Tax news
PwC Finland

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# *Corporate Income Tax*

## FINLAND

### A holding company belonging to an equity investor group was not considered as an equity investor

**Decision 14/1367/3 of the Administrative Court of Helsinki, 19.9.2014**

A Oy, a company with limited liability belonging to an investment portfolio managed by B Oy and its investment funds, was established for the purpose of acquisition of C Oy's shares. A Oy didn't have active business activities and received significant part of its income as group contributions from its subsidiary C Oy.

C Oy was contemplated to be dissolved. The Administrative Court of Helsinki decided that the loss occurred from the dissolution of C Oy is not tax deductible to A Oy. The conclusion was based on the fact that A Oy's business couldn't be considered as acting in the field of equity investing. A Oy was merely considered as an asset of its main owner B Oy.

### The cross border merger of a Finnish investment fund was considered tax neutral from investor´s perspective

**Decision of Supreme Administrative Court 2014:138**

An individual A was intending to acquire a fund unit in a Finnish investment fund X. X was contemplating a cross border merger to a Luxembourgian SIVAC, collective investment undertaking. According to the Supreme Administrative Court the merger was considered to be in compliance with the Business Income Tax Act 52 a—b §. Based on the principles determined in those articles, the merger was considered tax neutral in the taxation of A. The decision was affected by principles in the European Union tax law.

### Decision regarding a tax misdemeanor by Itäsuomi Court of Appeal dated 16.9.2014

The responsible person in Company X was charged and convicted of tax misdemeanor as prescribed in the Criminal Code 29th Chapter 4 § and thus received a pecuniary penalty of 50 day fines. The Court of Appeal found that the company's failure to pay taxes and fees was not caused by insolvency and that the responsible person had acted with the intention of obtaining benefit.

The Company had allocated payments to purposes that were important for the continuity of the company's operations to the detriment of the tax recipient. The company's dereliction of taxes and fees had been constant and on-going. As a result, the company's tax debt grew remarkably in relation to the company's other debts and left the tax recipient in a clearly unequal position.

The Court of Appeal stated that according to established case law, the tax payer cannot be considered insolvent in circumstances it fails to pay taxes and fees but concurrently continues its operations and pays the claims of other debtors and thus enables the continuity of the company's operations by neglecting to pay taxes and fees. The responsible person had thus clearly acted with the intention of obtaining benefit and the failure to pay taxes and fees could not be considered to result from insolvency.

### Tax Administration no longer sends pre-completed 6B form to limited companies

The pre-completed 6B tax return form will no longer be sent to Finnish limited companies. In November, companies will receive only a handout and short filling instructions related to tax return. The tax administration still sends pre-completed 6B form to ordinary real estate companies, pension funds, foreign corporations and foreign branches.

## SWITZERLAND

### Federal Council to avoid double taxation of permanent establishments

The Swiss Federal Council initiates consultation on a planned ordinance which would avoid the system-related double taxation of permanent establishments (PEs) of non-resident companies. PEs of non-resident companies receiving dividend, interest or royalty payments from third states may in certain cases be taxed both in the source state and in Switzerland, in case the income is attributed to the PE. The Federal Council thus plans granting a lump sum credit to PEs in order to avoid over-taxation.

### Federal Council initiates consultation on Corporate Tax Reform III

The Federal Council of Switzerland has launched consultation on the third Corporate Tax Reform to renew taxation procedures especially on cantonal level. The reason for the reform is to respond to the international pressure on the preferential cantonal tax treatments, on the other hand to maintain Switzerland's fiscal attractiveness. The reform would abolish preferential tax regimes for holding and domiciliary companies and replace them with new internationally accepted tax provisions. The new tax regimes would however come into effect in 2018 at the earliest, thus the current tax treatments should remain valid for the present.

## UNITED STATES

### Internal Revenue Services published FAQs on FATCA

The Internal Revenue Services of United States (IRS) has released several information packages on the Foreign Account Tax Compliance Act (FATCA) project. Frequently asked questions have been updated to the website of IRS regarding, inter alia, FATCA registration, IDES information exchange system and general features of FATCA.

FATCA is an American legislation amendment which aims at preventing American investors from tax evasion with the help of automatic exchange of information. The Finnish Tax Administration will start the exchange of tax data in 2015 concerning certain information from 2014.

## CHINA

### Examination on dividends paid to non-residents

The State Administration of Taxation in China has published a guideline requiring tax bureaus to examine dividend payment made to non-residents in 2012 and 2013. The special tax examination is conducted in order to detect possible tax avoidance situations.

**For further information, please contact**

Eija Kuivisto, eija.kuivisto@fi.pwc.com, tel. +358 (0)20 787 7876

## OECD published the first recommendations of BEPS Action Plan

**OECD BEPS 2014 Deliverables, 16 September 2014**

OECD has published reports on the BEPS items dealing with the first seven of the total 15 actions that together form the Base Erosion and Profit Shifting ("BEPS") Action Plan. BEPS refers to situations where differences in national tax laws leave gaps which can be further exploited by transferring activities abroad to jurisdictions with low or no taxation. The BEPS project aims to the development of domestic and international instruments to address this issue.

In this issue, we summarize the first seven actions and the related deliverables published on 16 September 2014. The remaining eight actions and the related deliverables are scheduled to be finalized in September and December of 2015.

The BEPS 2014 deliverables

### Tax Challenges of the Digital Economy

The report on the Tax Challenges of the Digital Economy states that the digital economy is so widespread that is does not represent a certain part of the economy but the economy itself. Thus, it is not possible to create and implement separate tax rules for the digital economy.

In general, the report identifies issues that the technological development and new innovations may bring up but states no recommendations regarding tax treaties or national tax law changes.

However, BEPS risks that arise from the business models typical to the digital economy will be addressed in other action reports of the BEPS project. The report states the need for reviewing the CFC rules, PE article and transfer pricing policies which all often deal with the digital economy.

### Hybrid Mismatch Arrangements

A Hybrid Mismatch Arrangement is an arrangement that exploits different tax treatment in two jurisdictions. The resulting mismatch in tax outcomes often means multiple deductions for a single expense or a deduction in one jurisdiction without corresponding taxation in another jurisdiction. In order to address the issue and neutralize the effect of hybrid instruments and entities, OECD proposes recommendations for domestic tax law changes and changes to the model tax treaty provisions.

Besides general recommendations for domestic law changes, the report presents hybrid mismatch rules that aim to harmonize the tax outcome between two jurisdictions. To avoid both double taxation and double non-taxation, the recommended hybrid mismatch rules are divided into a primary response and a defensive rule; the latter only applies in cases where the primary rules are not applied in the other jurisdiction.

The proposed changes in the model convention complement the abovementioned recommendations regarding the domestic tax laws. The changes cover e.g. situations where dual-resident entities would obtain improper treaty benefits.

The timing regarding the implementation of the rules will be decided  presumably only after a revised model tax treaty commentary has been introduced, foreseen in September 2015.

## Treaty Abuse

The report on treaty abuse calls for a clear statement that treaties are no designed to allow double non-taxation or reduce taxation through tax avoidance and treaty shopping. This statement is expected to guide the interpretation of tax treaties in legal proceedings.

Furthermore, the report presents anti-abuse rules in order to prevent treaty shopping. With these proposals, member states are expected to adopt “a minimum level of protection”. One solution would be to adopt a general treaty anti-abuse rule aimed for arrangements, such as letterbox entities, that principally pursue to obtain treaty benefits. This rather subjective rule is referred also as the Principal Purpose Test.

Alternatively, a Limitation of Benefits article could be adopted to provide a relatively objective basis of granting treaty benefits to entities with a nexus in the resident country. It would address a large number of treaty shopping situations based on the legal structure, ownership and activities of residents of a contracting state.

By implementing the abovementioned statement against treaty shopping and either a general treaty anti-abuse rule or a limitation of benefits article, member states would be compliant with the minimum level of protection against treaty shopping.

OECD highlights also the importance of tax policy considerations that are considered before entering into treaty or renegotiating an existing treaty.

Part of the provisions, especially the limitation of benefits rule, is still in draft form and should be considered subject to improvement before the final release of the report and the related commentary in September 2015.

## OECD guidance on transfer pricing documentation

The guidance in the report concerning transfer pricing documentation (Guidance on Transfer Pricing Documentation and Country-by-Country Reporting) will replace the transfer pricing documentation guidance contained in Chapter V of the OECD Transfer Pricing Guidelines. This guidance seeks to provide a coherent and consistent framework under which multinational enterprises (MNEs) should prepare global transfer pricing documentation, while simultaneously improving the ability of tax authorities to make better informed risk assessments and to conduct better targeted transfer pricing audits.

Under the OECD’s new guidance, MNEs will be required to prepare three-tiered transfer pricing documentation:

**Masterfile:** containing specific information relevant for all MNE group members;
**Local file**: referring specifically to material transactions of the local taxpayer; and
**Country-by-country report:** containing high-level data with respect to the global allocation of the MNE’s income and taxes and the certain measures of economic activity.

There is also additional guidance e.g. regarding time frame, frequency of the documentation and comprables updates, language of the documentation, determination of the materiality of the transactions and documentation penalties.

OECD is still in the process of determining how best to implement these new guidelines. In particular, it is continuing to deliberate how best to protect the confidentiality of commercially sensitive information, the most appropriate sharing mechanisms between tax authorities and an appropriate phase-in process. OECD also has committed to review e.g. whether additional transaction-by-transaction reporting in the country-by-country report is desirable.

The amount of information and level of detail required to be documented is increasing and thus it seems unlikely that the improved consistency of reporting will materially reduce MNE compliance costs due to the sheer increase in information required. Transfer pricing documentation according to the new guidance may require many OECD countries to change domestic law before guidance comes into effect. However, it is clear that there is a strong commitment to implement and in fact, the UK became the first country to formally commit to implementing the country-by-country report.

Therefore, it is recommendable that the tax payers already beforehand are prepared for the changes in the legislation.

## OECD guidance on Transfer Pricing Aspects of Intangibles

OECD published its final and interim revisions in relation to Chapters I (The Arm's Length Principle, II (Transfer Pricing Methods) and VI (Special Considerations for Intangible Property) of the OECD Transfer Pricing Guidelines. The revisions to the OECD Guidelines

- clarify the definition of intangibles
- provide guidance on identifying transactions involving intangibles
- provide supplemental guidance for determining arm's length conditions for transactions involving intangibles
- contain guidance on the transfer pricing treatment of local market features and corporate synergies.

Given that some of the transfer pricing issues related to intangibles are closely related to the work that will be performed by the OECD as part of Action 9 (Risks and Capital) and Action 10 (Other high-risk transactions) of the BEPS Action Plan in the course of 2015, key elements of the work on intangibles, such as section concerning ownership of intangibles and transactions involving the development, enhancement, maintenance, protection and exploitation of intangibles and section concerning the use of other methods, have not been finalized yet and thus need to be viewed as interim guidance.
The returns on intangible are shared between the group companies which perform and control the functions, provide assets, including funding, and bear and control risks related to the development, enhancement, maintenance, protection and exploitation of the intangible.

However, the principles for sharing the returns, e.g. what is the return for the entity providing the funding, will be determined next year.

More information

## Harmful Tax Practices

The report on harmful tax practices builds on the previous report by OECD published in 1998. However, OECD has moved their focus from traditional ring-fenced tax regimes to more broadly-based corporate tax reductions for certain type of income, derived for example from financial activities or intangibles. Thus, prior work on harmful tax practices is revamped with the focus on:

- Requiring substantial activity in the context of intangible regimes;
- Improving transparency by compulsory spontaneous exchange of information on rulings on preferential regimes; and
- Reviewing member and associate country regimes.

The action plan is based on three stage approach of looking first at the tax regimes of OECD members (September 2014), then at those of non-OECD members (September 2015) and finally revising the existing harmful tax framework (December 2015).

Considering substance requirements regarding intangible regimes, the primary focus is on "nexus approach". Regarding transparency and exchange of information, it should be noted that the word "compulsory" is understood to introduce an obligation to exchange information, rather than to exchange it upon request. The proposed framework covers only taxpayer-specific rulings that a single taxpayer is entitled to rely.

## Development of a Multilateral Instrument

If BEPS measures are to be countered, the speed of implementation is a key factor. Without any special measures, implementing all the proposals presented in different BEPS actions would be a slow process as individual treaties are being re-negotiated.

To address this situation, OECD proposes to develop a multilateral instrument that would enable countries implement the measures developed in the BEPS process more rapidly. According to OECD, this approach has not been used in tax legislation but precedents for modifying bilateral treaties with such multilateral instruments are found in other areas of international law. These findings are supported by a 30+ page annex that presents a toolbox for a multilateral instrument, which presents prior practices of multilateral conventions that have been implemented in other areas of public international law.

OECD indicates that a mandate for an international conference for the negotiations of multilateral instrument is considered in January 2015.

### For further information, please contact

Merja Raunio, merja.raunio@fi.pwc.com, tel. (0)20 787 7402
Martti Virolainen, martti.virolainen@fi.pwc.com, tel. (0)20 787 7396

## *Corporate Law*

### New Act on Credit Institutions

The new Act on Credit Institutions entered into force on 15 August 2014. The Act implements the directive (CRD IV, 2013/26/EU) and regulation (CRR, 575/2013) of the European Parliament and of the Council which are based on the international banking regulation reform Basel III. The new Act aims to improve the liquidity and enhance the loss-bearing capacity of credit institutions and investment firms. In addition, provisions of the new Act are intended to improve the administration and risk management as well as the supervision of financial position, governance and risk management controls of credit institutions and certain investment firms.

**For further information, please contact**

Mikko Reinikainen, mikko.reinikainen@fi.pwc.com, tel. (0)20 787 7463
Eeva Terho, eeva.terho@fi.pwc.com, tel. (0)20 787 8356