

HR & Tax Alert



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Finland – Changes to taxation of foreign hired-out employees and payments for services rendered in Finland by non-residents

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Executive summary

On 24 November 2006, the Finnish Parliament accepted changes to several Tax Acts relating to the taxation of foreign hired-out employees and payments for services rendered in Finland by non-residents. Major changes contained within include:

- Foreign hired out employees, as defined by the OECD Model Tax Convention, may now have their salary income taxed in Finland even where their employer is a non Finnish resident company.
- Residents of countries with which Finland has a tax treaty can now be entered into the pre-assessment register even if they do not conduct their business in Finland through a permanent establishment.

Changes have effect from 1 January 2007.

Taxation of foreign hired-out employees

Until now, Finland has not taxed salary income received by a non-resident for work performed in Finland, if the non-resident has been employed by a foreign employer. This restriction has also applied when the foreign employer is a company whose main activity is the hiring-out of labour and the non-resident employee has been hired out to a Finnish client and the work is performed in Finland. Such foreign workers hired through a non resident employment agency are referred to as foreign hired out employees.

Finland will now tax salary income received by foreign hired-out employees for their work in Finland regardless of the length of their employment in Finland. The law will be effective as of 1 January 2007. Taking into account tax treaties, Finland will be entitled to tax the salaries of hired-out employees resident in the Nordic and Baltic countries. The salaries of hired-out employees resident in other treaty countries would only be taxable in Finland if the employee was present in Finland for more than 183 days in a calendar year or a twelve-month period, depending on the treaty, or if the remuneration was borne by a permanent establishment of the employer in Finland.

The definition of a hired-out employee corresponds to the definition presented in the Commentary on the OECD Model Tax Convention. At this stage, it is still somewhat unclear whether the law will also be applied to employees of companies other than those whose main branch of business is employment services and if so, under what circumstances.

Taxation of Non-Residents in Finland

The prepayment system of taxes in Finland has two distinct features. Taxes are withheld from certain types of payments (eg. wages and salary), while preassessment and estimated advance taxes are used to collect tax on other types of income (e.g. rental income and capital gains), where withholding is not possible or practical.

A deduction of tax at source of 35% is levied on non-residents' salary income in Finland. However, non-residents are entitled to a monthly standard deduction of 510 euros (or 17 euros per day if the period to which the salary relates to is shorter than a month). The hired-out employee is obliged to apply for advance taxes if the foreign employer is not under obligation to withhold tax on salary in Finland and Finland has the right to tax the salary according to the relevant tax treaty.

The application for the advance tax should be filed by the end of the month following the month the work commenced. In cases where the employee neglects to file the advance tax application a punitive tax increase of up to 2 000 euros may be imposed.

Reporting requirements

Reporting requirements will be imposed on the foreign employer or its representative in Finland as well as the principal Finnish company for whom the work is carried out. These requirements will have effect only when Finland has the right to tax the salary of the hired-out employee, according to the relevant tax treaty. The Finnish principal will be obliged to report the identity and contact information of the foreign employer and its representative. The foreign employer or its representative will in turn be obliged to give notice of the commencement of a hired-out employee's work in Finland by the end of the month following the month the work commenced as well as give an annual notification of the salaries

paid to hired-out employees and other employees who have resided in Finland for more than six months.

Taxation of payments for services rendered in Finland by non-residents

Changes were also accepted to the rules on taxation at source of payments other than salary for services rendered in Finland by non-residents. Residents of countries with which Finland has a tax treaty can now be entered into the pre-assessment register even if they do not conduct their business in Finland through a permanent establishment.

According to the Prepayment Act, even where payments are not deemed to be wages or salary, tax must be withheld from remuneration paid in respect of work, a task or service done for another person. Where there is no registration in the preassessment register the payer will be obliged to withhold a tax of 13 % if the payment is paid to a company or partnership and 35 % if the payment is made to a physical person. The payer may abstain from withholding tax if the payee is registered in the pre-assessment register, presents a certificate from the local tax office according to which no tax is to be withheld, or presents other evidence according to which a tax treaty prevents taxation of the payee in Finland. However, if the work includes construction, shipbuilding, installation work, transportation, cleaning or nursing and health care, tax shall be withheld unless the payee is registered in the pre-assessment register or presents a certificate from the local tax office.

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