and applicable tax treaty. OECD model tax treaty includes general guidelines for analysing the risk of a PE.

Fixed place of business

- A fixed place of business through which the business of an enterprise is wholly or partly carried on.
- Requires a place of business, i.e. a space, facilities, premises, installations, machinery or equipment, available for its use in the state. Also place of management.
- It is sufficient that employees use another company's facilities.
- The place of business must be fixed with a certain degree of permanence.
- *Art. 5(1-2) of the OECD Model*

Building and construction sites

- Building site or a construction or installation project.
- Requires a specific time period in order to constitute a PE. The time depends on the applicable tax treaty. Usually 6-12 months.
- The time test applies to each individual site or project separately. Projects which are unconnected with each other are treated separately even when carried out in the same state by the same constructor.
- *Art. 5(3) of the OECD Model*

Agents and representatives (sales)

- Broker, general commission agent or any other agent of an independent status acting in the ordinary course of their business do not create a PE.
- The agent must be independent both legally and economically. E.g. instructions and risk position are analysed.
- An agent may constitute a PE if the agent is not independent or does not act in the ordinary course of its business, e.g. concludes contracts, receives orders etc.
- *Art. 5(5) of the OECD Model*

Auxiliary and preparatory activities

- A fixed place, through which an enterprise carries on mere preparatory or auxiliary activities does not constitute a permanent establishment.
- Such activities may include the use of facilities solely for the purposes of storage, display or delivery of goods or collecting information for the enterprise.
- It should be analysed whether the operations of the PE are auxiliary or preparatory compared to the main business activities.
- *Art. 5(4) of the OECD Model Tax*

Risk indicators of a PE

The risk of a PE depends on the activities performed and permanence of the arrangement

Fixed place of business

Are there any kind of premises?
Are the group entity's core business activities carried out in these premises?
Is the arrangement permanent?
Do the activities include management level decisions?
If yes, the risk of a PE is higher

Building and construction sites

Does the project last longer than 6 months?
Does the project relate to construction or installation work?
Is the project connected to other projects in the same jurisdiction?
Are there multiple different employees consecutively longer than 6 months?
If yes, the risk of a PE is higher

Dependent agents and representatives

Does the representative have a right to conclude contracts in the name of the entity or receive orders that are binding?
If yes, the risk of a PE is higher

Auxiliary and preparatory activities

Are the activities merely preparatory or auxiliary in nature?
Are the activities just supporting activities and not core business activities?
If yes, the risk of a PE is lower

Building and construction sites

Does the project last less than 6 months?
If yes, the risk of a PE is lower

Independent agents and representatives

Does the agent operate in its own name?
Does the agent operate independently without instructions of the Group entity?
If yes, the risk of a PE is lower

Compliance obligations re PEs

- Tax reporting
- Financial reporting
- Registrations
- Profit allocation
- Elimination of double taxation
- Effects to employer obligations

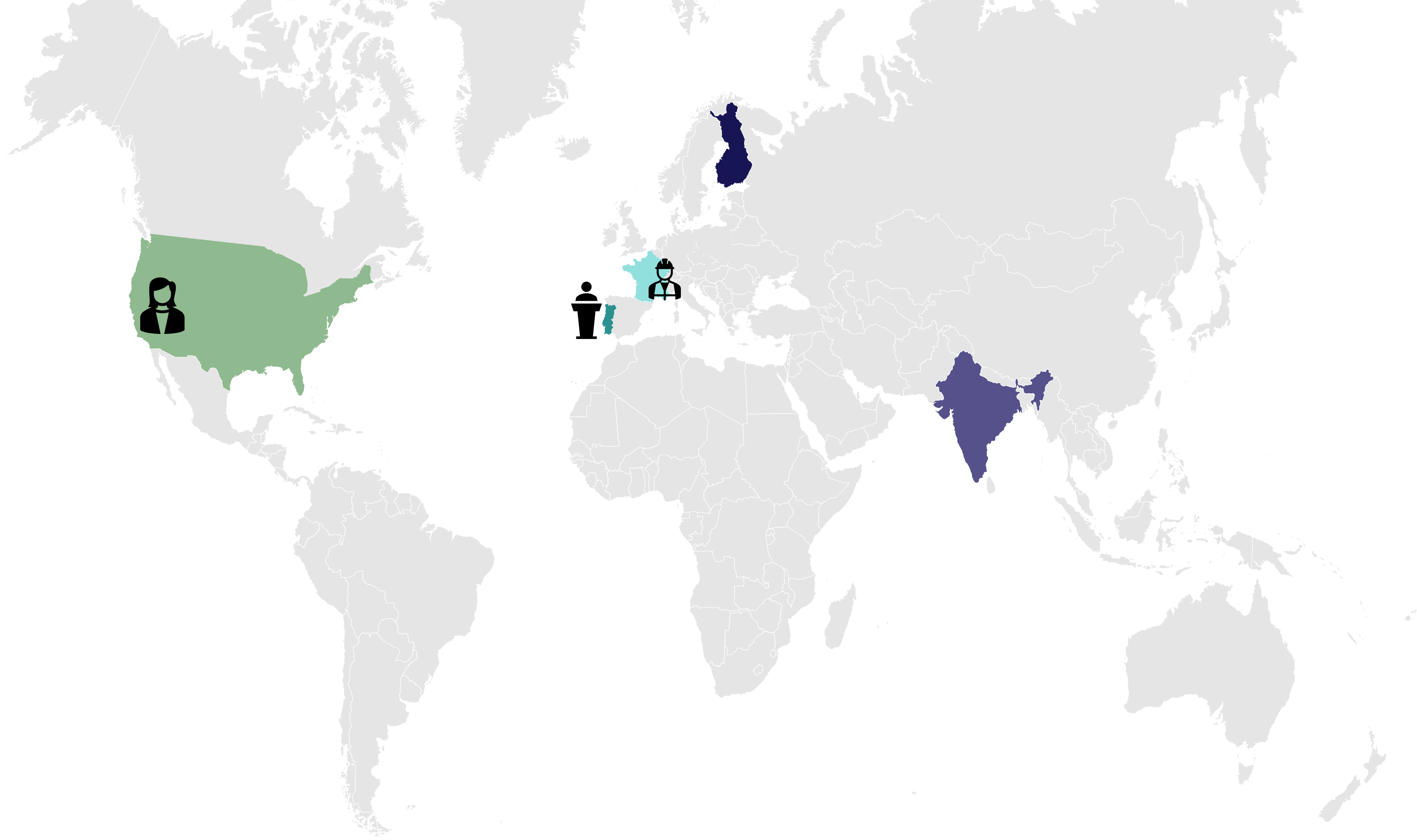
Potential changes in the future

- The PE concept has historically been associated with physical presence in the source state.
  - Thus, PE has usually required that a foreign company has employees, office premises etc. in the source state.
- International tax rules are old and do not reflect the change from industrial production to digitalized economy.
  - Therefore, formation of a PE through digital services is subject to various interpretations.
  - There are both global, EU level and local initiatives to tax digital services. Therefore, taxation of digital services could change in the future.
- The exchange of data between countries has developed a lot during the past years.
- Nowadays, the authorities use technology in inspections, hence the level of control globally is a lot higher than before.

CASE STUDIES

CASE STUDY

Let's put the earlier in practice! You can choose to work in groups or by yourself based on your own preference.



Suomi Oy

USA Ltd.

India Ltd.

Construction site in France

Sales in the USA

CEO in Portugal

Questions

Case studies

Corporate income tax

- How would you analyse the risk of a PE? What needs to be taken into account?
- How high is the risk of a PE? Which facts and circumstances are most critical?
- As a tax consultant, what information would you need to analyse the PE risk?
- If there will be a PE, what kind of compliance obligations needs to be taken into consideration?

Employee & employer obligations

- Which factors would you consider when analyzing to which country employee pays taxes for salary income?
- How about social security status - is there social security coordination between the countries?
- What kind of employer obligations should we consider in such set-up?
- What other important aspects would you clarify as an employee in such cross-border employment scenario?

Case studies

1

Construction site in France

- Suomi Oy has construction project in France;
- The project will last for 15 months;
- Suomi Oy utilizes local subcontractor, but 5 Suomi Oy's employees will work in France during the 15 months;
- In addition, 20 employees from the Indian group company will work in France during the 15 months – they work in France in Suomi Oy's project and their salary is paid by India Ltd.
- Employees from Suomi Oy and the Indian group company will mostly work at the construction site; in addition, they will utilize the subcontractors office premises;
- Each employee from Suomi Oy and the Indian group company will be in France 1-4 months.

Case studies

2

CEO in Portugal

- Suomi Oy's CEO moved to Portugal in December 2021.
- The CEO has an apartment in Helsinki, but the CEO mostly spends time and works in Portugal.
- The CEO is planning to retire during the year 2024.
- CEO's compensation is paid by Suomi Oy.

Case studies

3

Sales in the USA

- Suomi Oy has hired a local sales agent from the USA to perform sales activities on behalf of the Finnish business.
  - The employee in question is a US citizen and lives in California with her family.
  - The employment contract is permanent.
  - Salary is paid by Suomi Oy.

Case studies

4

Relocation from Indian talent pool

- Finance manager from India is permanently relocated to Suomi Oy.
  - Concludes a permanent employment contract with Suomi Oy.
  - Family will move along to Finland.

Case discussion – Construction site in France

Corporate income taxation

Assesing the PE risk

- Both Suomi Oy and India Ltd carry on Suomi Oy's core business activities in France.
- Local subcontractors office premises could be considered as Suomi Oy's and India Ltd's fixed place of business.
- The construction activities last 15 months; based on FIN-FRA DTT construction activities constitute a PE if it last longer than 12 months. Also FRA-IN DTT should be analysed.
- It is very likely that Suomi Oy has PE in France.

Compliance obligations in France:

- Necessary registrations;
- Corporate income tax returns;
- Bookkeeping; financial statements (or P/L)
- Profit allocation to the PE

Compliance obligations in Finland:

- Finland taxes Suomi Oy's all income; also the income that is taxed in France.
- Finland will eliminate double taxation based on the DTT and domestic legislation.
- Corporate income tax rate in France is higher than in Finland; all tax paid in France cannot be credited in Finland.

Don't forget VAT!

Employee obligations

Tax status based on the domestic legislation

- Tax resident in both of the countries, at least if the assignment lasts for over six months.

Country of residence based on the DTT

- If the permanent home (and family) has remained in home country, the assignee will likely be considered as a DTT resident in the home country.

Registration obligations towards tax or other authorities

- Local tax numbers, moving notifications etc.

Taxability of each compensation item and tax rates

- The French regulations should be reviewed, the host country might have some special schemes with lower tax rates for expats.
- Finnish six months' rule might be applicable -> assignment salary tax-exempt in Finland
- In Finland, an employee on temporary assignment abroad, can get as tax-exempt at least accommodation, travels to/from host country and per diems up to certain euro limit.

Tax reporting / tax return filing in both countries

Abolishment of double taxation (DTT)

Employer obligations

Reporting obligations

- Posted Worker notification
- Reporting towards the tax and social security authorities in France and India
- Income's Register reporting in Finland

Registration obligations (to facilitate the reporting)

Tax withholdings and other statutory payments

- Tax withholding obligations most likely in both of the countries – double taxation dilemma to be resolved already in the payroll phase.
- Assuming the Finnish social security coverage applies, no French payments required, but for the Indian employees, the case may be different.

A1 /CoC applications for the assignees

Payroll and salary book-keeping

- Payrolls in Finland & India.
- No actual payroll activities in France, the book-keeping regulations to be reviewed.

Labor law regulations

- The employment contract is assumed to be in accordance with the home country regulations, hence the home country rules apply also during the assignment.
- It must be reviewed, whether the French labor law requires better working conditions or other circumstances than the home country law.

Visa and work authorization (depends on citizenship)

Case discussion – CEO in Portugal

Corporate income taxation

Assesing the PE risk

- Finland and Portugal do not have a DTT in force.
- Portugal is member of the OECD; old DTT between Finland and Portugal was based on OECD Model → might give some hints of the potential tax risk.
- Portugal could claim that Suomi Oy is managed from Portugal. The risk in practice depends on local legislation and tax praxis.
- Is there domestic legislation re effective place of management? If yes, question of tax residency.

Compliance obligations in Portugal:

- If there will be a PE based on local legisltation, Suomi Oy must take care of:
    - Necessary registrations;
    - Corporate income tax returns;
    - Bookkeeping; financial statements (or P/L)
    - Profit allocation to the PE.

Compliance obligations in Finland:

- Finland taxes Suomi Oy's all income; also the income that is taxed in Portugal.
- Finland will eliminate double taxation based on domestic legislation.
- Corporate income tax rate in Portugal is higher than in Finland; all tax paid in France cannot be credited in Finland.

Don't forget VAT!

Employee obligations

Tax status based on the domestic legislation

- Tax resident in both of the countries, unless the person has broken all ties to Finland.

No DTT between the countries

- Domestic regulations of both countries apply without restrictions.

Registration obligations towards tax or other authorities

- Local tax numbers, moving notifications etc.

Taxability of each compensation item and tax rates

- The Portuguese regulations should be reviewed.
- The host country might have some special schemes with lower tax rates for expats.
- If Finnish tax resident, in principle

Tax reporting / tax return filing in both countries.

Abolishment of double taxation – based on domestic regulations in the country of residence.

Employer obligations

Reporting obligations

- Reporting towards the tax and social security authorities in Portugal (?)
- Income's Register reporting in Finland

Registration obligations (to facilitate the reporting)

Tax withholdings and other statutory payments

- Tax withholding obligations depend on the employee's residency status. It must be reviewed, if the CEO can settle the Portuguese tax and other payments independently.
- Finnish social security can be remained in case the set-up is considered as temporary.

A1 application for the CEO

Payroll and salary book-keeping

- Payroll in Finland, payments in practice from the Finnish employer company.
- No actual payroll activities in Portugal, the book-keeping regulations to be reviewed.

Labor law regulations

- The employment contract is assumed to be in accordance with the Finnish regulations, hence the Finnish rules apply also during the assignment.
- It must be reviewed, whether the Portuguese labor law requires better working conditions or other circumstances than the Finnish law.

Visa and work authorization – no actions

Case discussion – Sales in the USA

Corporate income taxation

Assesing the PE risk

- Finland and USA have a DTT in force; interpretation may differ in the USA in practice. .
- They key question is what kind of sales activities the employee performs and for which group entity?
- It should be analysed does the employee have a right to conclude contracts in the name of Suomi Oy or receive orders that are binding → PE
- Or does the sales agent merely collect information or perform market studies → potentially auxiliary or preparatory

Compliance obligations in Portugal:

- If there will be a PE, Suomi Oy must take care of:
  - Necessary registrations;
  - Corporate income tax returns;
  - Bookkeeping; financial statements (or P/L)
  - Profit allocation to the PE.

Compliance obligations in Finland:

- Finland taxes Suomi Oy's all income; also the income that is taxed in the USA.
- Finland will eliminate double taxation based on domestic legislation.
- Corporate income tax rate in the USA is higher than in Finland; all tax paid in the USA cannot be credited in Finland.

Don't forget VAT!

Employee obligations

Tax status based on the domestic legislation

- Tax resident in the USA – employment relationship with Finnish company does not trigger residency.

Country of residence based on the DTT

- If only domestic resident in the USA, also DTT resident in the USA.

Registration obligations towards tax or other authorities

- Most likely none, as US citizen

Taxability of each compensation item and tax rates

- She might have e.g. trainings in Finland, and the salary for those days could be taxable in Finland (tax-at-source).
- Otherwise, US federal and state tax regulations to be followed.

Tax reporting / tax return filing in the USA

Abolishment of double taxation

- Finnish taxes to be claimed back on the US tax return.based on the DTT.

Employer obligations

Reporting obligations

- Reporting towards the tax and social security authorities in the USA.
- Income's Register reporting in Finland.

Registration obligations (to facilitate the reporting)

Tax withholdings and other statutory payments

- Tax and social security withholding obligations in the USA.

Payroll and salary book-keeping

- Payroll in Finland, payments in practice from the Finnish employer company.
- No actual payroll activities in the USA, the book-keeping regulations to be reviewed.

Labor law regulations

- The employment contract is assumed to be in accordance with the Finnish regulations, hence the Finnish rules apply also when working abroad.
- It must be reviewed, whether the US labor law requires better working conditions or other circumstances than the Finnish law.

Visa and work authorization – no actions

Case discussion – Relocation from talent pool in India

Corporate income taxation

Assesing the PE risk

- No PE risk because the employee will be relocated to Suomi Oy and the employee will live in Finland permanently.
- Potential questions:
  - Does the employee travel to India often? If yes, does the employee work remotely from India?

Compliance obligations in Portugal:

- N/A

Compliance obligations in Finland:

- N/A

In this case you don't have to worry about VAT

Employee obligations

Tax status based on the domestic legislation

- Tax resident at least in Finland, domestic Indian rules must be reviewed for breaking the Indian residency.

Country of residence based on the DTT

- Permanent home and family in Finland, hence DTT resident in Finland (most likely).

Registration obligations towards tax or other authorities

- Local tax numbers, moving notifications etc.

Taxability of each compensation item and tax rates

- The general Finnish regulations apply, but special expat tax regime possible for the first four years.

Tax reporting / tax return filing in Finland, potentially also in India

Abolishment of double taxation (if any) based on DTT

Employer obligations

Reporting obligations

- Reporting towards the tax and social security authorities in Finland
- Reporting in India, if the residency is not broken

Registration obligations

- None for Finnish company in Finland
- If employee remains tax resident in India also, the Finnish company may be required to process reporting in India

Tax withholdings and other statutory payments

- Tax & social security withholdings in Finland.
- Withholdings in India possible, if tax residency in India remained.

Payroll and salary book-keeping

- Payroll in Finland, payments in practice from the Finnish employer company.

Labor law regulations

- The employment contract is assumed to be in accordance with the Finnish regulations.

Visa and work authorization in Finland for the employee and his family

Key takeaways

- Global compliance is a very important factor for a successful global business.
- In cross-border situations, the domestic legislation in home and host countries should be reviewed first and then see if the DTT between the countries is limiting the taxation rights.
- The corporate income tax position affects the employer and employee obligations in the working countries.
- The cross-border situations may have real impacts on the employee's life (e.g. pension accrual, cash-flow balance) if the set-up is not planned well.
- Analysing permanent establishment risk requires local interpretation; interpretation might differ in the contracting states.
- Result of the permanent establishment analysis is often strong ”Maybe” rather than clear ”Yes” or ”No”.

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