The Private Wealth and Private Client Review

Eighth Edition

Editor
John Riches

The Law Reviews

THE PRIVATE WEALTH AND PRIVATE CLIENT REVIEW

EIGHTH EDITION

Reproduced with permission from Law Business Research Ltd
This article was first published in September 2019
For further information please contact Nick.Barette@thelawreviews.co.uk

Editor
John Riches

THE LAWREVIEWS

PUBLISHER
Tom Barnes

SENIOR BUSINESS DEVELOPMENT MANAGER
Nick Barette

BUSINESS DEVELOPMENT MANAGER
Joel Woods

SENIOR ACCOUNT MANAGERS
Pere Aspinall, Jack Bagnall

ACCOUNT MANAGERS
Olivia Budd, Katie Hodgetts, Reece Whelan

PRODUCT MARKETING EXECUTIVE
Rebecca Mogridge

RESEARCH LEAD
Kieran Hansen

EDITORIAL COORDINATOR
Gavin Jordan

HEAD OF PRODUCTION
Adam Myers

PRODUCTION EDITOR
Claire Ancell

SUBEDITOR
Neil Fanning

CHIEF EXECUTIVE OFFICER
Nick Brailey

Published in the United Kingdom
by Law Business Research Ltd, London
Meridian House, 34-35 Farringdon Street, London, EC4A 4HL, UK

www.TheLawReviews.co.uk

ISBN 978-1-83862-056-1

Printed in Great Britain by
Encompass Print Solutions, Derbyshire
Tel: 0844 2480 112

ACKNOWLEDGEMENTS

The publisher acknowledges and thanks the following for their assistance throughout the preparation of this book:

CHRISTIE'S

CONE MARSHALL LIMITED

CONYERS DILL & PEARMAN

DORDA RECHTSANWÄLTE GMBH

ELIAS NEOCLEOUS & CO LLC

ESTUDIO BECCAR VARELA

HANNAFORD TURNER LLP

HANNES SNELLMAN ATTORNEYS LTD

HASSANS INTERNATIONAL LAW FIRM

HAYNES AND BOONE, SC

HIGGS & JOHNSON

IQ EQ (ISLE OF MAN) LIMITED

LEE HISHAMMUDDIN ALLEN & GLEDHILL

LENZ & STAEHELIN

MAISTO E ASSOCIATI

MARXER & PARTNER RECHTSANWÄLTE

MCDERMOTT WILL & EMERY LLP

NAGASHIMA OHNO & TSUNEMATSU

NIJSDRAYE | ATTORNEYS AT LAW

O'SULLIVAN ESTATE LAWYERS LLP

P+P PÖLLATH + PARTNERS

PERCHSTONE GRAEYS LP

PERSPECTA TRUST LLC

POTAMITISVEKRIS

PRAXISIFM GROUP LIMITED

RECABARREN & ASOCIADOS

RETTER S.À.R.L.

RMW LAW LLP

RUSSELL-COOKE LLP

SOŁTYSIŃSKI KAWECKI & SZLĘZAK

SRS ADVOGADOS

STEP

STEPHENSON HARWOOD

SULLIVAN & CROMWELL LLP

TOGNETTI ADVOCACIA

UGGC AVOCATS

WITHERS LLP

WOLF THEISS

CONTENTS

PREFACE

In my foreword this year, I will focus on the continuing interest that is being devoted to the position of wealthy families and the markedly different approaches that prevail in Western Europe and the United States in terms of tax information exchange and anti-money laundering policy.

While public beneficial registers for companies will be introduced in the EU in the first quarter of 2020, the United States continues to pursue its own agenda where the primary focus of its anti-money laundering policy continues to be around financial institutions.

In broad terms, it is still accurate to say that the principal impetus for ongoing policy initiatives in this area is being driven by the EU, OECD and the Financial Action Task Force (FATF). This has been underlined by two important events in the past week or so as I finalise this foreword. Firstly, the decision of the UK Crown Dependencies[1] to voluntarily adopt public registers of beneficial ownership by 2023. Secondly, FATF's publication of its 2019 guidance for trust and corporate service providers (TCSPs) (the last version was published in 2008). I will return to both of these topics below but, in general terms, they underscore the sense of the 'transparency juggernaut' maintaining its momentum.

I will first deal with EU developments. The focus of activity here is the measures being introduced at Member State level to implement the Fourth and Fifth Anti-money Laundering Directives (4AMLD and 5AMLD, respectively). With some notable exceptions (including the UK, Malta Germany, Luxembourg, Portugal and Ireland), Member States have been quite slow to implement 4AMLD. In practice, implementation in other jurisdictions looks like it will be subsumed into the widened scope of 5AMLD.

So far as corporate registers are concerned, these are due to become public in the EU and wider EEA in early 2020 under 5AMLD (in the UK, the register was public from inception so the change here will be less marked). In the arena of trust registers, the scope of trusts that are within scope has been substantially expanded from those that generate tax consequences and those that are administered in the relevant jurisdiction. The Directive makes reference to 'express' trusts. There is significant uncertainty as to how this term will be construed as, on an expansive reading, it would require, in a UK context or co-ownership of land and joint bank accounts, to be reported. As a general proposition, trust registers are private and it would only be possible to gain access to the information on the beneficial owners of a trust where the applicant can demonstrate a legitimate interest.

It seems likely, from a consultation that has recently been launched by the UK government, that those seeking access to the trust register will have to demonstrate some

1 Jersey, Guernsey and the Isle of Man.

specific evidence of money laundering or terrorist financing activity to justify this. In essence, general 'fishing' expeditions by investigative journalists into the affairs of the wealthy will, hopefully, be discouraged.

Some curious features of the directive implementing 5AMLD have potentially wide-ranging consequences for trusts that are not regarded as resident in the EU or EEA. On a literal reading of the directive, it could be argued that such trusts will be required to register in circumstances where they have a business relationship with an obliged entity – this includes not only financial institutions but lawyers, accountants and other equivalent professionals. We will have to await the detailed regulations to see the final policy stance taken on this issue.

One other area where 5AMLD leads to a surprising outcome is in circumstances where a trust is deemed to control any company that is not incorporated within the EU or EEA. In these circumstances, the directive makes provision for public access to information about the trust; the logic here is that if the relevant company does not open up its information to public scrutiny then the trust that owns it should be disclosed instead. What is completely unclear at this stage is whether this will provide de facto public access to information about trusts that control non-EU or non-EEA companies or whether it will only afford such access in circumstances where the applicant already has detailed information about the relevant company or trust.

Another interesting issue that arises in Luxembourg, where a trust is the ultimate beneficial owner of a Luxembourg company, is that information about the settlor, beneficiaries, protectors and any other natural person exercising effective control will be publicly available on the corporate Register of Beneficial Owners from 31 August 2019. This is markedly different from the position under the UK Corporate register in the case of a trustee owner where the persons with significant control or 'PSC' rules look to those who control the trustee decisions alone rather than those who are beneficiaries of a trust.

The general scope of trust registers in the EU under 4AMLD is starting to become clearer. Following on from the UK and Malta, Ireland recently published its regulations at the end of January 2019. These regulations will, as noted, be potentially subject to material expansion once 5AMLD is implemented.

One general concept within 5AMLD is the proposal that trusts can be effectively passported; in other words, once the trust can evidence registration on one EU or EEA register, this will avoid the need for duplicate registrations. Whether this will result in any practical compliance gains or advantages remains to be seen. In terms of its scope, the information being provided on trusts in the centralised Beneficial Ownership Register will be restricted to information about individuals and will not address (as is the case with Common Reporting Standard (CRS)) asset values.

There are clear signs that the EU is intent upon exporting its concept of centralised trusts and corporate beneficial ownership registers to the rest of the world. Recent commentaries have suggested a move to a global standard in this regard by 2023. NGOs active in the transparency arena have started to advocate the creation of an overarching integrated global asset register for wealthy families although it is difficult to gauge policymakers' enthusiasm for such a radical step.

The position of the UK if Brexit finally happens is also interesting. The UK seems intent upon implementing 5AMLD and has shown no signs of losing its enthusiasm for expanding measures in this area along with its European neighbours. The UK has also been putting pressure on both its crown dependencies (CDs) and overseas territories (OTs)[2] to adopt the EU's position on public beneficial ownership registers for companies.

Before the CD's announcement on 19 June 2019,[3] it seemed that the OTs were more likely to agree to the EU's position because of their constitutional status where the UK has a stronger formal say in how they make policy. What is interesting about the CD's position is, in the statement issued by the three Island Governments on 19 June, they describe a three-stage process as follows:

> *1. the interconnection of the islands' registers of beneficial ownership of companies with those within the EU for access by law enforcement authorities and Financial Intelligence Units;*
> *2. access for financial service businesses and certain other prescribed businesses for corporate due diligence purposes;*
> *3. public access aligned to the approach taken in the EU Directive.*

It seems obvious that the CD's collective approach here is to forestall criticism from the EU in particular by being seen to take the lead in moving to public access in a phased manner. The fact that public access is the last stage of this process is revealing. The willingness in interim stages to share information with the EU and obliged entities in the regulated sector may well be a model that other jurisdictions will consider following.

Whether the voluntary adoption of public registers of beneficial ownership for companies in the CDs will stimulate other jurisdictions to follow suit remains to be seen. There have been some indications that the UK and EU stance here is to promote a new global standard of public registers for companies by 2023 mentioned above. Given the UK's pronouncements here, it seems inevitable that the OTs will be forced to adopt equivalent measures to the CDs. It will be interesting to see whether other major offshore jurisdictions such as Switzerland and the Bahamas will react to these events.

As a different matter, the separate subject of establishing centralised trust registers outside the EU is bound to be raised as a parallel issue. This may take longer to surface than pressure to establish corporate registers, but seems bound to raise its head at some stage.

From a wider FATF perspective, the key development in 2019 is the publication in late June 2019 of updated guidance to non-financial services professionals. Three sets of parallel guidance to lawyers, accountants and TCSPs[4] have been issued. There has been a significant time gap since the previous edition, which was published in 2008.

One area where the new guidance will have an important impact in the context of TCSPs is in defining 'beneficial ownership'. In this regard, the new guidance follows an expansive view of what constitutes 'control' for the purpose of beneficial ownership akin to the approach taken in the UK Trust Register. This will be potentially significant going forward in considering who needs to be disclosed in the context of trust structures in governance terms. In particular, holding powers as a minority member of a group or a veto power with respect not only to the appointment and removal of trustees but also to the addition and removal of beneficiaries, for example, will be enough to render an individual as being characterised as a 'natural person exercising effective control'. This is potentially very significant because there

2 A wider group that includes Bermuda, British Virgin Isles ,the Cayman Islands and Gibraltar.

3 https://www.gov.je/News/2019/Pages/BeneficialOwnership.aspx.

4 https://www.fatf-gafi.org/publications/fatfgeneral/documents/public-consultation-guidance-tcsp.html.

has been no guidance offered by FATF since it published its 2012 recommendations on how to interpret this expression.

It is still very early to try and discern what the impact of the information flows triggered under CRS has been. For compliant structures, the provision of CRS information should only confirm what has already been disclosed by a taxpayer to domestic tax authorities. However, given the growing concerns being expressed by politicians on the 'inequality' theme, the assembling of information about asset holding positions of wealthy individuals may be the tool that is deployed in assessing the potential impact of future wealth or inheritance taxes where these are not currently employed.

There is also a potentially significant crossover from the FATF domain into CRS reporting. In particular, a broader concept of who may be regarded as a 'controller' in the anti-money laundering context is likely to be applied for CRS purposes in due course, given the express linkage that exists in CRS that directly imports FATF definitions of beneficial ownership into the concept of who may be reportable in a trust context as a 'controlling person'.[5] This could, in particular, lead specifically to the disclosure of family members who have more subtle or 'indirect' means of influence over a family trust structure.

One development in an aligned field worth mentioning is the rules on substance for entities incorporated in offshore jurisdictions. These substance rules have taken on an increased significance recently.

The EU Council has created a code of conduct for business taxation to limit the impact of low tax regimes. In 2017, it established a code of conduct group tasked with considering the measures on business tax within a number of non-EU jurisdictions.

In response to assessments undertaken by the EU, the affected jurisdictions (which include a number of the CDs and OTs) have introduced new rules requiring economic substance that will take effect in 2019.

These rules impact companies carrying on 'relevant activities'. The substance requirements have three principal components. These are to demonstrate, that within the jurisdiction, the company:

a is directed and managed;

b undertakes core income-generating activities; and

c has physical presence.

While these measures are primarily relevant in a base erosion and profit shifting (BEPS) context, they are indicative of wider trends in terms of being able to demonstrate the overall substance of these measures that are operated in offshore jurisdictions. This is of potentially greater significance to private wealth structures that may be seen as more passive than active.

There are nine relevant activities that cover banking, insurance, fund management and financing. One specific area includes the role of pure equity holding companies (PEHs). While supposedly aimed at private equity structures, it could conceivably impact a conventional holding company holding varied investments for a family trust.

At this early stage, there is no clear guidance that delineates the boundaries of what constitutes a PEH; what can be said is that family structures could find themselves impacted if the guidance is couched in wide terms.

5 See page 59 of OECD publication in commenting on meaning of 'controlling person' for CRS purposes.

There is no doubt that the increased cost and complexity of regulation is driving trends towards simpler structures with fewer layers and involving fewer jurisdictions. There appears to be a greater reluctance on the part of corporate service providers to offer a purely passive role as a registered office without any detailed understanding of the operation of the underlying entities themselves. This appears to be coupled with a trend towards re-domiciling entities into jurisdictions where substance can be demonstrated.

At the same time, an increasing awareness as to the implications of disclosure of beneficial ownership is also generating a more reflective view on the retention of control either by settlors or by beneficiaries or connected family members.

In summary, therefore, the theme of ever-greater levels of transparency and increased complexity of overlapping regulation continues. The dichotomy between Western Europe and the United States, in terms of their different approach to these issues, also remains very apparent to observers.

John Riches
RMW Law LLP
London
August 2019

Chapter 16

FINLAND

Johan Hägerström and Stefan Stellato[1]

I INTRODUCTION

Finland is a northern European country with a population of 5.5 million, a substantial portion of which lives in the metropolitan area in the south of the country, including the Finnish capital Helsinki. Finland joined the European Union in 1995 and was among the first Member States to adopt the euro in 1999. Finland's geographical position as a western European market economy and a stable parliamentary democracy sharing a long border with Russia is unique and has shaped the history of the country. In 2017, Finland celebrated the centenary of its independence from Russia. Finland is now one of the safest and least corrupt countries in the world, with a high standard of living and a high degree of income equality. It also boasts a world-renowned school system, contributing to most Finns having a very good command of English. Finland is the home of a significant Swedish-speaking minority and the country has two official languages, Finnish and Swedish.

The success of the cell phone and networks manufacturer Nokia Corp, along with a number of high-tech companies, was a major factor contributing to a long period of strong economic growth that Finland enjoyed in the 1990s and 2000s. Finland has, on the other hand, suffered heavily from the recent financial crisis, which coincided with a sharp decline in Nokia's businesses, as well as a downturn in trade with Russia. This combination lead, inter alia, to a very slow recovery in terms of GDP growth and to Finnish long-term debt being downgraded from its previous AAA-rating by all major credit agencies. Now that Finland has recovered from the financial crisis, it is struggling with increasing levels of national debt and an ageing population.

The Finnish economy was dominated by agriculture until the 1950s, and rapid industrialisation and growth took place during the following few decades. Since the 1970s, Finland has been among the wealthiest countries in the world. Finland is a Nordic welfare state, characterised by free market capitalism combined with a significant public sector, large-scale income redistribution and high tax rates. Because of these factors, wealth is quite evenly distributed among Finns and Finland is home to relatively few high net worth individuals (HNWIs).[2]

1 Johan Hägerström is a senior associate and Stefan Stellato is an associate in the tax group of Hannes Snellman Attorneys Ltd in Helsinki.

2 The former mobile phone manufacturer Nokia (and the Nokia cluster as a whole) generated a handful of HNWIs, but over the past years HNWIs generated by the gaming industry have received more attention.

Despite, for example, a broad network of tax treaties, the Finnish high-tax environment is, perhaps, unlikely to attract HNWIs to Finland. Other factors, such as safety, northern nature, stable institutions, low corruption and a renowned education system are, in this regard, more important assets for Finland.

II TAX

i Recent developments

One issue that stands out particularly clearly in the recent developments of Finnish tax law is the ever-increasing disapproval of tax avoidance and planning, as manifested also on an international level by the Organisation for Economic Co-operation and Development (OECD) and EU actions against such activities. In addition, the reputational damage to persons and companies engaging in tax avoidance and planning has grown. Finnish persons and companies involved, for instance, in matters concerning the LGT Bank in Liechtenstein or in arrangements published in the 'Panama Papers' are likely to agree.

As a main rule, tax-related information is secret, including, for example, rulings and tax returns. However, taxable income and taxes payable (as determined in the annual tax assessment) are public information in Finland. Unsurprisingly, access to this information attracts significant media attention, and each year the media publishes listings on the income and effective tax rates of high-income people and companies. Because of the fact that not all tax-related information is public (e.g., later decisions amending the taxation of a given year remain secret) and that tax-exempt income and income routed to personal holding companies do not show in the statistics, these listings may be somewhat misleading.

The worsening of the general tax atmosphere can also be seen in that the Finnish general anti-avoidance rule (GAAR) is being applied ever more frequently. The GAAR now appears to be engaged in attacking practices that were previously widely considered acceptable. The Tax Administration is, for example, broadly questioning the deductibility of intra-group interest expenses in corporate taxation and closely scrutinising various holding and personal services company arrangements.

Another general trend in Finnish taxation over recent years is the increase of both tax rates and progressiveness. To name a few examples, the tax on capital income, which for a long time was proportional, became progressive in 2012. New tax brackets have been added at the high end of the scale for earned income, gift and inheritance tax, although all of these taxes have recently been slightly reduced.

A reverse trend can be discerned in the taxation of corporations – the corporate income tax rate has gradually decreased and the present 20 per cent rate was introduced in 2014. The focus of taxation is also shifting from taxation of income to the taxation of consumption, and the standard VAT rate is 24 per cent. Taxation with underlying environmental or health-related goals is common, for example, within excise taxation.[3] Finland levied a wealth tax for a long time, until it was eliminated in 2006. At about the same time, the avoir fiscal dividend tax system was abolished because of its incompatibility with EC law.

Legislative amendments that enter into force in 2020 aim to better align the tax treatment of different forms of investment. The amendments include the abolishment of the

3 EU rules on state aid forced Finland to abolish its recently introduced sweets tax, an excise tax, from the beginning of 2017.

possibility to withdraw invested capital from insurance wrappers without triggering taxation, the introduction of a share saving account and broad changes to the taxation principles concerning investment funds.

Finally, Finland had a parliamentary election in April 2019, which the Social Democratic Party won with a margin of just one or two seats over the more right-leaning Finns Party and the National Coalition Party. Nevertheless, the new government is much more left-leaning than its predecessor and during the negotiations to form it, even quite radical tax-related proposals were discussed. Such proposals included, for example, reintroduction of a wealth tax, abolishment of generation shift reliefs, exit tax for individuals, increased tax on dividends from unlisted companies, withholding tax targeted at foreign institutional investors, meat tax, etc. However, the governing parties could reach an agreement to advance only part of the proposals and it seems safe to assume that even less will actually be implemented.

ii International agreements

Finland has a wide network of bilateral tax treaties. Finnish tax treaties typically follow the OECD Model closely and most of them provide for double taxation relief through the credit method. A number of Finnish tax treaties contain provisions that extend the taxing rights of Finland for a number of years after a Finnish citizen moves abroad.

Finland has recently renegotiated its outdated tax treaties with, inter alia, Germany, Spain and Portugal. The new treaty with Germany has been applied since 2018, and the one with Spain as of 2019. Renegotiation of the treaties, especially with Spain and Portugal, was the result of increasing media attention towards high-income individuals moving to Spain or Portugal to avoid tax on their private-sector pensions, as the relevant treaty did not allow Finland to tax such pensions. The Finnish government terminated its current tax treaty with Portugal with effect from 2019 to put pressure on the country, which was not working sufficiently to have the new treaty accepted nationally. Therefore, there is currently no applicable tax treaty between Finland and Portugal.

Finland is a signatory of the Nordic Multilateral Tax Treaty, which is a multilateral double taxation convention largely based on the OECD Model Tax Convention.[4] Finland is also among the countries that signed the OECD Multilateral Instrument (MLI) in June 2017. Finland included most of its tax treaties as covered agreements, but made broad reservations to the applicable provisions. Consequently, it is expected that the most important practical effects of the MLI will be the introduction of the principal purpose test and mandatory arbitration procedure. The MLI will be applied as of 2020 at the earliest.

The EU's Anti-Tax Avoidance Directive (ATAD) and its 2017 amendment (ATAD II) oblige Finland to make significant amendments to its national laws. Significant amendments were made especially to the interest-deduction limitation and controlled foreign corporation (CFC) rules, which were among the rules that must be introduced as of 2019.

Finland has an agreement with the US to exchange information under the US Foreign Account Tax Compliance Act. Finland has also agreed on automatic exchange of information in the context of the OECD Common Reporting Standard (CRS), implemented at the EU level through the DAC2 Directive (2014/107/EU). Finland is among the countries that started reporting in 2017. Since 2017, Finland requires, based on OECD and EU transfer pricing initiatives, multinational groups with revenues exceeding a certain global threshold

4 The signatory countries of the Nordic Multilateral Tax Treaty are Denmark, Finland, Iceland, Norway and Sweden.

to file country-by-country reports. In addition, the DAC6 Directive rules on mandatory disclosure will set an obligation for taxpayers and intermediaries to report, in particular, tax-driven cross-border arrangements with the first exchange of information taking place in late 2020.

In 2016, in a case related to the LGT Bank/Liechtenstein tax affair, the Supreme Administrative Court ruled that documents received from a foreign authority may be taken into account as evidence, even if it is possible that the documents were obtained through a criminal act.

iii Income tax

Two categories of tax liability exist in income taxation: unlimited and limited tax liability. People that reside in Finland (as defined in the Income Tax Act) are subject to unlimited tax liability and pay tax on their worldwide income. Conversely, people who do not reside in Finland are subject to limited tax liability and pay Finnish taxes solely on their Finnish-sourced income, as defined in the Income Tax Act.

A three-year rule applies to Finnish citizens when they move abroad. Under the rule, a Finnish citizen is considered a Finnish tax resident during the year of emigration and for the subsequent three calendar years, leading to tax liability for both Finnish and foreign-sourced income. However, if the person establishes, to the satisfaction of the tax authority, that no 'close ties' to Finland remain, Finnish tax non-residency (and limited tax liability) may begin before the end of the three-year period. This three-year rule does not apply to foreign citizens.

Taxable income is calculated separately for earned income and capital income. Capital income is income generated through the possession of wealth and earned income is defined as all other income. Earned income is typically salaries, directors' fees or benefits in kind and is taxable at progressive rates of up to approximately 55 per cent. Capital income is taxable at a rate of 30 per cent up to €30,000 per calendar year and the excess at a rate of 34 per cent.

Taxable income for all entity types is assessed separately under three different acts, depending, among others, on if the source of the income is employment, business or farming. Losses from one source of income may not be offset against another source of income, apart from in rare exceptions. The system will be simplified somewhat by taxing most corporations exclusively under the business income source as of tax year 2020.

Capital gains are generally taxable at the capital income tax rate of 30 or 34 per cent. Some capital gains are exempt, including the sale of a house or apartment that has been used as a permanent home for two consecutive years.

The extensive taxation of capital gains creates an incentive for persons with inherent capital gains to move abroad and realise the gains while no longer subject to Finnish unlimited taxation, or at least resident in another state under the applicable tax treaty. However, moving abroad before realising a significant capital gain requires careful examination of the applicable tax treaty and tax law provisions, including the above-mentioned three-year rule.

Interest income is also taxable at the capital income tax rates. However, interest paid on deposits in Finnish bank accounts and Finnish bonds is subject to a final tax at source at a flat rate of 30 per cent. As far as interest expenses are concerned, deductions are generally granted only where interest is paid with an aim to obtain taxable income. The interest on loans to buy a permanent home was, however, fully deductible until 2012, when the deductible portion started a gradual decrease and there are now plans to remove the deduction entirely in the future.

The taxation of dividend income is very complex, and the tax rates range from approximately 7.5 per cent to above 55 per cent. These discrepancies highlight the importance of careful tax analysis, but may also offer significant tax advantages. Examples of factors that may have an impact on the applicable tax rate are whether the company distributing the dividend is listed, the value of the company's net assets, the place of incorporation and on what basis the amount of the dividend is determined.

As far as natural persons resident in Finland are concerned, the least tax is payable when receiving from an unlisted company a dividend that meets two conditions: it equals less than 8 per cent of the shares' calculated mathematical value and is less than €150,000 in a calendar year. When these requirements are met, 75 per cent of the dividend is exempt and 25 per cent is taxed as capital income, leading to a tax rate of around 7.5 to 8.5 per cent. At the other extreme are, among others, dividends paid in place of wages and dividends paid by companies in non-EU/EEA and non-treaty countries. Such dividends are fully taxable as earned income at progressive tax rates of up to approximately 55 per cent.

Limited liability companies and certain similar types of companies are subject to 20 per cent corporate income tax on their profits. Cross-border restructurings may trigger exit taxation where assets are, in one way or other, transferred outside the reach of Finnish taxation. In the case of exchange of shares, the tax deferral allowed is forfeited, if a person who has been granted shares in consideration moves his or her residence, as intended in the relevant tax treaty or national laws, outside the EEA within five years after the end of the year in which the exchange of shares was carried out.

Finland originally introduced a CFC rule in 1995 and an interest-deduction limitation rule in 2014, which were both tightened as of 2019 owing to the ATAD. Under the current CFC rule, Finland taxes the income of a foreign entity if a Finnish taxpayer, either alone or together with its related parties, has, directly or indirectly, at least 25 per cent of votes, ownership, right to capital or right to profits or assets, and the foreign entity's effective tax rate is less than three-fifths of that calculated under the Finnish rules. An entity within the EEA may escape the CFC rule if it carries out actual economic activities. An entity outside the EEA may also escape the CFC rule, but it must meet more criteria.

iv Gift and inheritance tax

Inheritance or gift tax is payable, if the place of residence of the decedent or donor, or the place of residence of the beneficiary or donee, was in Finland at the time of death or donation. In addition, tax must be paid on Finnish real property and on shares in any corporate body in which more than 50 per cent of the assets consist in Finnish real property, even if both the decedent or donor and the beneficiary or donee resided overseas.[5] Only inheritances that are at least €20,000 and gifts that are at least €5,000 are subject to tax.

Inheritance tax is assessed on each beneficiary's net portion of the estate. Tax is payable on portions that are at least €20,000, but widows may deduct an additional €90,000 and minors in immediate lineal descent an additional €60,000 from their portions.

For the purposes of both inheritance and gift tax, the value of any rights of possession is deducted from the beneficiary's portion, if such a special possession has been provided for in a will or a deed of gift. The value of the right of possession is not as such taxable, but income derived from the right of possession constitutes taxable income. For example, the title of a

5 This extended definition of real property is also found in some other tax laws and in tax treaties.

house may be donated to person A, but the donor may retain the right to use the house. In this case, person A is taxed on the value of the house less the value of the possession right (calculated according to a formula) and the donor is taxed only on income received from the right of possession (e.g., rental income). However, person A may deduct as their acquisition cost the value of the house including the value of the possession right in the capital gains taxation upon a subsequent disposal.

Both gift and inheritance tax have two brackets – the lower tax bracket I applies to close relatives and the higher tax bracket II applies to more distant relatives and to beneficiaries and donees that are not relatives of the decedent or donor.[6] The taxes are progressive within both brackets. As an example of the applicable rates in 2019 in tax bracket I, the tax payable on an inheritance portion of €200,000 is €21,700. An inheritance portion of €1 million is subject to a tax of €149,700 at the lower limit of €1 million and at 19 per cent on any part exceeding €1 million. In tax bracket II, rates are roughly double those of bracket I.

The Inheritance and Gift Tax Act leaves considerable room for tax planning. It may, for example, be wise to pass down property to a greater number of beneficiaries to multiply recipient-specific allowances and thresholds, but also to mitigate progressivity. The same goals may be obtained by skipping generations by willing or donating property to, for example, grandchildren.[7] Rights of possession are also frequently retained to lower the valuation of the donated property and hence the payable gift tax.

There are, however, rules aimed at curbing tax planning. Gifts received from the same donor during a three-year period are aggregated. Loans with no intention to pay back and sales at less than 75 per cent of fair market value are subject to gift taxation. There is also an exception to the general rule, according to which the donee may use the gift tax value as their acquisition cost – if the donee disposes of the gift within one year from receipt, the acquisition cost will be the donor's original acquisition cost. Also, in inheritance taxation the value for inheritance tax purposes becomes the beneficiary's or heir's acquisition cost, but there is no one-year rule, such as the one in gift taxation.

The media regularly brings to the public's attention cases where people move abroad with the aim to avoid gift or inheritance tax. Finland's neighbours Sweden and Norway, which levy neither inheritance nor gift tax, are particularly attractive from this point of view. However, among others, the tax provisions concerning Finnish real property and Finnish real estate holding companies place hurdles for such tax planning strategies.

The Income Tax Act and the Inheritance and Gift Tax Act provide for relief for certain transactions that aim at passing a business or a farm to the next generation. The relief is implemented, for example, through favourable valuations in inheritance and gift taxation, non-taxation of capital gains, allowing sales at 50 per cent of fair market value without triggering gift taxation or longer tax payment times. The types of relief depend on the way in which the change of generation is carried out and on whether relief is granted under the Income Tax Act or the Inheritance and Gift Tax Act.

6 Tax bracket I for gift and inheritance tax purposes includes, among others, the donor's or the decedent's spouse or registered partner, any heir in lineal ascent or descent and any heir of the spouse in lineal descent. As a general rule, cohabitants come under tax bracket II, but they may come under tax bracket I, for example, if they have earlier been married or have a child together.

7 Wills may be, partially because of their flexibility, an attractive tool for inheritance tax planning. For example, suspensive conditions that give ownership rights to the beneficiary only after certain conditions are fulfilled have been used to create an interim ownerless period and thus defer the payment of inheritance tax. It should be noted that this strategy has obvious pitfalls.

Relief is subject to various conditions, which include that at least 10 per cent of the activity is transferred and the activity is continued by the transferee after the transfer. A further sale of a company, farm or other business that has been transferred to the next generation in a transaction enjoying change of generation relief leads to forfeiture of the relief and to a penalty payment if the sale occurs within five years of the purchase agreement or the tax assessment in which the relief was granted.[8] The tax provisions on change of generation transactions are a politically highly sensitive topic in Finland.[9]

v Property and transfer taxes

Owners of real property pay real estate tax, which is typically around 1 per cent of the value of the real estate per year. When acquiring real estate, a transfer tax of 4 per cent is payable by the purchaser. The transfer tax rate applicable to housing and real estate companies is 2 per cent, in which case the tax base also includes certain loans of the company, and 1.6 per cent for other shares. No transfer tax is generally payable on listed shares or assets received as a gift or inheritance.

III SUCCESSION

i Legal implications of marriage, registered partnership and cohabitation

Marriage and registered partnership have almost identical legal effects, the main differences being that the possibilities to take the other partner's last name and adoption are more limited in registered partnerships. Cohabitation, in turn, does not create any immediate legal rights or obligations. The possibility to conclude new registered partnerships ended in March 2017, when legislation allowing same-sex marriages entered into force. Existing registered partnerships can now be turned into marriages with a notification.[10]

Marriage does not cause changes in the ownership of property. Nor is there liability for debt taken by the other spouse, but there may be joint liability for debt taken for the maintenance of the family. The common home is protected by requiring both spouses' consent to its sale, even where owned by one spouse alone.

A petition for divorce may be filed by the spouses jointly or by only one of them. The reasons for divorce are not examined. Upon granting a divorce, normally after a reconsideration period of six months, one of the spouses may be ordered to pay maintenance to the other spouse, if deemed equitable.[11]

8 Until 2017, a further sale at a later point was treated favourably: the capital gain was calculated using as the acquisition cost the full fair market value at the time of the generation-shift transfer (and not the actual taxable value that was lowered based on the above-discussed reliefs). This rule was changed as of 2017 and the capital gain is now calculated using as acquisition cost the (lowered) taxable value that was actually applied.

9 One common argument against taxes on inheritances is that they endanger the prerequisites to continue a business, especially where the transferred business has no liquid assets that could be used to pay the tax due.

10 Because of significant similarities (see the text below), references to marriage also apply to registered partnerships.

11 Since 2011, there is a somewhat limited possibility to receive compensation also upon a cohabitation separation if one partner has assisted the other in accumulating property over a long period.

At divorce, the net marital property is totalled and divided into two in order to determine the share of each spouse. The spouse with less property receives an equalisation payment, which is tax exempt, from the other spouse so that each spouse leaves the marriage with the same amount of what used to be matrimonial property.

However, prenuptial agreements cover around a third of all marriages and they frequently entirely remove the duty to make equalisation payments. Some flexibility as to how a prenuptial agreement is drafted is allowed and it is, for example, quite common to provide that the agreement shall apply only at divorce (but not death of a spouse) or that the prenuptial agreement only affects property accumulated before the marriage. In order to be effective, a prenuptial agreement must be concluded in writing, dated, signed, attested and registered by the local register office.

ii Intestacy and wills

Finland is a signatory of the Nordic Convention of 19 November 1934 concerning Inheritance, Testamentary Dispositions and the Administration of Estates of Deceased Persons between Denmark, Finland, Iceland, Norway and Sweden. In 1976, Finland joined the Hague Convention of 5 October 1961 on the Conflicts of Laws Relating to the Form of Testamentary Dispositions.

As an EU Member State, Regulation No. 650/2012 on international successions is of particular importance for Finland. This Regulation governs issues such as applicable law, recognition and enforcement of decisions and the creation of a European Certificate of Succession. It brings more choice, simplicity and clarity to cross-border successions and is binding on most EU Member States.[12]

In some situations, gifts and other payments received during the decedent's lifetime are taken into consideration in determining the size of the estate to be distributed. After a married person passes away, a division of property is carried out between the spouses. Thus, if the decedent's net assets exceed the net assets of the surviving spouse, the death estate makes an equalisation payment to the surviving spouse. No inheritance or gift tax is due on equalisation payments. A surviving spouse with more net assets than the decedent may decide not to make an equalisation payment to the estate of the deceased person. No division of property is carried out if the spouses' marital rights in each other's property have been removed through a prenuptial agreement.

In the case of intestacy, the children inherit the whole estate even if the decedent was married. If there is no spouse and there are no children, the parents inherit everything, and if there are no living parents, the decedent's brothers and sisters inherit.

A will can be used as a tool to choose the heirs and give them either a share of the estate or a legacy. As a main rule, for a will to be effective, it has to be made in writing and signed in the presence of two witnesses. Direct descendants are protected by a forced heirship regime that gives them the right to claim a reserved portion that equals half of the share that they would have received absent the will. The surviving spouse is protected almost invariably through retention of possession (but not ownership) of the undivided common home.

12 Denmark, Ireland and the UK do not participate in the Regulation.

IV WEALTH STRUCTURING AND REGULATION

i Wealth structuring vehicles

Finnish law does not recognise the common law institution of trust.[13] In addition, the use of foundations for wealth structuring purposes is very limited, because foundations are typically required to have a charitable purpose and they are subject to strict supervision enforced with even criminal sanctions. Limited partnerships, on the other hand, are mainly used by private equity investors and in other circumstances where the features of a transparent entity are desirable.

Thus, the most common vehicle for wealth structuring remains the limited liability company. As the taxation of dividends in the hands of an individual shareholder is affected by the value of the dividend-distributing company's net assets, accumulating property in a limited liability company is often advantageous from a tax perspective.[14] Setting up a limited liability company is very straightforward and, as of July 2019, there is no required minimum incorporation capital. At least one member of the board has to reside within the EU or the EEA, unless a special permission is granted.

Another reason why corporations are an attractive vehicle for accumulating wealth is that invoicing through personal service companies or holding companies, especially in the field of professional services, may to some extent be used as an alternative to receiving the same amount of income as wages. As discussed above, earned income is taxed at rates of up to approximately 55 per cent, whereas the tax burden when charging through a corporation may be more modest – the corporate tax rate is 20 per cent and dividend distributions are often taxed at only 7.5 per cent. Depending on the circumstances, there might not even be a need to distribute dividends, resulting in ulterior tax savings.

Legislative amendments aiming to better align the tax treatment of different forms of investment will apply as of 2020. The amendments introduce a share saving account, which allows private persons to invest a maximum of €50,000 in listed shares and to benefit from a tax deferral on dividend income and capital gains.

The legislative amendments will also impact insurance wrappers, the attractiveness of which will be reduced by, for example, abolishment of the possibility to withdraw invested capital without triggering taxation and by complete forfeiture of tax deferral when the policy owner yields too close control over the assets. In the past years, insurance wrappers have been a popular tax planning strategy even among the general population.

Finnish investment funds are contractual funds and are currently automatically exempt from corporate income tax. As of tax year 2020, however, they will have to meet certain conditions related to, for example, a minimum number of unit holders and open-endedness to maintain tax exemption. HNWIs, who tend to choose limited liability companies or insurance wrappers, rarely use Finnish investment funds as wealth structuring vehicles. For many HNWIs, foreign private funds could be a more attractive alternative especially after the 2020 amendments.

13 There is, however, some case law, e.g., regarding foreign trusts and their treatment in Finnish taxation.

14 As noted above, the taxation of dividends in Finland is very complex. Another factor affecting the use of a Finnish holding company is that dividends from unlisted companies within the EU/EEA, regardless of ownership, and dividends from listed companies within the EU/EEA, subject to a holding requirement of at least 10 per cent, are generally tax exempt. There are no similar exemptions if the shares are held by an individual personally.

ii Regulation of financial service providers and prevention of money laundering

Marketing and offering of services in Finland by investment firms and fund managers of UCITS or alternative investment funds require prior registration with the Finnish Financial Supervisory Authority, which is also the supervising authority. When marketing is directed to non-professional investors (retail investors), certain additional requirements, such as providing key investor information documents and the Consumer Protection Act, apply. The definition of a professional client under the Investment Services Act is based on MiFID II requirements.

Finnish legislation on the prevention of money laundering is largely based on international standards, which include the EU's Anti-Money Laundering Directives, which are based on recommendations of the Financial Action Task Force. The 4th Anti-Money Laundering Directive was implemented into Finnish legislation by the recast Act on the Prevention of Money Laundering and Financing of Terrorism (AML Act) and the Act on the Financial Intelligence Unit. Finland has transposed the 5th Anti-Money Laundering Directive into national law, but some of the transposing measures apply from 10 January 2020. Requirements under the AML Act apply to, inter alia, investment firms, fund managers, credit institutions and other entities offering financing in Finland. The duties include identification and verification of customers, ongoing monitoring of customer relationships, record-keeping, detecting and analysing suspicious transactions and reporting suspicious transactions to the Financial Intelligence Unit, which operates in connection with the National Bureau of Investigation. Violations are subject to administrative and criminal sanctions, and negligence towards the obligations may lead to corporate criminal liability and criminal liability for individual employees. Money laundering offences are sanctioned in the Penal Code.

V OUTLOOK AND CONCLUSIONS

The continuously increasing exchange of information is a clear trend in Finland. The Finnish authorities are receiving a substantial amount of information from international exchange of information arrangements, and this flow of information has already lead to some investigations concerning the taxpayers affected. In the absence of an effective voluntary disclosure policy, it has been less popular among Finnish taxpayers to disclose unreported overseas assets on a voluntary basis. In addition, the DAC6 Directive rules on mandatory disclosure will set an obligation for taxpayers and intermediaries to report especially tax-driven cross-border arrangements with the first exchange of information taking place late 2020. Attorney-client privilege could exempt tax advisors that are attorneys from mandatory disclosure requirements.

As far as tax planning is concerned, the generation-shift reliefs, as well as holding company and personal service company arrangements, may present attractive opportunities, but careful planning is essential, as tax planning is becoming less tolerated than before. The GAAR is being interpreted ever more broadly and new measures against tax planning are introduced. Implementation of OECD Base Erosion and Profit Shifting proposals and EU legislation against tax avoidance and aggressive tax planning, chiefly ATAD and ATAD II, is very topical. The tax treatment of different forms of investment will be aligned as of 2020, limiting for example the tax benefits of insurance wrappers. As ever-fewer tax planning alternatives remain available and, for example, because Finland levies inheritance tax, moving abroad may at present be a relatively effective planning strategy.

There has been a small shift from taxation of income to taxation of consumption and the new government has signalled that this will continue to be the emphasis. Above all, the new government has signalled a strong appetite to tackle tax planning with measures, which could be difficult to foresee. What is clear is that Finland will remain a high-tax jurisdiction for individuals, but other factors for which Finland is well known, such as institutional stability, low levels of corruption, good education and a clean environment, are also likely to stay.

ABOUT THE AUTHORS

JOHAN HÄGERSTRÖM

Hannes Snellman Attorneys Ltd

Johan Hägerström is a senior associate in the Hannes Snellman tax group. He advises clients particularly in matters related to private wealth, cross-border relocation and tax litigation. He has also past experience as an in-house tax counsel and private wealth structurer working in Luxembourg, as well as a tax advisor at KPMG Finland.

STEFAN STELLATO

Hannes Snellman Attorneys Ltd

Stefan Stellato is an associate in the Hannes Snellman tax group. Prior to graduation from the University of Helsinki, he spent a semester studying at university in New York. Besides his master of laws degree, he holds a master of science (economics and business administration) degree from Hanken School of Economics in Helsinki.

HANNES SNELLMAN ATTORNEYS LTD

Eteläesplanadi 20
00130 Helsinki
Finland
Tel: +358 9 228 841
Fax: +358 9 177 393
johan.hagerstrom@hannessnellman.com
stefan.stellato@hannessnellman.com
www.hannessnellman.com

Law
Business
Research

ISBN 978-1-83862-056-1