Income taxation of foreign corporate entities

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Business income and other types of income derived from Finnish sources

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1 Introduction

This is an unofficial translation. The official instruction is drafted in Finnish and Swedish languages.

This guidance discusses the taxation of Finnish-sourced income of foreign corporate entities. The terms 'foreign corporate entity' and 'foreign company' refer to an entity not organised under the laws of Finland, with another state

than Finland as its registered domicile.

All foreign legal persons that are similar to Finnish corporate entities (§ 3, Income Tax Act, tuloverolaki, TVL) are considered 'foreign corporate entities'. For example, any foreign companies that are similar to Finnish limited-liability companies (osakeyhtiö / Oy) such as the Swedish aktiebolag (AB) and the Estonian osaühing (Oü) are included in the scope of the 'foreign corporate entities' concept.

For guidance on VAT, click VAT registration of foreigners in Finland. For guidance on employer obligations, click Obligations of a foreign employer and for guidance on prepayment registration, click Starting up business.

Other guidance is available at prh.fi, the Trade Register, and ytj.fi, Business Information System. The websites have information including administrative requirements on setting up a branch office in Finland. In addition, the Ministry of Employment and the Economy has set up the www.enterprisefinland.fi site offering business services.

2 Taxing rights of Finland

National legal rules governing foreigners' liability to tax are found in § 9, § 10 and § 13a, Income Tax Act (TVL), and in § 83, Act on Assessment Procedure (laki verotusmenettelystä, VML). Foreign corporate entities have a limited liability to tax, and for this reason, they pay income tax on their Finnish-sourced income only. Such income may be received from the operation of a trade or business in this country. If a foreign corporate entity has a permanent establishment in Finland, it must pay tax on all the income that can be attributed to that permanent establishment (PE). Income of a PE may in some cases be sourced in other countries (for more information, see chapter 5 below).

If Finland has no tax treaty with the domicile country of the foreign entity, Finland's taxing rights are determined by national tax rules only, and in these circumstances, the taxing rights are more substantial than if a tax treaty exists between the domicile country and Finland.

Tax treaties may restrict Finland's taxing rights, which are discussed in greater detail in chapter 3 (below) of this guidance.

3 Impact of tax treaties

Finland has signed tax treaties with some 70 countries. The objective of the treaties is to reach mutual agreement between two sovereign countries on how the taxing rights should be shared and divided, and on how international double taxation can be eliminated in situations where a taxpayer (which may be a corporate as well as an individual taxpayer) domiciled in a treaty country receives income from another treaty country. Finland has additionally signed other international treaties, including Tax Information Exchange Agreements (TIEAs).

Tax treaties can restrict Finland's taxing rights, but they cannot amplify them. In this way, when a tax treaty applies, income tax cannot be collected simply by virtue of national tax rules unless it is also accepted under the provisions of the tax treaty.

If Finland has the right to levy tax on income of a foreign corporate entity, Finnish national tax rules determine the computation of taxable income (see chapters 5 and 6 of this guidance). Similarly, national tax rules define the tax rate, unless the provisions of the applicable tax treaty restrict the rate. Moreover, the categorization of various types of income by tax treaty provisions has no direct impact on the Finnish classification of sources of income.

Existing tax treaties are based on the Model Tax Convention of the Organisation for Economic Co-operation and Development, the OECD. Consequently, the OECD Commentary of the Model Tax Convention (Model Tax Convention on Income and on Capital) can be used for purposes of interpretation of the tax treaties. It does not bear importance whether other country of the treaty is an OECD member, because Finland's tax treaties with all countries are generally based on the Model Tax Convention of the OECD (for a court ruling discussing this matter, see case KHO 2011:101 in the archives of Supreme Administrative Court). The Finnish Tax Administration uses the Commentary for purposes of interpretation whenever there is no contradiction with the provisions of the applicable tax treaty. The Commentary is taken into account also in this guidance.

Tax treaties include provisions on the taxation of business income that usually allow Finland to tax the business income of a foreign taxpayer only if it has a permanent establishment in Finland. If there is a permanent establishment, Finland has the right to tax all the income that the permanent establishment generates, including any other income types enumerated in the tax treaty (see chapter 5 below).

However, even if there is no permanent establishment, the applicable treaty provisions, which govern other types of income, may permit Finland to tax the other types of income. For example, royalties from Finland may be within Finland's taxing rights even if the foreign tax payer has no permanent establishment in Finland (see chapter 6 below).

Click here for a list of tax treaties.

4 Permanent establishment for purposes of income tax

4.1. Effects of the existence of a permanent establishment on the application of tax treaties

Under the provisions of national legislation, Finland may collect tax on the income received from the operation of a trade or business in Finland (see chapter 2 above). However, when a tax treaty is applied, Finland may only levy tax on business income if the foreign company has a PE in Finland. In situations requiring interpretation as to whether a PE exists, the definition of a PE found in the applicable tax treaty is significant, instead of what is provided in Finland's national tax rules, which set out a more ample scope of taxing rights.

Article 5 of the Model Tax Treaty of the OECD has been used as a standard that governs the definitions of a PE in the tax treaties Finland has made. Some details may vary in different tax treaties. In Finnish national legislation, the definition of a PE is in § 13 a, Income Tax Act.

There are differences between the income-tax rules and the VAT rules on permanent establishments. As a result, a foreign enterprise may be treated as having a permanent (or fixed) establishment for purposes of VAT but not for purposes of income tax. In certain more rare situations, foreign enterprises may conversely be treated as having a permanent establishment for purposes of income tax but not as having a permanent (or fixed) establishment for purposes of VAT. For more information, click VAT registration of foreigners in Finland.

Because a foreign corporate entity may have more than one business unit in Finland, it may consequently be treated as having more than one PE here. Nevertheless, for purposes of tax assessment, all the PEs are treated as one unit (that is, as the same corporate taxpayer), and the foreign corporate entity concerned may only be issued one single Finnish Business ID code.

4.2. The general rule on the permanent establishment

4.2.1 Existence of a place of business

Article 5, paragraph 1 of the OECD Model Tax Convention contains the general rule (definition) of the 'permanent establishment' term, stating that it means a fixed place of business, through which the business of an enterprise is wholly or partly carried on. A similar provision is in all the tax treaties Finland has made.

Article 5, paragraph 2 of the OECD Model Tax Convention includes a number of examples concerning the general rule. The list is not exhaustive. Accordingly, the term 'permanent establishment' includes especially:

a) a place of management;
b) a branch;
c) an office;
d) a factory;
e) a workshop, and
f) a mine, an oil or gas well, a quarry or any other place for extraction of natural resources.

Any premises, facilities or installations used for carrying on business of an enterprise, whether or not they are used exclusively for that purpose, may be interpreted as the place of business under the above general rule. This means that the place of business does not have to be a definite, limited space, such as a room. It is enough for the purposes of the general rule that the space is at the disposal of the enterprise in fact: it is immaterial whether the premises, facilities or installations are owned or rented by or are otherwise at the disposal of the enterprise. Again, the place of business may be situated in the business facilities of another enterprise, e.g. if there is a certain space at the disposal of the foreign enterprise, used on a regular basis.

To be considered a PE under the above general rule, the place of business must meet the following conditions:

a) it must be established at a distinct geographical place;
b) it must be established with a certain degree of permanence, and
c) the business of the enterprise must be actually carried through the fixed place of business.

See below for a further discussion of the above requirements. The chapter ends with a discussion on a couple of special situations.

4.2.2 Fixed place of business in terms of its location

It is required that the place of business has a fixed location. Thus, there has to be a link between the place of business and a specific geographical point. However, the equipment of the place of business does not have to be attached to the ground. It is enough that the equipment remains on a particular site.

A fixed place of business can be made up by a larger area within which the actual business location varies if the business operations in the area constitute a coherent whole commercially and geographically with respect to the business. Both of the above requirements must be fulfilled simultaneously. A single commercial and geographical unit could be for example an office hotel, a pedestrian street, a mine, an outdoor market or a fair.

4.2.3 Permanency of a place of business in terms of time

There is no provision laying down an exact time limit that would define how long an operation of a trade or business must go on, but it has been provided that a temporary and short-lived setup does not usually constitute a PE. According to tax practice, and the guidance of the OECD Commentary, a business carried on in a country through a place of business that is maintained for less than six months has normally not been considered as having enough permanence in terms of time. Conversely, if the duration has exceeded six months, the business has been usually considered permanent. Temporary interruptions are not taken into account when assessing the permanency of a place of business.

A foreign enterprise may set up a place of business designed to be used for such a short period of time that it would not constitute a PE. However, if it is in fact maintained for such a period that it can no longer be considered a temporary one, it becomes a fixed place of business retrospectively.

Setting up a place of business may involve a period of preparations. The period during which the fixed place of business itself is being set up by the enterprise should not be counted, provided that this activity differs substantially from the activity, which the place of business is to serve permanently.

Operations that last for a shorter period than six months may constitute a PE from their inception under the following circumstances:

a. Business operations that were intended permanent are prematurely liquidated due to special circumstances. For example, in a situation where a foreign enterprise obtains a space to set up a retail store and starts selling goods there, but discontinues the business after two months after making the conclusion that it is a bad investment.

b. The business activities are seasonal and of a recurrent nature. An example of an operation in this category is the recurrent selling of ice cream at an outdoor marketplace in the summer (for a three-month period every summer). For assessing whether a recurrent operation has enough permanence, consideration must be given to the period of time during which the place is used, in combination with the number of times during which it is used (which may extend over a number of years).

c. The foreign enterprise operates a certain business exclusively in Finland. In these circumstances, the business has a stronger connection with Finland than with the country where the foreign company is domiciled.

4.2.4 Carrying on activities through a place of business

A place of business will only constitute a permanent establishment if the enterprise, wholly or partially, conducts business through it. This normally means that the foreign enterprise has personnel there who work for it. The personnel do not necessarily have to be employees of the foreign enterprise: it is sufficient if they are under its authority (e.g. they may be leased employees whose actual employer is another enterprise). The personnel may also conduct the business activities through the place of business; i.e. they do not have to work entirely at the place of business.

A permanent establishment may exist even if business is carried on mainly through an automatic equipment or facility, regardless of whether the foreign company itself has arranged for its technical maintenance and supervision, or whether there is an external service provider taking care of it. For example, a PE is made up of a transformer station connected to an electric power line although its technical maintenance is carried out by an outside service provider (for more information, see ruling KVL 52/2007 of the Central Tax Board).

The business of employee leasing or leasing of equipment does not give rise to a PE in Finland if the leasing business is conducted through a location in another country (for more information, see ruling KHO 1986/1679 II 501 of the Supreme Administrative Court). For guidance on the distinction between employee leasing and subcontracting, click Leased employees - taxation in Finland.

4.2.5 Special situations concerning the general rule of permanent establishment

Home office

If an employee or director of an enterprise works from a home office, a PE may be constituted at the home office. This requires that the employee or director has a space at home through which they work on a permanent basis.

Working from home non-recurrently or randomly is not considered permanent. Similarly, it does not constitute a PE if the work done through the home office is of auxiliary or preparatory nature (see chapter 4.4 below).

A PE might be constituted at an employee's home for example in a situation where a foreign enterprise has not provided the employee an office space, although it is a requirement for his work, and if the enterprise assumes the employee works through his home in Finland.

Place of management

A place of management could constitute a PE under the general rule according to the OECD Model Tax Convention (art. 5.2 cited above). Consequently, it is required that a place of management has sufficient permanence in terms of time in a fixed location. According to tax-assessment practice, a place of management can be located, for example, inside the premises of another enterprise (e.g. ruling KHO 1999/1031 of the Supreme Administrative Court) or at the home of a company director. A place of management is a place where decisions concerning the entire company or parts of it are made. These management decisions must be business-oriented, active and independent.

The assessment whether decision-making falls into category of management or not is based on case by case analysis in which weighting should be given among other pertinent circumstances to the size of the enterprise and the nature of its business. If a certain location is customarily the place where the annual general meetings or board meetings of an enterprise are held, it does not, by itself, necessarily mean that it is a place of management.

Corporate entities may have more than one place of management (in different countries). However, they can only have one 'place of effective management' (Art. 4 of the OECD Model). Nevertheless, other places of management than the 'place of effective management' may amount to a PE. The country of the place of effective management is where a corporate entity is deemed as a resident in a double-residency situation. Such a situation comes up when there are two countries that both consider a certain corporate entity to have full tax liability in their country. Under Finnish national law, foreign corporate entities cannot be fully tax-liable in Finland. For this reason, situations of double-residency do not normally arise for foreign corporate entities operating in Finland. However, in countries including the United Kingdom, Norway and Denmark, a Finnish company may be treated as a resident of the country if its 'place of effective management' is located there (see ruling KHO:2003:33 of Supreme Administrative Court).

4.3. Construction and installation projects

4.3.1 Permanent establishment based on the duration of a project

A building site or a construction or installation project constitutes a permanent establishment only if it lasts longer than what the applicable tax treaty has defined as the time limit. In the Model Tax Convention, this time limit has been set at 12 months. In the Model and in the majority of Finland's tax treaties as well, the relevant provisions are found in Article 5, paragraph 3. This paragraph also defines the types of activities on which the time limit should be applied. The definition of the activities and the time limit deviates in a number of treaties from the Model Tax Convention (see chapter 4.3.2 below). For example, under the treaty between Estonia and Finland, a project site that lasts longer than 6 months constitutes a PE.

A site usually exists from the date when the contractor begins his work, including any preparatory work, in the country where the construction is to be established. In general, a site continues to exist until the work is completed or permanently abandoned. A site should not be regarded as ceasing to exist when work is temporarily discontinued. Temporary interruptions may be seasonal, due to weather conditions, or due to other reasons such as lack of materials or problems with the availability of workforce. Similarly, the duration of a site normally includes its finishing works after final inspection. However, if additional work is done due to a warranty clause (such as a guarantee repair job) the required time for warranty works is not included in the total duration of original site.

If a foreign company has several projects in Finland, each one of them should be treated separately from the perspective of the time limit. However, if various projects form a coherent whole commercially and geographically, the projects could be considered as a single unit and the durations could be summed together. Similarly, if a certain project is artificially divided up into several parts, the projects could be considered as a single unit.

A single construction or installation site may form a coherent whole commercially and geographically even if the orders have been placed by several persons (e.g. when the worksite is located in the same place or when buildings are constructed next to each other). Tax assessment practice has adopted the view that a coherent whole commercially and geographically may be formed, for example, when projects that are close to one another geographically are done for same client. However, no such coherent whole commercially and geographically exists in a case where it is evident that the projects in question have nothing to do with one another. A longer interruption between projects at the same location could be an example of such a situation. Similarly, a coherent whole commercially and geographically does

not exist if projects based on separate contracts have no commercial link between them. A case by case analysis is required to assess whether a coherent whole commercially and geographically could be formed.

When considering the total duration of a main contractor's activity on a site, the period spent by subcontractors must be included in it. If the main contractor is responsible for the completion of the project to the buyer, the main contractor might have a PE in Finland even if a subcontractor wholly or partially does the work at the project site. As far as the subcontractor is concerned, a PE is constituted if its activities last more than required time limit, or if the business activity otherwise constitutes a PE.

4.3.2 Operations covered by the tax treaty paragraph on construction, building and installation

The tax treaty paragraph on construction, building and installation also covers demolition, renovation and repair of buildings, the laying of pipelines, and earthworks, excavation and dredging. However, excluded from the treaty paragraph are contracts that merely involve maintenance work or redecoration, such as painting or wallpapering. Nevertheless, painting and other finishing of surfaces may be treated as construction or installation work if they are part of the finishing of a project at a new construction site.

Provisions of a number of Finland's treaties lay down that supervision and assembly work must be governed by the treaty paragraph on construction, building and installation. In other words, special provisions apply to such work.

Any preparatory work of a construction or installation project in Finland is normally considered part of the project. Preparatory work may involve planning, design, supervision and consultations in Finland. Planning or supervision activity may in itself give rise to a PE by virtue of the treaty paragraph on construction, building and installation, even if they are carried out by another enterprise than the contractor who is responsible for the construction or installation. This interpretation is applied to situations in which the tax treaty between Finland and the domicile country of the contractor company has been signed after the Commentary version for 2003 was published (i.e. after 28 January 2003). When the applicable treaty is older, planning or supervision activity are normally not considered to amount to a PE due to the above-mentioned treaty paragraph if the activity is carried out by other enterprise than a contractor that is responsible for construction or installation. The latter interpretation is in line with the pre-2003 OECD Commentary. However, even in such cases, there is the possibility that the contractor must be treated as having a PE because of the general rule, or because of a dependent agent.

4.3.3 Permanent establishments by the general rule or by a dependent agent in construction, building and installation

Foreign companies engaged in construction, building or installation may have a PE in Finland because of the general rule (as noted above in 4.2). This requires that the conditions of the general rule are fulfilled. For example, there may be a place of business being used as the place of management for many building sites or construction projects. However, an office that has been set up at a building site does not amount to a PE under the general rule if it only serves that one site. Instead, the paragraph of the tax treaty on construction, building and installation must be applied to the case.

PEs in construction, building and installation industries may additionally arise because of the presence of a dependent agent (see 4.5 below).

4.4. Negative list (activities of preparatory or auxiliary character)

Article 5, paragraph 4 of the OECD Model Tax Convention enumerates some activities that may be regarded as preparatory or auxiliary. Such activities do not normally constitute a PE even if the other conditions were met. Tax treaties between Finland and other countries contain a similar list.

For example, advertising, collection of information, supply of information or scientific research may fall within activities of preparatory or auxiliary character. Similarly, the maintenance of a stock of goods or merchandise belonging to the enterprise for the purpose of storage, display or delivery may be a preparatory or auxiliary activity that does not constitute a PE. However, a case by case analysis based on business circumstances must be made in order to judge whether the activities are of preparatory or auxiliary character.

Activities cannot be considered preparatory or auxiliary if they make up an essential part of the business of the foreign company, or if they make up a business unit of their own. This restriction also concerns the activities enumerated above, such as advertising. For this reason, the following activities normally cannot be considered preparatory or auxiliary:

a. performance of functions closely related to the main business of the foreign enterprise (e.g. scientific research in circumstances where the patents resulting from it have a significant role in the business);

b. active participation in sales efforts (for more information, see court rulings including KHO 1991/4893 ja KVL 1997/206);

c. management functions;

d. after-sales operations including repair and maintenance of sold merchandise;

e. customization of goods and services for the special needs of certain clients; and

f. offering goods or services in the interest of other parties than the head office of the foreign enterprise itself (e.g. advertising the products of another company of the group).

4.5. Dependent agent permanent establishments

The existence of an agent or a representative may constitute a PE for a foreign enterprise even if the enterprise or its representative has no fixed place of business in Finland. The majority of 'dependent agent PEs' involve selling (in Finland) of goods or services of a foreign principal enterprise.

A dependent agent may cause a foreign principal enterprise to have a PE if the agent regularly enters into contracts for its principal. This does not necessarily mean that such a representative has the formal right to sign contracts for the principal. As an example, it is sufficient that the agent receives orders and forwards them to the foreign enterprise being the principal if the latter routinely accepts the orders.

A dependent agent may be an individual as well as a corporate entity. However, it does not amount to a PE if the agent's work is of auxiliary or preparatory nature (see 4.4 above).

Moreover, it does not amount to a PE if the foreign enterprise operates its business through a broker, a general commission agent or any other agent who is independent. An independent agent is financially and legally independent from its foreign principal. An independent agent typically acts in the ordinary course of its business (the agent is responsible to its principal for the results of its work, but the principal does not control how the work is carried out) and carries the risks that relate to its business.

4.6 Operation of ships and aircraft in international traffic

The majority of Finland's tax treaties contain a special provision on the category of income that has been received through the operation of ships or aircraft in international traffic. This special provision lays down that the only country that can levy tax on such income is the country where the 'place of effective management' of the company is located. In the OECD Model Tax Convention and in the majority of Finland's treaties, the relevant provisions are found in article 8. The article concerns the income that is sourced directly from the transportation of passengers or cargo by ships or aircraft, and additionally the income from the operations that support them and are associated with them. In these situations, the income of a PE is usually outside the taxing rights of Finland even if there was, for example, a sales office of a foreign airline located permanently in this country. Instead, the taxing rights of Finland may concern other Finnish-sourced income of a foreign airline company, including income derived from immoveable property.

Moreover, the fact that, for example, an airline company has a PE in Finland may be significant from the perspective of employer obligations and the taxation of PE's employees. For more information on employer obligations click Obligations of a foreign employer. More information also Operation of ships and aircraft in international traffic.

5 Income attributable to the Permanent Establishment

5.1. Obligation to give declarations and arrange audit

A foreign corporate entity is obliged to give declarations and documentations of its business operations in Finland corresponding to Finnish Tax Administration's Official Decision (Verohallinnon päätös ilmoittamisvelvollisuudesta ja muistiinpanoista A123/200/2016, 23§)

Statutory audit in Finland of a Finnish PE must be arranged, if the foreign corporate entity's annual accounts are not being compiled, audited and made public in the manner corresponding to the current EU rules (§ 1:1, Auditing Act, tilintarkastuslaki). In practice, the obligation to arrange audit in Finland mostly concerns the PEs of foreign non-EU and non-EEA corporate entities, because the accounting laws applicable to them do not correspond to the current EU rules. In addition, special rules apply to the audit arrangements of the Finnish branches of foreign credit institutions, financial institutions and insurance companies.

5.2. The arm's length principle in income taxation

When a PE exists, Finnish tax authorities have the right to impose income tax on its income. The guideline known as the 'arm's length principle' is applied in determining the income attributable to the PE. Thus, what must be attributed to the PE are the income and costs that would have accrued to it if it were an independent company, operating a similar trade or business in similar circumstances. The Finnish Tax Administration interprets the arm's length

principle according to the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations, 2010 (see ruling KHO:2013:36 of Supreme Administrative Court). However, it must be noted that such interpretation has to take the specific characteristics of PEs into account because they are not directly comparable with separate corporate entities.

A PE may have dealings with other parts of the same corporate entity (e.g. with the head office or a PE in another country). The arm's length principle is normally applicable to these dealings as well (for exceptions, see 5.3 below). The taxable income of a PE might be adjusted if it is not arm's length, and consequently, the taxable profits of the PE are smaller, or the tax-deductible losses greater, than they would have been. The 'transfer pricing adjustments' are based on § 31, Act on Assessment Procedure and the tax treaty provisions governing the definition of business income (Article 7, OECD Model Tax Convention). As a result, the taxable income will be readjusted to an arm's length amount, i.e. the amount of profit or loss that the PE would have made if the conditions had been similar to those between independent enterprises.

5.3. Taxable income and deductible costs of a permanent establishment

The taxable income of a PE is calculated in a similar manner as in the case of Finnish corporate entities, such as Finnish limited-liability companies (Oy). The applicable law is Business Tax Act (EVL, 360/1968).

As a result, the income generated by a PE is taxable as defined in the Business Tax Act. All the income generated by a PE is attributed to it, including its dividends, interests, royalties and capital gains for sales of assets. On the other hand, the business costs related to income generated by a PE are deductible. Provisions on deductibility are found in the Business Tax Act. Examples of deductible expenses include the payroll costs of a PE. The expenses of a PE remain deductible regardless of whether they have arisen in Finland or in other countries.

However, no tax deduction is usually granted for interest or royalties paid out by the PE within the corporate entity itself (for example, in connection with the PE's dealings with the head office), because they are not regarded as amounts actually paid to a separate corporate entity. For example, if a foreign Company X has a PE in Finland, the PE cannot make deductible interest payments to Company X in its country of domicile, because both the payer and the beneficiary of the interest are parts of the same legal person. An exception from this rule could be made for example with the PEs of financial institutions.

5.4. Income derived from partnership or consortium

The Supreme Administrative Court has held (KHO 2002:34) that the business of an entire partnership should be the basis for determining the category of income accruing to a partner of the partnership. Accordingly, if a foreign nonresident is, for example, a partner in a Finnish limited partnership that operates a business in Finland, any portion of its income should be treated as taxable business income in the hands of the nonresident partner.

The portion of income of a foreign company from a Finnish partnership/consortium must be declared in an income tax return in the same way as any other taxable income. However, the company may leave such income out of its tax return if the taxable amount is not known at the time when it files the return. Any expenses related to the portion of income from partnerships can be deducted on the tax return, as laid down in the provisions of Finnish tax legislation (Income Tax Act or Business Tax Act, depending on the source of income in Finnish tax law).

If there is a Finnish limited partnership that only operates in the venture-capital investment business, and a foreign company is its silent (limited) partner, income derived from this partnership is only taxable to the extent that equals the proportion that would be taxable if the partnership's income from Finland was directly the income of the partner. The precondition for this special tax treatment is that the nonresident partner's country of residence has a tax treaty with Finland (§ 9.5, Income Tax Act).

5.5. Business losses attributable to a permanent establishment

If the business operations of a PE result in losses, they will be deductible during the ten subsequent tax years, with the same loss carryforward rules as are in effect for Finnish corporate entities. This means that the rules governing the tax treatment of losses, set out in Income Tax Act, are equally applicable to PEs.

Correspondingly, if more than half of a foreign company's stock has changed hands, the company's right to the carryforward of PE losses is cancelled, unless a special permission is granted. Rules on the deductibility of previous losses after changes in ownership are found in § 122, Income Tax Act. However, publicly listed companies are entitled to deduct allowable losses without the special permission after changes of ownership, on the condition that more than half of the company's shares, which are not traded publicly (if the company has this kind of shares), have not changed hands as described

above (§ 122, Income Tax Act).

5.6 Closing down a permanent establishment

A foreign company may close down the PE located in Finland, and its assets may be sold, or transferred back to the country of residence. The closure operations of the PE's business have an impact on the taxation of the last tax year of the PE.

If a PE is terminated by selling its assets to an outside buyer, the selling price of the assets must be added to the income of the PE for the last tax year. Undepreciated acquisition costs (in tax accounting) of the assets may be deducted from the selling price. If the assets of the PE are transferred away from Finland, or if they otherwise cease to be connected with the PE, their arm's length value must be added to the income of the PE. This procedure is no different from the domestic procedure in conjunction with the liquidation of a domestic corporate entity. Additionally, if the PE had any reserves in the balance sheet, closing it down will mean that the reserve amounts may be added to the income of the PE for the last tax year (§ 51 e, Business Tax Act).

As an alternative, the PE can be converted into an independent limited-liability company under the provisions of § 52 d-e, Business Tax Act. Such conversion is based on the principle of continuity, and it is not treated as a liquidation. This procedure can only be implemented in situations where the foreign company is a resident of another EEA (European Economic Area) country. They are the countries of the European Union plus Iceland, Liechtenstein and Norway. The provisions of § 52 d-e, Business Tax Act are also applicable to such conversions when the foreign company is a resident of a country that has a tax treaty with Finland with a clause that prevents discriminatory tax treatment of a permanent establishment (see ruling KHO:2013:169 of the Supreme Administrative Court. Anti-discrimination clauses are normally found in article 24). When a PE of a foreign company is converted into an independent limited-liability company, any approved allowable losses are transferred to the new company under the conditions laid down in the provisions of § 123 a, Income Tax Act, if the foreign company is a resident of an EU country (see ruling KHO:2013:169 of the Supreme Administrative Court, in which the allowable losses were not transferred).

6 Income tax treatment if no permanent establishment is in existence

6.1. Categories of income

This chapter discusses the types of income that occur most frequently in foreign-held entities, and which are within Finland's taxing rights although the foreign company does not have a permanent establishment in Finland. However, for guidance regarding income derived from partnerships, see 5.4 in the previous chapter.

6.2. Income derived from immoveable property and residential units

National tax rules provide that Finland has the taxing rights on income derived from real property and housing-company flats and apartments if they are located in Finnish territory. By extension, income types including capital gains and rental income are taxable, even if the foreign entity has no PE in Finland (§ 10, Income Tax Act). The existing tax treaties usually impose no restrictions of Finland's taxing rights in this regard, because tax-treaty provisions are generally based on the idea that income from real property should be taxable in the country of its location.

Under Finnish law, shares in a Finnish housing company are not considered real property. However, most of Finland's tax treaties allow Finland to tax income derived from housing-company shares, if the apartments (that the shares give right to) are located in Finland. Nevertheless, for example, the tax treaty with Spain limits Finland's taxing rights on income from housing-company shares. Consequently, Finland cannot impose taxes on rental income from housing-company shares in the hands of a Spanish resident, even if the rented flat or apartment is located in Finland.

Finnish national tax rules are decisive when the source of income is determined, if income is derived from real property or units of a housing company. If a foreign entity has this type of income, it is expected to report it on the tax return, without any prompting on the tax authorities' part. Matters associated with assessment procedures and the dealing with any non-compliant behaviour are subject to the same rules as where the foreign entity has a PE (for more information, see chapter 7).

6.3 Dividends, interest and royalties

For comprehensive guidance on this income category, click Payments of dividends, interest and royalties to nonresidents.

The payers of these kinds of income are expected to collect tax at source, at rates defined in the Finnish national legislation or in tax treaties. If the income consisting of dividends, interest and royalties is attributable to a PE of a foreign corporate enterprise, Finland collects tax on it as part of the PE

foreign corporate enterprise, Finland collects tax on it as part of the PE income, and the PE must report it when filing its tax return (see 5.3 above and 7.1 below).

Receipts of interest in Finland are not taxable income to a foreign entity if the interest is paid for a balance of commercial accounts receivable / accounts payable, or it is a bank deposit, a government bond, debenture, other similar instrument or a loan from a foreign country to the Finnish operation. Payments for equity and share capital are not considered interest. Furthermore, to be exempt from income tax, receipts of interest should not be attributable to the business of a PE (§ 9.2, Income Tax Act).

6.4 Securities trading and sales of other moveable property

Investing in Finnish securities and other moveable property and trading them through a place located in a foreign country does not give rise to a PE in Finland for a foreign enterprise. Therefore, the resulting income will not be taxed in Finland as business income. However, the income may be within Finland's taxing rights, by virtue of national tax rules that concern other than PE income and by virtue of the applicable tax treaty provisions that govern other types of income (see 6.3 above). Moreover, the income may be within Finland's taxing rights in a situation where a foreign nonresident receives Finnish-sourced income from a partnership (see 5.4 above).

Capital gains received from sales of securities or moveable property are usually not taxable in Finland. However, unless the relevant tax treaty prevents Finland from taxing the income, if one or several Finnish-located real property units make up more than 50 percent of the assets of a housing company, any other joint-stock company, or cooperative society, the capital gains will be taxable if a sale of shares in such an entity, or a sale of real property has resulted in a profit (§ 10, subparagraph 10, Income Tax Act).

7 Assessment procedure, tax control, and consequences of taxpayer's non-compliance

7.1. Income tax returns

Foreign corporate entities receiving income from Finnish sources must file a tax return on their initiative, without prompting, whenever they receive income that is taxable in Finland and taxation has not been assessed at source. Foreign corporate entities must additionally provide more information if the authorities should ask them to do so, in order to facilitate statutory tax assessment or later adjustments to it (§ 11, Act on Assessment Procedure.

Both the taxpayer and the Tax Administration are legally required to participate in the efforts that must be made for clearing up any tax matters. The party that has better opportunities to obtain information should provide it (§ 26.4, Act on Assessment Procedure). Taxation must be carried out using the facts that are at the disposal of the tax authority, received from the taxpayer and third-party sources (§ 26.5, Act on Assessment Procedure).

If a PE in Finland exists, the foreign entity must file a tax return every year in order to report the revenues, expenses, assets and liabilities of the PE. The foreign entity must pay income tax at the normal corporate tax rate (which is 20% from 2014). Computations of taxable income are made using the facts reported on tax returns.

Foreign and domestic corporate entities alike have the same deadlines for filing tax return. The deadline is four months after the end of the month when the financial year closes. The foreign entity's financial year determines that of the PE for tax purposes. It is important to specify the financial year (also known as 'accounting period' and 'accounting year') for the Tax Administration when the foreign enterprise is registered in Finland. If the end date should change, the company must notify the Tax Administration.

A foreign enterprise must deliver the return to the Tax Administration. If necessary, it may deliver the return to a diplomatic representation of Finland, which will then immediately forward it to the Tax Administration.

Foreign and domestic corporate entities alike fill out the same income tax return forms published by the Tax Administration. The applicable form is 6B Tax return of business activities / Corporation. Its mandatory enclosure is form 62 Itemization of reserves, revaluations and depreciation on which depreciation must be reported. Almost all return forms are available in English (besides the official languages Finnish and Swedish). They are available at tax offices and may be downloaded freely at tax.fi (this site). For more information, click Income tax returns from foreign companies.

PEs of foreign enterprises are expected to enclose a profit and loss account and balance sheet with their tax return. Assets and liabilities are also to be reported. If submitted documents are in a foreign language, a Finnish or Swedish translation is usually necessary. The translation should be made by an authorised translator or other qualified translator. The tax authorities have a right to request a translation if necessary.

E-filing services can be used to submit a tax return. For more information on online services, click e-Filing.

If the tax return is filed in paper form, it should be authorized with the

signature of a person who has the right to sign the company name. It should also show the name, address and details of the fiscal representative/contact person in Finland.

7.2. Tax control and consequences of taxpayer's non-compliance

Foreign and domestic corporate entities alike are subject to tax control, constantly exercised by the Finnish Tax Administration. Control consists of assessment procedure, tax audits, taxpayer guidance and monitoring of tax payments. Similarly, the ongoing exchange of information between Finnish and foreign tax authorities is a part of tax control. It is based on international conventions and mutual cooperation with the authorities.

The tax authorities may impose a punitive tax increase if a taxpayer fails to fulfil his obligations. The tax increase is imposed according to these instructions (only available in Finnish and Swedish) and § 32, Act on Assessment Procedure.

Taxable income of a foreign corporate entity may be estimated if it has a PE in Finland and it fails to file a tax return, or files an incorrect tax return that cannot be used in tax assessment, even if corrections were made. If tax assessment is based on an estimate, an additional punitive tax increase will be imposed. Separate legal rules of the Penal Code on tax crimes may be applied if negligence is considered deliberate.

8 Elimination of double taxation

When a foreign corporate entity generates income in Finland it may be subject to taxation not only in Finland but also in its country of domicile and registration. Double taxation is usually eliminated in the domicile country (country of residence). This is done according to the provisions of the applicable tax treaty and according to the national tax rules of the country of residence. For this reason, to gain more information on the elimination of double taxation, foreign taxpayers should consult their country of residence. The country can either credit the Finnish tax or treat the Finnish-sourced income as tax-exempt.

9 Tax liability of a company representative

9.1. Representative entered in Trade Register

The obligation of foreign corporate entities to appoint a representative is laid down in the provisions of Act on the Right to Carry on a Trade (elinkeinolaki). The Trade Register requires that a start-up form should be submitted if a foreign entity opens a Finnish branch office (sivuliike) or other comparable place of business. The branch must have a representative with the right to receive official communications, including subpoenas, on behalf of the foreign entity. The representative's name and contact information are entered in the Trade Register.

The appointed representative may be domiciled in an EEA country if a foreign corporate entity or a foundation has been organized under the laws of an EEA country, and it has its headquarters, tax domicile or head office in an EEA country. However, if the above requirements are not met, the appointed representative should be domiciled in Finland.

For more information on how to appoint a representative, go to the Trade Register website prh.fi or to the Business Information System website ytj.fi.

9.2. Representative's responsibility for tax payments

Pursuant to § 52, Act on Assessment Procedure, the representative of a foreign entity may be liable for income taxes of the entity. This liability concerns taxes that are levied on natural and legal persons resident outside the EEA. Consequently, a representative is not liable for taxes levied on corporate entities that are residents of an EEA country.

A representative entered in the Trade Register is liable for tax levied on a branch of a foreign corporate entity, if the entity is resident in a non-EEA country. If a non-EEA resident credit institution has a branch office in Finland, the director of the branch is liable for the tax levied on the credit institution.

9.3. Limitations of the representative's tax liability

The representative's tax liability only concerns an appointed representative whose name is entered in Trade Register records. Consequently, such a representative will carry no liability for taxes that have been levied when the representative did not act as the representative of the entity in question (see ruling KHO 2006:57).

Your comments on this page

Glossary

Go to Glossary to look up important tax concepts and terminology.

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- Registration checks ›
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