Finland

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General

1. What are recent tax developments in your country which are relevant for M&A deals?

The most relevant recent developments in Finland relate closely to the BEPS project. Interest deduction limitations that entered into force in 2014 have impacted the structuring of the deals. Additionally, the Finnish Tax Administration has become more aggressive in challenging existing structures and arrangements which place taxpayers in a position to evaluate and document their actions more prudently.

Especially the developments in taxation have caused changes to means of financing. Recent case law has reduced attractiveness of PIK loans provided by private individuals. In private equity deals, partnership loans have been replaced by preference shares. Moreover, different kinds of bond instruments have become more frequent means of external financing.

2. What is the general approach of your jurisdiction regarding the implementation of OECD BEPS actions (Action Plan 6 specifically) and, if applicable, the amendments to the EU Parent-Subsidiary Directive?

Finland has been active in putting the BEPS actions into practice. Finland already has restrictions on deductibility of interest and CFC legislation in place. Additionally, Finland has committed to implement country-by-country reporting.

New provisions of the Parent-Subsidiary Directive have been implemented in Finnish tax law with effect from the beginning of 2016. The amendments included a Limitation-On-Benefits (LOB) rule and a General Anti-Abuse Rule (GAAR).

The LOB rule tackles the situation in which payments are treated as deductible expenses in the source Member State and as a tax exempt dividend in the recipient Member State. As an exception to the general rule of tax exemption of dividends provided by the Parent-Subsidiary Directive, the dividend is taxable if either one of the following two conditions are met:

- The payment is deductible for the distributing company; or
- The arrangement in question has as a main purpose or as one of the main purposes to obtain tax benefits and the arrangement is not genuine having regard to all relevant facts and circumstances.

The general anti-abuse rule introduces a principal purpose test, providing that the arrangement is considered not to be genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality.

3. What are the main differences among acquisitions made through a share deal versus an asset deal in your country?

a. Share deal

A share deal may be less preferable from the buyer's perspective for two reasons. Firstly, the transfer tax of either 1.6% or 2.0% of the acquisition price is levied on the transfer of other than publicly traded shares in Finnish companies. If the value of the company is mainly based on other aspects than the securities or real estate it owns, then the basis for transfer taxation can be significantly higher in comparison to an asset deal.

Secondly, the buyer cannot depreciate the acquisition cost of shares. However, the depreciation of target assets may be continued within the company according to the depreciation plan applied by the seller.

In a share deal, previous losses of the target company may be lost (or retained) after a qualified change in ownership. Please see section 8 below for further details regarding this aspect.

Under Finnish VAT legislation, there is no VAT due on share deals.

b. Asset deal

An asset deal is generally preferable from the buyer's perspective. The acquisition cost is allocated to the acquired assets often resulting in a step-up in the book values of the assets in question. The buyer may begin to make depreciations on these new values (in accordance with general depreciation rules). The purchase price may also be allocated to goodwill, which may also be depreciated.

A transfer tax of 1.6% for Finnish non-listed securities, 2.0% for housing or real estate companies and similar, and 4.0% for Finnish directly-owned real estate is levied in cases where these assets are included in the acquired assets. With regard to real estates, transfer in the form of shares is therefore more advantageous than transferring the real estate directly.

Another drawback is that tax losses may not be transferred in an asset deal.

An asset deal is out of scope of VAT when it fulfills the requirements set out in the VAT legislation. A case-by-case analysis is usually required.

Buy-side

4. What strategies are in place, if any, to step up the value of the tangible and intangible assets in case of share deals?

No special provisions in the Finnish tax law provide for a step-up in the value of the target's underlying assets upon the acquisition of its shares. The acquisition cost of the shares is deductible from sales proceeds if the shares are later sold by the purchaser (unless a participation exemption applies – see section 15 below for further details).

5. What are the particular rules of depreciation of goodwill in your country?

For tax purposes, goodwill (i.e. the difference between the target's book value and the purchase price paid for it that cannot be specifically allocated to other assets) is regarded as an intangible asset that cannot be separately disposed of or sold. In an asset deal the possible purchase price paid for goodwill is depreciable during the probable economic impact period of goodwill (maximum ten tax years). The value of the goodwill is allocated to the number of years and the depreciated amount remains the same each year.

In a share deal the goodwill cannot be amortised or depreciated for tax purposes– the entire shares acquisition cost usually becomes deductible only in a subsequent transfer.

6. Are there any limitations to the deductibility of interest on borrowings?

There is a limitation on the deductibility of intra-group interest expenses. Limitations concerning the tax deductibility of interest payments have been applicable to corporations, partnerships, corresponding foreign entities and their permanent establishments as of the fiscal year 2014. The limitations are applied only if the interest expenses exceed the interest income received by the company. A general safe haven of €500,000 is applied if net interest expenses (including third party and related party interests) exceed €500,000; the interest limitation will nevertheless be applied to the entire amount.

Interest may become non-deductible if such net interest expenses exceed 25% of the company's tax EBITDA (taxable business profits added with the aggregate amount of interest costs, depreciations and group contributions received, and deducted with the amount of group contributions granted).

Interest payments for third party loans will not be affected. However third party loans will be deemed as intra-group loans if a related party pledges a receivable to an unrelated party as security for the loan and the unrelated party provides a loan to another related party, or the loan from an unrelated party is de facto a back-to-back loan from a related party. Further, interest expenses will remain fully deductible if the equity ratio of the company is equal to or higher than the consolidated equity ratio of the group.

The regulation allows an indefinite carry forward of interest expenses that cannot be deducted based on the above-mentioned restrictions.

In addition, transfer pricing provisions, general anti-avoidance provision and the provision on hidden profit distributions in Finnish domestic law may be applied to deny tax deductibility of interest expenses.

In most cases, no withholding tax is levied in Finland on interest payments to non-resident companies based on domestic law.

7. What are usual strategies to push down the debt on acquisitions?

The use of a Finnish Special Purpose Vehicle (SPV) by a foreign buyer to acquire a Finnish target is the preferred strategy to push down debt for most acquisitions. The SPV is financed by a loan from a foreign group company, which is often located in a jurisdiction with a low corporate income tax rate. As the deductibility of related party interest expenses has been restricted, feasibility of the debt structure has to be evaluated in detail. Financing from third parties may also be a tax efficient alternative.

Following the acquisition, the target's profits may be offset against the SPV's losses under Finnish group contribution rules. Alternatively the target may be merged with the SPV or liquidated to consolidate profits and losses.

According to Finnish group contribution rules, eligible contributions from an affiliated company are deducted from taxable profit of the contributing company and are added to the recipient company's taxable profit. The same rules apply to a Finnish permanent establishment of a foreign head office if it is tax resident in a EU Member State or in a country with which Finland has concluded a tax treaty and the treaty contains a non-discrimination article.

All these strategies have to be carefully analysed to avoid the application of anti-abuse provisions in Finland, as well as to comply with transfer pricing rules.

8. Are losses of the target company(ies) available after an acquisition is made?

Tax losses incurred may be carried forward for the subsequent 10 tax years. Losses are deductible in the order in which they are incurred.

If more than 50% of the shares in a company have changed hands during the loss year or thereafter, the right to carry forward losses is forfeited. Also, if a corresponding change of ownership has taken place in a company owning at least 20% of the shares in the loss-making company, the losses are forfeited.

The Finnish Tax Administration may upon application by the taxpayer and under certain conditions grant a special permission to utilise losses despite of the change in the ownership. If a special permission to utilise tax losses is obtained, the losses may be utilised only against taxable income earned by the company itself, since group contributions cannot be utilised to offset losses after a change in the ownership.

For a listed company, the right to carry forward losses is not forfeited unless more than half of the non-listed shares change hands (i.e. changes in the ownership of listed shares do not result in the forfeiture of losses). Changes in ownership of listed shares do not affect losses of companies owned by listed companies either.

No special provisions allow for the losses of one company in a group to be deducted from the profits of other companies in the same group (however group contributions may be used to achieve a similar effect, as described in section 7 above).

Under Finnish tax legislation, the carry back of losses is not allowed.

9. Is there any indirect tax on the transfer of shares (stamp duty, transfer tax, etc.)?

A transfer tax of 1.6% of the acquisition price is levied on the transfer of shares and other securities in Finnish companies. For real estate and housing companies, the transfer tax is 2%. As a main rule, transfer tax is not applicable to the trade of shares in publicly listed companies. Additionally, the transfer of shares between parties not tax resident in Finland are exempt from Finnish transfer tax unless the target is directly or indirectly a Finnish real estate or housing company. The purchaser is liable to pay the transfer tax.

10. Are there any restrictions on the deductibility of acquisition costs?

The costs accruing directly from facilitating the acquisition, such as fees from legal and other professional services and transfer tax are included in the acquisition costs of shares. The buyer cannot depreciate the acquisition cost of the shares, but when determining taxable capital gain in potential future share sales, the acquisition costs are deducted from the sale price.

Financing costs related to the acquisition of shares are deducted as yearly expenses i.e. they are not included in the shares' acquisition costs. This means that costs relating to financing or refinancing of the target company should be deductible, although acquisition cost of the acquired shares are not subject to depreciations. Due to this divergent treatment, drawing the line between the financing costs and other cost relating to the acquisition may be of essence from a tax point of view. Especially with regard to shares to which participation exemption is applicable, the classification of costs as acquisition cost of shares may cause non-deductibility of costs (please see section 15 below for further details).

11. Can VAT (if applicable) be recovered on acquisition costs?

Yes, VAT on acquisition costs can be recovered in the proportion that the company acquiring the shares or assets has VAT taxable activities.

12. Are there any particular issues to consider in the acquisition by foreign companies *(for example non-resident taxation rules/substance rules and tax efficient exit routes)?*

A company subject to only limited tax liability in Finland is taxed in Finland only for the Finnish source income unless the person has a permanent establishment in Finland. Capital gains derived from the sale of shares are not regarded as Finnish source income under Finnish legislation, as long as the company's assets do not essentially consist of real estate property.

Dividend distributions made by a Finnish company to a foreign corporate recipient are generally subject to withholding tax at 20%. However, this rate may be reduced in situations such as the following:

- Situations covered by the Parent-Subsidiary Directive;
- Situations where a tax treaty provides for a lower withholding tax rate;
- With regard to dividends paid to other EEC Member States, where the dividend would be tax exempt in similar domestic relations, assuming an agreement concerning exchange of information (or the Directive 77/799/EEC) is applicable between the countries, and assuming that the dividend recipient does not have the possibility of full tax credit in its home country.

Since dividends are tax exempt in most domestic relations between limited companies, the exemption actually applies to dividends paid to most EU Member States even if the Parent-Subsidiary Directive is not applicable.

13. Can the group reorganise after the acquisition in a tax neutral environment through mergers or a tax group?

As an EU Member State, Finland has harmonised its tax provisions for tax neutral corporate transactions in accordance with the Merger Directive. These rules also apply to domestic transactions; however not to transactions with companies outside the EU/EEC. With the exception of exchanges of shares, the same rules apply to corporate bodies other than limited companies and the rules on mergers also apply to domestic business partnerships.

Tax neutral mergers, divisions and transfers of assets are commonly utilised as pre or post-acquisition measures. An exchange of shares is mostly used as a means of carrying out the acquisition itself. Tax neutrality of reorganisations in effect means that arrangements do not cause income tax implications either for companies participating in the arrangements or their shareholders. Tax neutrality is often subject to fulfillment of certain conditions, for example in mergers, divisions and exchanges of shares, there are restrictions on the amount of cash contributions. Even though the threshold for the amount of cash contribution would not be exceeded, the transaction is deemed to be a taxable event to the extent that cash compensation has been used.

The rules for mergers, divisions and transfers of assets also apply to the transferring company when the receiving company is resident in another EU Member State. This is on the condition that the transferred assets remain effectively connected with a permanent establishment the receiving company has in Finland. If this condition is not fulfilled, or if the assets cease to be effectively connected with such permanent establishment, the difference between fair value and book value of assets will be realised for tax purposes.

The exchange of shares is not treated as a taxable transaction, except when a natural person receiving new shares becomes resident outside the EEA within five years of the end of the tax year in which the exchange took place or is resident within the EEA, or during the said time period transfers the shares received in the exchange of shares. Based on these exit tax provisions, the originally exempted amount is then treated as taxable income for that person.

If it can be established that the main purpose of the transaction has been to avoid or evade tax, the rules for mergers, divisions, transfers of assets and exchanges of shares do not apply. Due consideration must therefore be taken, for example, if a partial division or a transfer of assets has been carried out, shortly after which the new entity is planned to be disposed of in a tax exempt share sale.

The corporate restructurings described above are exempt from asset transfer tax (with the exception of the exchange of shares) as long as the transaction is carried out according to specific tax and corporate legislation.

14. Is there any particular issue to consider in the case of companies which main assets are real estate?

Many of Finland's Double Taxation Agreements (DTAs) include a paragraph entitling Finland to tax income arising from a shareholding in a Finnish company which owns real estate in Finland and shareholders of which are entitled to use the real estate based on their shareholding. Typically, Finland's taxing right also covers capital gains derived from the disposal of shares in real estate companies the assets of which mainly comprise of directly or indirectly owned real estate located in Finland. However, there are also DTAs not allowing Finland to tax income or capital gains relating to such shares.

A real estate company is not a specifically defined legal term in Finnish law even though it is commonly used in practice; real estate companies can be organised, e.g. as ordinary limited liability companies, residential housing companies or Mutual Real Estate Companies (MRECs).

Residential housing companies and MRECs are taxed under the Income Tax Act. In practice, residential housing companies do not pay tax. The purpose of the company is only to provide residence to the shareholders who pay all costs of the company through a monthly maintenance charge. MRECs are limited liability companies with purpose to own and manage at least one building or a part of a building. Its shares are attributable to certain parts of the real property and based on their shareholding, shareholders are entitled to hold and control the respective parts of the real estate. Therefore, for example, rental income arising from the leasing of the real estate accrues directly to the shareholders. Typically, income received by MRECs comprises of monthly charges that the shareholders pay to the mutual real estate company.

Regular Real Estate Companies (RECs) operate just as any limited liability companies – i.e. if there is no flow-through of income to the shareholders and taxable profits are expected to be incurred on the REC level.

Capital gains derived by Finnish and foreign corporations (provided Finland is allowed to tax the capital gains) from the sale of RECs are subject to the general corporate income tax (currently 20%). Specific transfer tax provisions apply to sales of real estate companies (please see section 9 above).

Sell-side

15. How are capital gains taxed in your country? Is there any participation exemption regime available?

Finnish tax law includes a participation exemption regime. Capital gains derived by companies from the transfer of shares are not considered taxable income, and consequently acquisition costs of shares are not tax-deductible, if the following conditions are met:

- The transferor of the shares is a limited liability company, a co-operative a savings bank or a mutual insurance company taxed in accordance with the Business Income Tax Act;
- The transferor is not engaged in venture capital or private equity activities;
- The shares belong to the transferor's fixed assets;
- The transferor has owned at least 10% of the share capital of the target company without interruption for at least one year during a period that has ended no more than one year prior to the transfer. The transferred shares must also be among the shares which have been owned in this way;
- The target company is not a residential housing company, a real estate company or a limited company the activities of which de facto mainly consist of real estate holding or managing;
- The company to be transferred is:
- A Finnish resident company;
- A company referred to in Article 2 of the EU Parent-Subsidiary Directive;
- A company resident in a country with which Finland has a tax treaty, which is applied to dividends distributed by that company.

Capital losses accruing from the transfer of shares that are fixed assets but that cannot be transferred are tax exempt and are only deductible from taxable capital gains derived from transfers of fixed asset shares in the same tax year and the subsequent five tax years. This limitation is not applied to the transfer of shares in residential housing companies, real estate companies and real estate holding or management companies. However if the taxpayer has not owned the transferred shares uninterruptedly for at least one year, the deductible loss is decreased by any dividends, group contributions or comparable items paid by the target company to the taxpayer, which have reduced the target company's assets.

Even if under participation exemption rules acquisition costs of shares would not be tax-deductible, based on case law, the seller may be entitled to deduct for example expert and auditing fees relating to the sale of shares for the part acquisition cost including those costs that exceed the tax exempt sales price.

In the current Finnish tax practice, recovery of VAT on transaction costs relating to the sales of shares is generally denied by the tax authorities. In the absence of recent case law, the correctness of such interpretation is not clear.

16. Is there any fiscal advantage if the proceeds from the sale are reinvested?

There is no specific tax advantage for reinvesting the sale proceeds.

17. Are there any local substance requirements for holding/finance companies?

There are no substance requirements for holding/finance companies tax resident in Finland.

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