

CONTRACT

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FOR



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Study on Effects of Tax Systems on the Retention of Earnings and the Increase of Own Equity

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- ANNEX 9 -
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FINLAND



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INTRODUCTION

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At the moment there are actually no real tax obstacles for the retention of earnings. The only promotive provision is that in SME companies dividend is tax free up to the amount of 9% of retained earnings. As seen in the answers to the questionnaires many owners and experts see as a solution that retained earnings would be tax free, at least for a limited time.

Part 1 - General questions

1. What are the main characteristics of the tax systems applicable on enterprises and business owners in your Country (corporate income tax, income tax, capital gains tax, other profit based taxes, capital based taxes, other taxes...)?

Corporations (in Finnish “osakeyhtiö”) have to pay corporate income tax which is now 26 % in Finland (**Income Tax Act art. 124**). Corporate income is not taxed as income of the owners of the corporation (**Business Income Tax Act art. 1 and 2**) . Corporations may distribute dividends to the share holders. Dividend is partly tax exempted due to the net assets of the corporation (**Income Tax Act art. 33b**) . Part of dividend may be taxed as capital income or even as earned income of the recipient (**Income Tax Act art 33b**).

Income of other legal forms such as sole trader (in Finnish “ammatinharjoittaja”) and general and limited partnership (in Finnish “henkilöyhtiö”) are taxed as income of the partners (**Income Tax Act art. 16, 30, 38 , 40 and 41**). Thus for example limited partners are not legal entities for tax purposes. This income is taxed partly as capital income and partly as earned income (**Income Tax Act art. 40**). Capital income tax % is now 28 % and earned income tax in progressive (**Income Tax Act art. 124**).

Enterprises also have to pay VAT if turnover of the enterprise is more than 8 500 € in the accounting period (**VAT Act art. 3**).

1.1. Corporate Income

1.1.1. What are the general principles for the computation of taxable profits?

Corporation is able to deduct most of its costs from its turn over (**Business Income Tax Act art. 7-8**). Certain costs are not deductible and certain costs are only partly deductible (**Business Income Tax Act art. 8 and 16**) .

Some costs are deductible only by doing early writeoffs (**Business Income Tax Act art. 30-39**) . The amount of writeoffs depends on the type of investments.

In some particular cases corporates are able to form a reserve in the taxation (**Business Income Tax Act art. 46-49**).

1.1.2. What are the main differences between tax balance sheet and commercial balance sheet?

Valuation of real estates is different (**Act in Finnish: Laki varojen arvostamisesta verotuksessa § 3**) . Also handling of subordinated loan differs.

1.1.3. What are the most important adjustments for the computation of taxable profits/taxable gains on the base of accounting profits?

In order to calculate taxable profit corporations have to do some adjustments on the base of accounting profit.

Writeoffs may be different in taxation and in accounting (**Business Income Tax Act and Bookkeeping Act**). There are also some costs or deductions which are not deductible or are only partly deductible at taxation but which are deductible in book keeping. **For example entertainment expenses are only 50 per cent deductible at taxation (Business Income Tax Act art. 8)**

1.2. Income

1.2.1. What are the general principles of income taxation of business owners on business income, wages, distributed earnings, interest on loans and capital gain (sale of shares)?

Owners of the corporate are taxed only when they will draw up income from the corporation (**Income Tax Act art. 1, 2 and Business Income Tax**

Act art. 1). Income will be distributed to the owners by dividends, by wages or by interests.

Dividend is partly tax exempted due to the net assets of the corporation (**Income Tax Act art. 33b**). Part of dividend may be taxed as capital income (tax rate 28 %) or even as earned income of the recipient.

For corporate owners it usually is more tax efficient to take income from the corporation by dividends than to pay progressively taxed wages. For some extent it is quite tax efficient for corporate owners to have progressive taxed earned income.

However for some very small corporations dividend taxation is not anymore so tax efficient as it used to be before the latest tax reform.

Interest rate on loans is limited (**Taxation Proceedings Act art. 29 (in Finnish Verotusmenettelylaki)**).

Capital gains of shares are in some cases tax exempted if shares are owned by another corporate (**Business Income Tax Act art. 6 and 6b**). For individuals capital gains are taxable and tax rate is 28 % (**Income Tax Act art. 124**). Individuals are able to deduct from selling price of the assets either purchase price of assets or certain deemed acquisition cost (**Income Tax Act art. 46-47**).

Income of other legal forms such as sole trader and general partnership will be taxed as income of the partner (**Income Tax Act art. 30**).

1.2.2. Is there a different tax treatment for income from different income sources?

Incomes of corporates from different sources are taxed separately (**Business Income Tax Act art 1-2 and Income Tax Act art. 25**). Tax per cent is the same, 26 % (**Income Tax Act art. 124**). The corporate is not able to deduct losses of one income source from profit of another income source (**Income Tax Act art. 119 and 120**).

1.3. Capital

Finland	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For CORPORATIONS (distinguish specific tax rates for SMEs)				
	2002	2003	2004	2005	2006
Corporate tax					
1. Tax rate					
Standard	29	29	29	26	26
Reduced	-	-	-	-	-
Minimum Tax	-	-	-	-	-
Special Rates	-	-	-	-	-
Non profit tax (local tax on corporations, energy tax...)	insurance premium tax Insurace companies), energy tax	insurance premium tax Insurace companies), energy tax	insurance premium tax Insurace companies), energy tax	insurance premium tax Insurace companies), energy tax	insurance premium tax Insurace companies), energy tax
2. Tax accounting rules	Book keeping act and business income tax Act	Book keeping act and business income tax Act	Book keeping act and business income tax Act	Book keeping act and business income tax Act	Book keeping act and business income tax Act
3. Depreciation					
Basis	rest value after the latest depreciation	rest value after the latest depreciation	rest value after the latest depreciation	rest value after the latest depreciation	rest value after the latest depreciation
Methods	in taxation x% of the rest value	in taxation x% of the rest value	in taxation x% of the rest value	in taxation x% of the rest value	in taxation x% of the rest value
Rates	buildings 4-20%, itangibles 1/5-1/10 per year, bomb shelters 25% per year, other investments 25% (Business Income Tax Act art. 30, 34, 36, 37)	buildings 4-20%, itangibles 1/5-1/10 per year, bomb shelters 25% per year, other investments 25% (Business Income Tax Act art. 30, 34, 36, 37)	buildings 4-20%, itangibles 1/5-1/10 per year, bomb shelters 25% per year, other investments 25% (Business Income Tax Act art. 30, 34, 36, 37)	buildings 4-20%, itangibles 1/5-1/10 per year, bomb shelters 25% per year, other investments 25% (Business Income Tax Act art. 30, 34, 36, 37)	buildings 4-20%, itangibles 1/5-1/10 per year, bomb shelters 25% per year, other investments 25% (Business Income Tax Act art. 30, 34, 36, 37)
Accounting	the real loss in value according to the usage period (Book	the real loss in value according to the usage period (Book	the real loss in value according to the usage period (Book	the real loss in value according to the usage period (Book	the real loss in value according to the usage period (Book

Finland	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For CORPORATIONS (distinguish specific tax rates for SMEs)				
	2002	2003	2004	2005	2006
	Keeping Act art. 5)	Keeping Act art. 5)	Keeping Act art. 5)	Keeping Act art. 5)	Keeping Act art. 5)
Intangibles	Linear 1/5-1/10 per year (Book Keeping Act art 5a, 9)	Linear 1/5-1/10 per year (Book Keeping Act art 5a, 9)	Linear 1/5-1/10 per year (Book Keeping Act art 5a, 9)	Linear 1/5-1/10 per year (Book Keeping Act art 5a, 9)	Linear 1/5-1/10 per year (Book Keeping Act art 5a, 9)
Non depreciable assets	land, water areas, most shares	land, water areas, most shares	land, water areas, most shares	land, water areas, most shares	land, water areas, most shares
4. Provisions					
Risks and futures expenses	deductible in book keeping, not in taxation	deductible in book keeping, not in taxation	deductible in book keeping, not in taxation	deductible in book keeping, not in taxation	deductible in book keeping, not in taxation
Bad debts	deductible	deductible	deductible	deductible	deductible
Pensions	deductible (Business Income Tax Act art 8.1.4)	deductible (Business Income Tax Act art 8.1.4)	deductible (Business Income Tax Act art 8.1.4)	deductible (Business Income Tax Act art 8.1.4)	deductible (Business Income Tax Act art 8.1.4)
Repairs	deductible (Business Income Tax Act art 7)	deductible (Business Income Tax Act art 7)	deductible (Business Income Tax Act art 7)	deductible (Business Income Tax Act art 7)	deductible (Business Income Tax Act art 7)
5. Losses					
Carry forward	10 years (Invome Tax Act art 119, 120)	10 years (Invome Tax Act art 119, 120)	10 years (Invome Tax Act art 119, 120)	10 years (Invome Tax Act art 119, 120)	10 years (Invome Tax Act art 119, 120)
Carry back	no	no	no	no	no
Transfer of losses	in specific circumstances, requires a permission of tax authorities	in specific circumstances, requires a permission of tax authorities	in specific circumstances, requires a permission of tax authorities	in specific circumstances, requires a permission of tax authorities	in specific circumstances, requires a permission of tax authorities
5. Inventories					
Valuation rules	original purchase price or a probable less value (Business Income Tax Act art 28)	original purchase price or a probable less value (Business Income Tax Act art 28)	original purchase price or a probable less value (Business Income Tax Act art 28)	original purchase price or a probable less value (Business Income Tax Act art 28)	original purchase price or a probable less value (Business Income Tax Act art 28)
Allocation methods	FIFO	FIFO	FIFO	FIFO	FIFO
Personal Income tax					
Interest Income	29%	29%	29%	26% for corporates, 28% for others	26% for corporates, 28% for others
Dividends	avoir fiscal	avoir fiscal	avoir fiscal	partly tax free	partly tax free

Finland	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For CORPORATIONS (distinguish specific tax rates for SMEs)				
	2002	2003	2004	2005	2006
	(Avoir Fiscal Act)	(Avoir Fiscal Act)	(Avoir Fiscal Act)	(Business Income Tax Act art 6a, Income Tax Act art 33a, 33b)	(Business Income Tax Act art 6a, Income Tax Act art 33a, 33b,)
Employment income	the tax is progressive	the tax is progressive	the tax is progressive	the tax is progressive	the tax is progressive
Capital gains tax					
Sale of fixed assets	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation
Timing rules	simultaneously with depreciation	simultaneously with depreciation	simultaneously with depreciation	simultaneously with depreciation	simultaneously with depreciation
Accounting rules	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation
Inflation	-	-	-	-	-
Rates	29%	29%	29%	26%	26%
Exemptions	-	-	-	-	-
Sale of shares	29%	29%	29%	26%, can be tax free if the shares belong to the fixed assets (Business Income Tax Act art 6b)	26%, can be tax free if the shares belong to the fixed assets (Business Income Tax Act art 6b)
Capital loss					
Fixed assets	deductible if the selling price is less than the total rest value	deductible if the selling price is less than the total rest value	deductible if the selling price is less than the total rest value	deductible if the selling price is less than the total rest value	deductible if the selling price is less than the total rest value
Shares	deductible from profits the same year or in the next 5 years	deductible from profits the same year or in the next 5 years	deductible from profits the same year or in the next 5 years	deductible from profits the same year or in the next 5 years	deductible from profits the same year or in the next 5 years
Wages					
Average cost to the Undertaking	46% (includes pension costs and social costs)	46% (includes pension costs and social costs)	42% (includes pension costs and social costs)	42% (includes pension costs and social costs)	42% (includes pension costs and social costs)
Average cost to the	24%	24%	28%	28%	28%

Finland	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For CORPORATIONS (distinguish specific tax rates for SMEs)				
	2002	2003	2004	2005	2006
employee					
Overall tax on distributed earnings or Dividends					
Timing	the year of payment	the year of payment	the year of payment	the year of payment	the year of payment
Tax credit structure	avoir fiscal	avoir fiscal	avoir fiscal	partly free	partly free
Excluding non profit tax					
Including non profit tax					
Deduction of expenses					
General rule	expenses related to taxable income are deductible (Business Income Tax Act art 7,8)	expenses related to taxable income are deductible (Business Income Tax Act art 7,8)	expenses related to taxable income are deductible (Business Income Tax Act art 7,8)	expenses related to taxable income are deductible (Business Income Tax Act art 7,8)	expenses related to taxable income are deductible (Business Income Tax Act art 7,8)
Non-deductibility of expenses	expenses not related to business activities are not deductible (Business Income Tax Act art 7,8)	expenses not related to business activities are not deductible (Business Income Tax Act art 7,8)	expenses not related to business activities are not deductible (Business Income Tax Act art 7,8)	expenses not related to business activities are not deductible (Business Income Tax Act art 7,8)	expenses not related to business activities are not deductible (Business Income Tax Act art 7,8)
Thin capitalization	-	-	-	-	-
Overall corporate tax on Retained earnings	29%	29%	29%	26%	26%
Excluding non profit tax	-	-	-	-	-
Including non profit tax	-	-	-	-	-
Debt financing					
Interest deductibility	yes	yes	yes	yes	yes
Limits on	no	no	no	no	no

Finland	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For CORPORATIONS (distinguish specific tax rates for SMEs)				
	2002	2003	2004	2005	2006
interest deductibility					
Interest deductibility on business owner loan to Undertaking	yes	yes	yes	yes	yes

Finland	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For PARTNERSHIPS (distinguish specific rates for SMES)				
	2002	2003	2004	2005	2006
Tax applicable to partnerships					
1. Tax rate					
Standard	the income is taxed on the owners, the income is divided in capital income (tax 29%) and earned income (progressive tax)	the income is taxed on the owners, the income is divided in capital income (tax 29%) and earned income (progressive tax)	the income is taxed on the owners, the income is divided in capital income (tax 29%) and earned income (progressive tax)	the income is taxed on the owners, the income is divided in capital income (tax 29%) and earned income (progressive tax)	the income is taxed on the owners, the income is divided in capital income (tax 29%) and earned income (progressive tax)
Reduced	-	-	-	-	-
Minimum Tax	-	-	-	-	-
Special Rates	-	-	-	-	-
Non profit tax (local tax on corporations, energy tax...)	-	-	-	-	-
2. Tax accounting rules	Book keeping act and business income tax Act	Book keeping act and business income tax Act	Book keeping act and business income tax Act	Book keeping act and business income tax Act	Book keeping act and business income tax Act
3. Depreciation					
Basis	rest value after the latest depreciation	rest value after the latest depreciation	rest value after the latest depreciation	rest value after the latest depreciation	rest value after the latest depreciation
Methods	in taxation x% of the rest value	in taxation x% of the rest value	in taxation x% of the rest value	in taxation x% of the rest value	in taxation x% of the rest value
Rates	buildings 4-	buildings 4-	buildings 4-	buildings 4-	buildings 4-

Finland	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For PARTNERSHIPS (distinguish specific rates for SMES)				
	2002	2003	2004	2005	2006
	20%, intangibles 1/5-1/10 per year, bomb shelters 25% per year, other investments 25% (Business Income Tax Act art. 30, 34, 36, 37)	20%, intangibles 1/5-1/10 per year, bomb shelters 25% per year, other investments 25% (Business Income Tax Act art. 30, 34, 36, 37)	20%, intangibles 1/5-1/10 per year, bomb shelters 25% per year, other investments 25% (Business Income Tax Act art. 30, 34, 36, 37)	20%, intangibles 1/5-1/10 per year, bomb shelters 25% per year, other investments 25% (Business Income Tax Act art. 30, 34, 36, 37)	20%, intangibles 1/5-1/10 per year, bomb shelters 25% per year, other investments 25% (Business Income Tax Act art. 30, 34, 36, 37)
Accounting	the real loss in value according to the usage period (Book Keeping Act art. 5)	the real loss in value according to the usage period (Book Keeping Act art. 5)	the real loss in value according to the usage period (Book Keeping Act art. 5)	the real loss in value according to the usage period (Book Keeping Act art. 5)	the real loss in value according to the usage period (Book Keeping Act art. 5)
Intangibles	Linear 1/5-1/10 per year (Book Keeping Act art 5a, 9)	Linear 1/5-1/10 per year (Book Keeping Act art 5a, 9)	Linear 1/5-1/10 per year (Book Keeping Act art 5a, 9)	Linear 1/5-1/10 per year (Book Keeping Act art 5a, 9)	Linear 1/5-1/10 per year (Book Keeping Act art 5a, 9)
Non depreciable assets	land, water areas, most shares	land, water areas, most shares	land, water areas, most shares	land, water areas, most shares	land, water areas, most shares
4. Provisions					
Risks and futures expenses	deductible in book keeping, not in taxation	deductible in book keeping, not in taxation	deductible in book keeping, not in taxation	deductible in book keeping, not in taxation	deductible in book keeping, not in taxation
Bad debts	deductible	deductible	deductible	deductible	deductible
Pensions	deductible (Business Income Tax Act art 8.1.4)	deductible (Business Income Tax Act art 8.1.4)	deductible (Business Income Tax Act art 8.1.4)	deductible (Business Income Tax Act art 8.1.4)	deductible (Business Income Tax Act art 8.1.4)
Repairs	deductible (Business Income Tax Act art 7)	deductible (Business Income Tax Act art 7)	deductible (Business Income Tax Act art 7)	deductible (Business Income Tax Act art 7)	deductible (Business Income Tax Act art 7)
5. Losses					
Carry forward	10 years (Invome Tax Act art 119, 120)	10 years (Invome Tax Act art 119, 120)	10 years (Invome Tax Act art 119, 120)	10 years (Invome Tax Act art 119, 120)	10 years (Invome Tax Act art 119, 120)
Carry back	no	no	no	no	no
Transfer of losses	in specific circumstances, requires a permission of tax authorities	in specific circumstances, requires a permission of tax authorities	in specific circumstances, requires a permission of tax authorities	in specific circumstances, requires a permission of tax authorities	in specific circumstances, requires a permission of tax authorities

Finland	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For PARTNERSHIPS (distinguish specific rates for SMES)				
	2002	2003	2004	2005	2006
5. Inventories					
Valuation rules	original purchase price or a probable less value (Business Income Tax Act art 28)	original purchase price or a probable less value (Business Income Tax Act art 28)	original purchase price or a probable less value (Business Income Tax Act art 28)	original purchase price or a probable less value (Business Income Tax Act art 28)	original purchase price or a probable less value (Business Income Tax Act art 28)
Allocation methods	FIFO	FIFO	FIFO	FIFO	FIFO
Personal Income tax					
Interest Income	29%	29%	29%	28%	28%
Dividends	TAX FREE (Avoir Fiscal Act)	TAX FREE (Avoir Fiscal Act)	TAX FREE (Avoir Fiscal Act)	PARTLY TAX FREE (Income Tax Act art 33a, 33b)	PARTLY TAX FREE (Income Tax Act art 33a, 33b)
Employment income	the tax is progressive	the tax is progressive	the tax is progressive	the tax is progressive	the tax is progressive
Capital gains tax					
Sale of fixed assets	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation
Timing rules	simultaneously with depreciation	simultaneously with depreciation	simultaneously with depreciation	simultaneously with depreciation	simultaneously with depreciation
Accounting rules	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation	reduces the rest value and thus the depreciation
Inflation	-	-	-	-	-
Rates	partly progressive	partly progressive	partly progressive	partly progressive	partly progressive
Exemptions	-	-	-	-	-
Sale of shares	29%	29%	29%	28%	28%
Capital loss					
Fixed assets	deductible if the selling price is less than the total rest value	deductible if the selling price is less than the total rest value	deductible if the selling price is less than the total rest value	deductible if the selling price is less than the total rest value	deductible if the selling price is less than the total rest value
Shares	deductible from profits the same year	deductible from profits the same year	deductible from profits the same year	deductible from profits the same year	deductible from profits the same year

Finland	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For PARTNERSHIPS (distinguish specific rates for SMES)				
	2002	2003	2004	2005	2006
	or in the next 5 years	or in the next 5 years	or in the next 5 years	or in the next 5 years	or in the next 5 years
Wages					
Average cost to the Undertaking	46% (includes pension costs and social costs)	46% (includes pension costs and social costs)	42% (includes pension costs and social costs)	42% (includes pension costs and social costs)	42% (includes pension costs and social costs)
Average cost to the employee	24%	24%	28%	28%	28%
Dividends					
Timing	the year of payment	the year of payment	the year of payment	the year of payment	the year of payment
Tax credit structure	avoir fiscal	avoir fiscal	avoir fiscal	partly tax free	partly tax free
Deduction of expenses					
General rule	expenses related to taxable income are deductible (Business Income Tax Act art 7,8)	expenses related to taxable income are deductible (Business Income Tax Act art 7,8)	expenses related to taxable income are deductible (Business Income Tax Act art 7,8)	expenses related to taxable income are deductible (Business Income Tax Act art 7,8)	expenses related to taxable income are deductible (Business Income Tax Act art 7,8)
Non-deductibility of expenses	expenses not related to business activities are not deductible (Business Income Tax Act art 7,8)	expenses not related to business activities are not deductible (Business Income Tax Act art 7,8)	expenses not related to business activities are not deductible (Business Income Tax Act art 7,8)	expenses not related to business activities are not deductible (Business Income Tax Act art 7,8)	expenses not related to business activities are not deductible (Business Income Tax Act art 7,8)
Thin capitalization	-	-	-	-	-
Debt financing					
Interest deductibility	YES	YES	YES	YES	YES
Limits on interest deductibility	NO	NO	NO	NO	NO

1.3.1. Is there a different tax treatment between distributions of earnings and capital gains realised by the sale of the business or the shares in the undertaking?

There is different tax treatment for distribution of earnings and capital gains. Distribution of earnings is for some extent tax free. Capital gains will be taxed.

1.3.2. Are there different tax treatments for long-term capital gains and short-term capital gains?

Yes, the tax treatment is different if the seller is an individual and if it is more tax efficient to deduct certain deemed acquisition cost from selling price of the assets. If the shares have been owned at least 10 years, then deemed acquisition cost is 40 per cent from selling price and for less than 10 years owned shares deemed acquisition cost is only 20 per cent (Income Tax Act art. 46)

1.3.3. Are there different tax treatments for capital gain from SME business stock and capital gain from larger companies' business stock?

There is no difference when the seller of the stocks is an individual. If the seller is another company, then capital gain is in certain cases tax free (Business Income Tax Act art. 6 and 6b).

2. What are the main types of business entities and the main differences in (corporate) income taxation for sole traders, general partnerships, limited partnerships and corporation and other business entities if relevant?

Main types of business entities are corporation, general partnership, limited partnership and sole trader (Income Tax Act art. 3 and 4).

Profit of corporation is taxed as profit of the corporation.

Profit of general partnership and sole trader is taxed as income of the partners/traders.

2.1. *Are partnerships treated transparent for tax purposes?*

Yes

2.2. *Can partnerships opt for corporate income tax?*

No. It is possible to change form of business, but then there is not anymore a partnership but a corporate ([Income Tax Act art. 24](#)).

2.3. *Once they have opted for a regime is it easy to switch back?*

No ([Income Tax Act art. 24 and Supreme Administrative Court 2008/55](#)).

2.4. *Is there a difference in this respect between general and limited partnerships?*

No

2.5. *Can corporations opt to be treated tax transparent?*

No. According to the company act it is possible to switch a company to a partnership but according to tax law this is not possible without tax consequences ([Income Tax Act art. 24 and Supreme Administrative Court 2008/55](#)).

2.6. *Once they have opted for a regime is it easy to switch back?*

No

2.7. *Are their differences in this respect between the different types of corporations?*

According to Finnish income tax act it is possible for transparent treated taxable person to switch to a corporation without any direct tax consequences but it is not possible vice versa without direct tax consequences ([Income Tax Act art. 24](#) and [Supreme Administrative Court 2008/55](#)).

	INCLUDE RELEVANT TAX PROVISIONS IN 2002 AND SUBSEQUENT CHANGES UP TO 2007			
<u>Finland</u>	<u>General Partnership</u>	<u>Limited Partnership</u>	<u>Corporation</u>	<u>Sole Trader</u>
Corporate tax	-	-	29 % to 26 %	-
Income tax	progressive	progressive	-	progressive
Capital gains tax	29% to 28%	29% to 28%	29% to 26%	28%
Option for Transparent treatment	<u>rule</u>	<u>rule</u>	<u>not possible</u>	<u>rule-</u>

3. Are there any special tax regimes for SMEs for (corporate) income tax purposes?

NO ([Business Income Tax Act](#))

3.1. *What are the conditions to be fulfilled in order to benefit from these special tax regimes?*

Not applicable

3.2. *Are there limits on the length of time during which these special tax regimes are available, or other limits?*

Not applicable

4. Are there any special tax incentives, such as (re-)investment reserves or provisions, special depreciations/capital allowances deductible for (corporate) income tax purposes?

YES

There are some reserves for example reserve to cover credit loss, guarantee reserve, reduction in prices reserve. Some of these reserves are not to be used by all corporates (Business Income Tax Act art. 46-49).

- 4.1. *Do these elements of internal financing represent an important alternative to the financing by retained earnings?*

NO

- 4.2. *Are there any compulsory measures in relation to the retention of earnings (e.g. legal constraints for the distribution of profits and dividend policy)?*

Not in tax Acts. Company Act has rules concerning distribution of profits. According to Company Act company is not allowed to distribute dividend if there is a risk for insolvency.

5. Are there any differences in the tax treatment of stock and cash dividends¹?

NO

If a company will pay dividend, dividend will be taxed as shareholders income according to tax law although dividend would be paid as stocks. There might be some tax consequences for the company, if it will pay dividend as stocks.

¹ For the Undertaking stock dividend means increased own equity. For the shareholder it means additional shares in the Undertaking which may be untaxed until sold, unlike a cash dividend.

6. Have there been any changes in the tax regulation in recent years - since 2002 - that have had an important effect on the retention of earnings, the distribution earnings or the reinvestment of profits for a particular purpose?

YES

Taxation of dividends has been changed dramatically from the beginning of tax year 2005. The dividends are not deductible from the income of the corporate, and the taxes the corporate pay is not any more an allowance in the shareholders taxation. So partly the dividend are taxed by the corporate and also **the** share holders.

7. Are there any current plans for tax reforms that have as their object to have an impact on the retention of earnings?

NO

Retention of earnings will be taxed when the company will distribute it`s assests to the owners of the company.

PART 2 - TAX ASPECTS OF RETAINED EARNINGS VERSUS DISTRIBUTED PROFITS AND WAGES

8. What is the tax treatment of retained earnings compared to distribution of earnings on the level of the Undertaking and at a combined level of Undertaking (corporate) and business owner (individual)?

The company has to pay corporate income tax of its profit regardless of whether it will distribute dividend or not (**Business Income Tax Act**). Retained earnings are not taxed separately. The corporate will not have any tax consequences when it will distribute dividend to its shareholders.

- 8.1. *Is there an economic double taxation of distribution of earnings (taxation of Undertaking income and then taxation on the distribution of earnings at the Undertaking level or at the business owner level)?*

YES

In Finland the corporate pays 26 % tax of its profit. **Corporation is not able to deduct paid dividends.**

Business owner is able to get tax free dividend 9 % calculated from the corporates net assets. Maximum amount of tax free dividend is 90 000 € per year for one owner. If the corporate will distribute more than 90 000 € dividend the amount of the dividend exceeding 90 000 € 70 % will be taxed as capital income and 30 % will be tax free. If the corporate will distribute dividend more than 9 % of corporates net assets then of this dividend (over 9 % of net assets) 70 % of this dividend will be taxed as earned income and 30 % will be tax free (**Income Tax Act art. 33b**).

Business owner is not able to deduct taxes paid by the corporation and due to this fact there might be double taxation of distribution of earnings.

	INCLUDE RELEVANT TAX PROVISIONS IN 2002 AND SUBSEQUENT CHANGES UP TO 2007	
<u>Finland</u>	<u>Undertaking</u>	<u>Individual Business owner</u>
Corporate tax	29 %to 26 %	-
Income tax	-	dividends more than 9 % of net assets
Dividend tax	-	-
Dividend credit	Until end of year 2004	until end of year 2004
Capital gains tax	-	over 90 000 € dividends
If option for Transparent treatment chosen	=	=

9. Please describe the differences in the tax treatment of distribution of earnings realised as a capital gain in the context of a sale of the shares or of the business compared to that (i) of retained earnings, (ii) of wages salaries paid to the business owner and (iii) of a loan granted by the Undertaking to the business owner?

If a shareholder has owned stocks of the corporation over 10 years then capital gain tax from the selling price of the stocks is not more than 16,8 %. It might also be less than 16.8 % if purchase price is more than 40 % of selling price of shares (Income Tax Act art. 45-47, 124).

For some extent it is more tax efficient for shareholder to get dividend because dividend is to certain extent tax free (max 90 000 €/9 % of net assests per year). Retained earnings will increase corporations own equity and trough this way it

will increase amount of tax free dividend (**Income Tax Act art. 33b**). Due to this reason for shareholder it is usually to some extent more tax efficient to rise dividend than to have capital gain.

To pay salaries is to certain extent quite tax efficient for some of shareholders because corporation is able to deduct paid salaries in its book keeping and for shareholder dividend may be taxed quite low up to certain amount (**Business Income Tax Act art. 7-8**).

A loan granted to the business owner is not usually any tax efficient way to have property from corporation because loan which has not been paid back to the corporation at the end of calendar year will be handled as capital income (tax 28 %) of the business owner (**Income Tax Act art. 53a**). Business owner is in five year period able to deduct a loan paid back to corporation from capital income (**Income Tax Act art 54c and 131**).

	INCLUDE RELEVANT TAX PROVISIONS IN 2002 AND SUBSEQUENT CHANGES UP TO 2007			
<u>Finland</u>	<u>Distributed profits</u>	<u>Retained Profit</u>	<u>Wages/Salaries to business owner</u>	<u>Loan to business owner</u>
Sale of shares	tax free up to 9% of net assets	26% corporates, 28%/progressive for sole traders	progressive	28%
Sale of business	-	-	-	-

10. Is the combination of wages (paid to the business owner by the Undertaking), profit distributions and retained earnings a tax planning issue that is anticipated and addressed by business owners in view of minimising the overall tax burden of the business owner and the Undertaking?

YES

Tax planning is very important for business owners. Usually income of business owner is a combination of wages/salary and dividend. If shareholder has owned

stocks of the corporation over 10 years then capital gain tax from the selling price of the stocks is not more than 16,8 %. It might also be less than 16.8 % if purchase price is more than 40 % of selling price of shares (Income Tax Act art. 46) .

For some extent it is more tax efficient for shareholder to get dividend because dividend is to certain extent tax free (max 90 000 €/9 % of net assets per year) (Income Tax Act art. 33b). Retained earnings will increase corporations own equity and through this way it will increase amount of tax free dividend (Act in Finnish: Laki varojen arvostamisesta verotuksessa). Due to this reason for shareholder it is usually to some extent more tax efficient to rise dividend that to have capital gain.

To pay salaries is to certain extent quite tax efficient for some of shareholders because corporation is able to deduct paid salaries in it`s book keeping and for shareholder dividend may be taxed quite low up to certain amount (Business Income Tax Act art. 8).

A loan granted to the business owner is not usually any tax efficient way to have property from corporation because loan which has not been paid back to the corporation at the end of calendar year will be handled as capital income (tax 28 %) of the business owner. Business owner is in five year period able to deduct a loan paid back to corporation from capital income.

11. In respect to the previous question, is the business owner more interested in minimising his/her tax burden and then the Undertaking's or both equally?

Both equally if there is only one or few share owners.

12. Are there instances in which minimising the tax burden of the business owner would mean dramatically increasing the tax burden of the Undertaking?

No. Corporation income tax is flat 26 %. Thus minimising the tax burden of the business owner would not dramatically increase the tax burden of the corporation.

13. For corporate income tax or capital gains tax purposes, are there any incentives/disincentives to retain earnings rather than distribute them or pay wages?

YES

Wages are deductible at corporate taxation (**Business Income Act art. 8**). For corporates there is thus some incentive to pay wages. Dividend is not deductible for the corporations.

For capital gain purposes there are no incentives/disincentives.

13.1. Are there any limitations or ceilings for these incentives?

YES

According to the Finnish corporation act corporation is able to pay dividend only in the limit of free equity (**Corporation Act chapter 13**). Wages are limited to the reasonable amount.

13.2. Is there a risk that these incentives can be used more than one time by the business owners by splitting up the business activities into different legal entities?

NO

By splitting the business also assets of the corporation will be divided. **For example write offs are allowed to done only once (Business Income Tax act. 52c).**

14. What is the tax treatment of declared loans granted by the Undertaking to the business owner?

Declared loans will be treated as capital income (tax rate 28 %) of the business owner if business owner or his/her family owns more than 10 % of the shares of

the corporation and if declared loan has not been paid back to the corporation at the end of calendar year ([Income Tax Act art 53a](#)).

14.1. *Is there a minimum interest rate to be charged for tax purposes?*

Yes. If declared loan will not be treated as capital income (loan has been paid back to the corporation at the end of calendar year) then business owner has to pay interest which will vary yearly ([Taxation Proceedings Act art. 29](#)) .

14.2. *How is the interest rate treated for tax purposes for the Undertaking?*

It is income for the corporation ([Business Income Tax Act art 4](#)).

14.3. *How is the interest rate treated for tax purposes for the business owner?*

Business owner is able to deduct interest if he/she has used loaned money for acquisition of his/her apartment or for purpose from which he/she will acquire taxable income ([Income Tax Act art 58](#)). If loan will be used for some other acquisitions then the interest is not deductible ([Income Tax Act art 58](#)).

14.4. *What are the combined tax effects of such a loan compared to a distribution of earnings equivalent in amount?*

Loan is usually capital income of business owner ([Income Tax Act art. 53a](#)). Business owner has to pay back the loan to the corporation. For tax reasons the loan should be paid back during the next 5 years ([Income Tax Act art. 54c](#)).

Dividend is tax free for some extent ([Income Tax Act art. 33b](#)). In most cases dividend is thus more tax efficient for business owner.

15. Are there any other taxes (e.g. net worth tax) which are imposed or based on the net equity of the Undertaking?

NO

16. Are there any other tax incentives for either the retention of earnings or their distribution of profits?

NO

PART 3 - TAX ASPECTS OF RETAINED EARNINGS FINANCING VERSUS DEBT FINANCING

17. In debt financing, what is the tax treatment of interest expenses paid or accrued by the Undertaking?

Interests are deductible for the corporations. [Business Income Tax Act art 18](#)

- 17.1. Is there a different tax treatment to deductions on interest paid when the lender is a resident or a non-resident for tax purposes?*

No

- 17.2. Is there a different tax treatment on interest on long-term debt and interest on short-term debt?*

No

18. Are there any tax benefits that are actionable based on specific amounts of equity (e.g. notional interest expense based on the increase of own equity or the total amount of equity)?

No

- 18.1. What is the exact calculation method used to implement this incentive and to evaluate the benefits once this incentive is implemented?*

There is no method.

- 18.2. Are there any other tax provisions favouring increases in own equity?*

Increasing own equity will also increase amount of tax free dividend.

[Income Tax Act art 33 b](#)

19. Is debt financing of an enterprise by the business owner himself or his/her family recognised for tax purposes (ie. If the business owner or his/her family lends money to the Undertaking are they treated differently than other lenders for tax purposes)?

NO

Corporation is not allowed to pay too high interest rate of the loan business owners have lent to the corporation. If lent money is necessary for the corporation's financial situation then the interest rate is allowed to be higher (same rate when money will be lent from financial institutions) than in the situation when lent money is not necessary for the corporation due to its financial situation. [Income Tax Act 33d](#)

20. Is there a general discrimination between retained earnings financing and debt financing from a tax point of view?

YES

Interests are deductible for the corporation. [Business Income Tax Act art 18](#)

- 20.1. *Is there a general discrimination between retained earnings financing and equity financing from a tax point of view?*

NO

- 20.2. *Is there a general discrimination between equity financing and debt financing from a tax point of view?*

YES

Interest of debt is deductible for the corporation. [Business Income Tax Act art 18](#)

21. Are there any debt to equity ratios limiting the deductibility of interest expenses for tax purposes?

NO

21.1. If so, does the limitation apply to loans granted by the business owner and affiliated persons or does it include loans granted by third parties?

Not Applicable

21.2. What are the consequences if the debt to equity ratio is not respected?

Not Applicable

22. Are there any tax provisions likely to impact the conversion of retained earnings into share paid in capital (ie. share buy-back)?

YES

In certain situations there might be a risk for taxation of hidden dividend if the corporation will buy it`s shares from the owners. Hidden dividend will be taxed as earned income. . [Income Tax Act 33d](#)

23. Are there any other taxes that have as their object to affect or impact on either Undertaking debt financing or retained earnings financing?

NO

PART 4 - TAX ASPECTS OF BUSINESS INCOME VERSUS PRIVATE INCOME

24. In respect to individual business owners, what is the general tax treatment for private (ie: interest on passive investment) income compared to business income (ie: income generated from your business activity)?

There is different tax treatment concerning dividend taxation when individual business owner will receive dividend. Tax of dividends from listed company is 19,6%. Tax of dividends from non listed company depends from net assets of the company **Income Tax Act art 33a**

In Finland the corporate pays 26% tax of its profit. **Income Tax Act art 124**

Business owner is able to get tax free dividend 9% calculated from the corporates net assets. Maximum amount of tax free dividend is 90 000 € per year for one owner. If the corporate will distribute more than 90 000 € dividend the amount of the dividend exceeding 90 000 € 70% will be taxed as capital income and 30% will be tax free. If the corporate will distribute dividend more than 9% of corporates net assets then of this dividend (over 9% of net assets) 70% of this dividend will be taxed as earned income and 30% will be tax free. **Income Tax Act art 33 b**

Business owner is not able to deduct taxes paid by the corporation and due to this fact there might be double taxation of distribution of earnings.

	INCLUDE RELEVANT TAX PROVISIONS IN 2002 AND SUBSEQUENT CHANGES UP TO 2007	
<u>Finland</u>	<u>Private Investment Income</u>	<u>Business Income</u>
...	0% to 19,6% Income Tax	28%/progressive to

	Act art 33 a	28%/progressive Income Tax Act art 33 b
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24.1. Are there different allowances or special treatments for private investment income and business income?

NO

25. Is there a different tax treatment for interest income received in a private investors capacity (ie: business owner investment return in another Undertaking) and interest income earned through business activity (ie: business owner investment return from the Undertaking)?

NO

The taxation is the same.

26. Does the tax system encourage business owners to invest in private assets, which are subsequently rented or leased to their enterprises?

YES

By renting or leasing assets to business owners own corporation business owner is able to get rent from rented or leased assets. This rent will be taxed as capital income (28 %) which is normally less than earned income tax rate. **Income Tax Act art 124** Corporation is able to deduct paid rent. **Business Income Tax Act art 18**

27. By opposition to question 26, does the tax system encourage that assets be acquired by the Undertaking and rented or leased to the business owner?

YES

In some situations yes. For example in some cases it is more tax efficient that apartment where business owner lives is acquired by the corporation. In some cases these acquisitions might reduce amount of tax free dividend and thus it is not for tax purposes wise to acquire property by the corporation. **Business Income Tax Act art 33 b**

28. Are capital gains from private assets taxed in the same way as capital gains realised within the context of a business activity?

Not quite. Capital gains from private assets are taxed 28% for individuals and owners of general or limited partnerships. For corporates the tax rate at the moment is 26%. **Income Tax Act art 124**

28.1. If capital gains from private assets are taxed lower, does this represent an important incentive for the business not to invest in their own Undertaking?

Not Applicable

29. Are interest expenses incurred on private debts deductible for tax purposes?

YES

Expences for example acquisition of apartment used by owner and for investments that will bring taxable income are deductible. **Business Income Tax Act art 18** Interest expenses for private consumption are not deductible. **Income Tax Act art 58**

30. Is there a tax advantage for the Undertaking in transferring debts from the business owner to the Undertaking?

NO

It is not allowed to transfer debts to the corporation without any compensation. Tax benefit from the deduction of interests for the corporations is 26 % and tax benefit for business owner is 28 %. [Income Tax Act art 124](#)

31. Is there a tax advantage for the business owner in transferring debts from the business owner to the Undertaking?

NO

It is not allowed to transfer debts to the corporation without any compensation. Tax benefit from the deduction of interests for the corporations is 26 % and tax benefit for business owner is 28 %. [Income Tax Act art 124](#)

32. Are there other taxes such as inheritance tax which have an important impact on own equity and retention of earnings decisions?

YES

Concerning inheritance taxation it is not tax efficient to increase corporations own equity because inheritors do have to pay inheritance tax according to the net property of the corporation. There are special rules which will reduce amount of inheritance taxation when inheritor will continue the business of the deceased. [Inheritance Tax Act art 11, art 14, art 55, art 56, art 57](#)

Income Tax Act 1535/1992

Business Income Tax Act 360/1968

Inheritance Tax Act 378/1940

Vat Act 1501/1993