

# Eligibility for Treaty Benefits Under The Finland-U.S. Income Tax Treaty

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Reprinted from *Tax Notes International*, October 21, 2019, p. 245

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In this article, the authors provide flowcharts to assist practitioners in determining whether companies are eligible for benefits under the limitation on benefits provision in the Finland-U.S. income tax treaty.

To be entitled to benefits under income tax treaties, companies must satisfy specific eligibility requirements. This article includes decision-making flowcharts to assist taxpayers and tax practitioners in navigating the eligibility requirements of the Finland-U.S. income tax treaty and its accompanying protocol (collectively referred to as “the treaty”), as applied to Finnish companies and with a particular focus on the eligibility requirements for a 0 percent withholding tax rate on dividends.<sup>1</sup>

<sup>1</sup>“Convention Between the United States of America and Finland for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion With Respect to Taxes on Income,” signed on Sept. 21, 1989, and accompanying protocol signed on May 31, 2006.

Income tax treaties may exempt business income from source country income taxes and eliminate or reduce domestic withholding taxes on specified payments between residents of countries that are parties to the treaty. To be entitled to benefits under a U.S. income tax treaty, a company generally must not only be a resident of the tax treaty partner’s country, but it must also satisfy at least one of the tests required by an applicable limitation on benefits provision.

The flowcharts in this article focus on the eligibility of Finnish companies claiming treaty benefits under the treaty’s LOB article (article 16) on income that would otherwise be subject to U.S. federal income taxation. This article does not

address eligibility for treaty benefits of entities that are partnerships or otherwise transparent for U.S. or Finnish tax purposes. This article is based on the treaty, the accompanying protocol to the treaty, and the U.S. Treasury Department's technical explanations.

This article also addresses the eligibility of Finnish companies for the 0 percent withholding tax rate on dividends under article 10.3 and the LOB provision of the treaty.

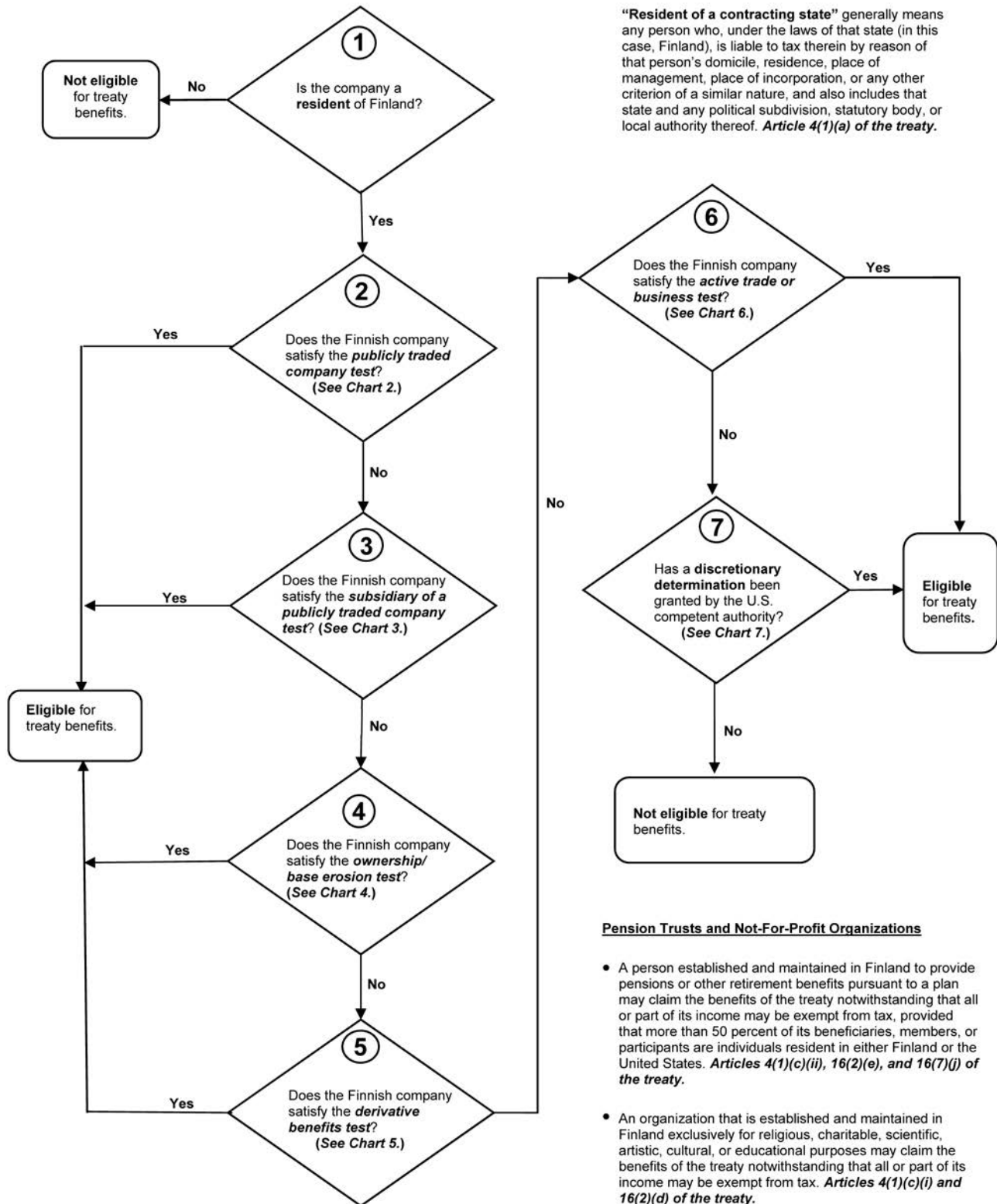
This article contains eight flowcharts that analyze the LOB provision of the treaty as applied to Finnish resident companies. These may serve as a useful practice tool for taxpayers and tax practitioners. Although the flowcharts provide a comprehensive review of applicable provisions under the treaty, taxpayers and their tax advisers should carefully evaluate each individual case and determine if the treaty's requirements are met based on all facts and circumstances.

This article is the 17th in a series of articles<sup>2</sup> that provide flowcharts to assist taxpayers and tax practitioners in determining a company's

eligibility for tax treaty benefits under the LOB provisions of specific U.S. income tax treaties and, when applicable, in determining eligibility for a 0 percent withholding tax rate on cross-border intercompany dividend payments to the company. ■

<sup>2</sup> See Jason Connery, Ron Dabrowski, and Jennifer Blasdel-Marinescu, "Eligibility for Treaty Benefits Under the New Zealand-U.S. Income Tax Treaty," *Tax Notes Int'l*, July 31, 2017, p. 465; Connery, Dabrowski, and Blasdel-Marinescu, "Eligibility for Treaty Benefits Under the Mexico-U.S. Income Tax Treaty," *Tax Notes Int'l*, June 27, 2016, p. 1285; Connery, Dabrowski, and Blasdel-Marinescu, "Eligibility for Treaty Benefits Under the Denmark-U.S. Income Tax Treaty," *Tax Notes Int'l*, June 29, 2015, p. 1219; Connery and Blasdel-Marinescu, "Eligibility for Treaty Benefits Under the Belgium-U.S. Income Tax Treaty," *Tax Notes Int'l*, Feb. 10, 2014, p. 563; Connery and Blasdel-Marinescu, "Eligibility for Treaty Benefits Under the Ireland-U.S. Income Tax Treaty," *Tax Notes Int'l*, June 17, 2013, p. 1223; Connery, Douglas Poms, and Blasdel-Marinescu, "Eligibility for Treaty Benefits Under the Sweden-U.S. Income Tax Treaty," *Tax Notes Int'l*, July 23, 2012, p. 359; Connery, Poms, and Blasdel-Marinescu, "Eligibility for Treaty Benefits Under the Australia-U.S. Income Tax Treaty," *Tax Notes Int'l*, Dec. 12, 2011, p. 843; Connery, Poms, and Blasdel, "Eligibility for Treaty Benefits Under the Switzerland-U.S. Income Tax Treaty," 62 *Tax Notes Int'l*, May 9, 2011, p. 505; Connery, Poms, and Blasdel, "Eligibility for Treaty Benefits Under the Japan-U.S. Income Tax Treaty," *Tax Notes Int'l*, Sept. 6, 2010, p. 789; Connery, Poms, and Blasdel, "Eligibility for Treaty Benefits Under the 2009 Protocol to the France-U.S. Income Tax Treaty," *Tax Notes Int'l*, Apr. 12, 2010, p. 149; John Venuti, Connery, Poms, and Blasdel, "Eligibility for Treaty Benefits Under the Netherlands-U.S. Income Tax Treaty," *Tax Notes Int'l*, Nov. 23, 2009, p. 601; Venuti, Connery, Poms, and Alexey Manasuev, "Eligibility for Treaty Benefits Under the Canada-U.S. Income Tax Treaty," *Tax Notes Int'l*, June 15, 2009, p. 967; Venuti, Dabrowski, Poms, and Manasuev, "Eligibility for Treaty Benefits Under U.K.-U.S. Income Tax Treaty," *Tax Notes Int'l*, Mar. 23, 2009, p. 1095; Venuti, Connery, Poms, and Manasuev, "Eligibility for Treaty Benefits Under the Luxembourg-U.S. Income Tax Treaty," *Tax Notes Int'l*, July 21, 2008, p. 285; Venuti, Dabrowski, Poms, and Manasuev, "Eligibility for Treaty Benefits Under the France-U.S. Income Tax Treaty," *Tax Notes Int'l*, Feb. 11, 2008, p. 523; and Venuti and Manasuev, "Eligibility for Zero Withholding on Dividends in the New 2006 Germany-U.S. Protocol," *Tax Notes Int'l*, Jan. 14, 2008, p. 181.

**Chart 1. Eligibility of Treaty Benefits Under Article 16 (LOB) of the Finland-U.S. Tax Treaty**





## Chart 2. Publicly Traded Company Test Under Article 16(2)(c)(i) (LOB) of the Finland-U.S. Tax Treaty

“Principal class of shares” means the ordinary or common shares of the company, provided that such class of shares represents the majority of the voting power and value of the company. If no single class of ordinary or common shares represents the majority of the aggregate voting power and value of the company, the principal class of shares is that class or those classes that in the aggregate represent a majority of the aggregate voting power and value of the company. *Article 16(7)(a) of the treaty.*

“Shares” includes depository receipts thereof. *Article 16(7)(c) of the treaty.*

“Disproportionate class of shares” means any class of shares of a company resident in one of the states that entitles the shareholder to disproportionately higher participation, through dividends, redemption payments, or otherwise, in the earnings generated in the other state by particular assets or activities of the company. *Article 16(7)(b) of the treaty.*

“Recognized stock exchange” means:

- (i) the NASDAQ System owned by the National Association of Securities Dealers, Inc. and any stock exchange registered with the U.S. Securities and Exchange Commission as a national securities exchange under the U.S. Securities Exchange Act of 1934;
- (ii) the Helsinki Stock Exchange;
- (iii) the Irish Stock Exchange and the stock exchanges of Amsterdam, Brussels, Copenhagen, Frankfurt, London, Oslo, Paris, Reykjavik, Riga, Stockholm, Tallinn, Vilnius, Vienna, and Zurich; and
- (iv) any other stock exchange agreed upon by the competent authorities.

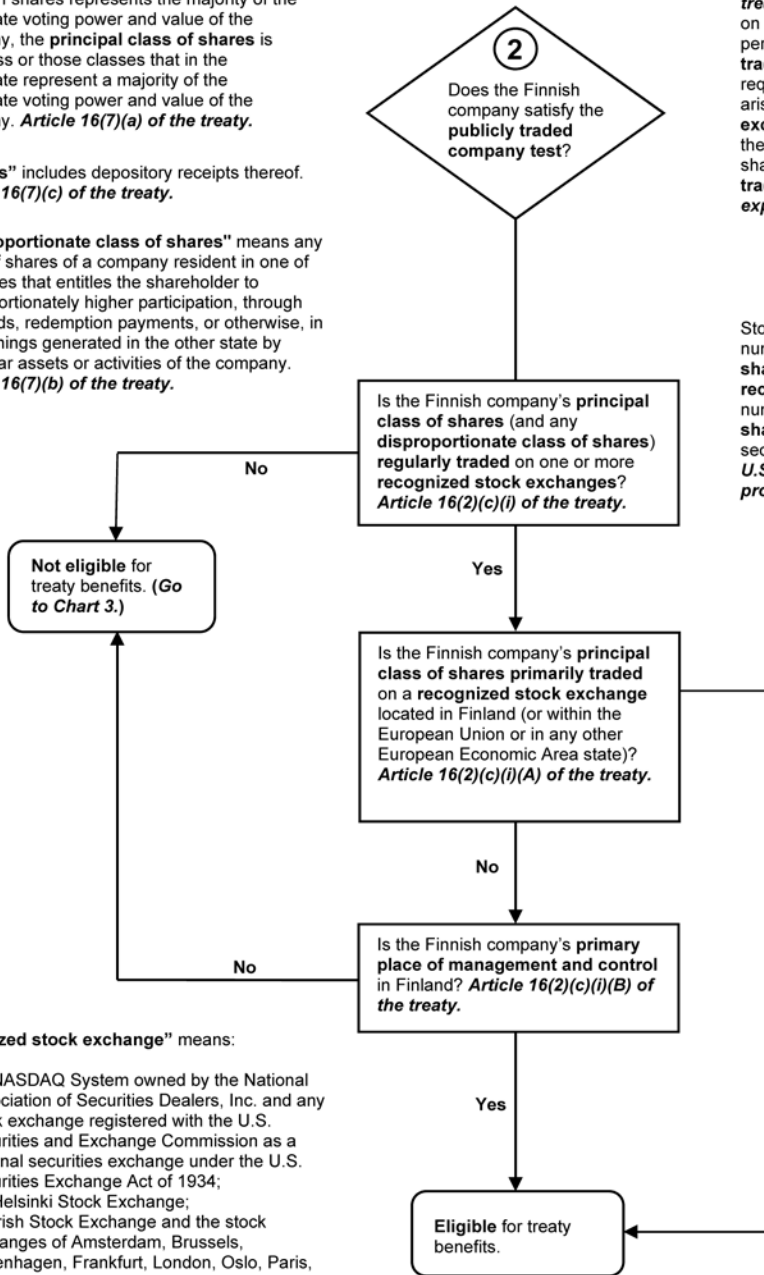
*Article 16(7)(d) of the treaty.*

A class of shares is considered to be “regularly traded” on one or more **recognized stock exchanges** in a taxable year if the aggregate number of shares of that class traded on such stock exchange or exchanges during the preceding taxable year is at least 6 percent of the average number of shares outstanding in that class during that preceding taxable year. *Article 16(7)(e) of the treaty.* For this purpose, if a class of shares was not listed on a **recognized stock exchange** during this 12-month period, the class of shares will be treated as **regularly traded** only if the class meets the aggregate trading requirements for the taxable period in which the income arises. Trading on one or more **recognized stock exchanges** may be aggregated for purposes of meeting the **regularly traded** standard. Authorized but unissued shares are not considered for purposes of the **regularly traded** requirement. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*

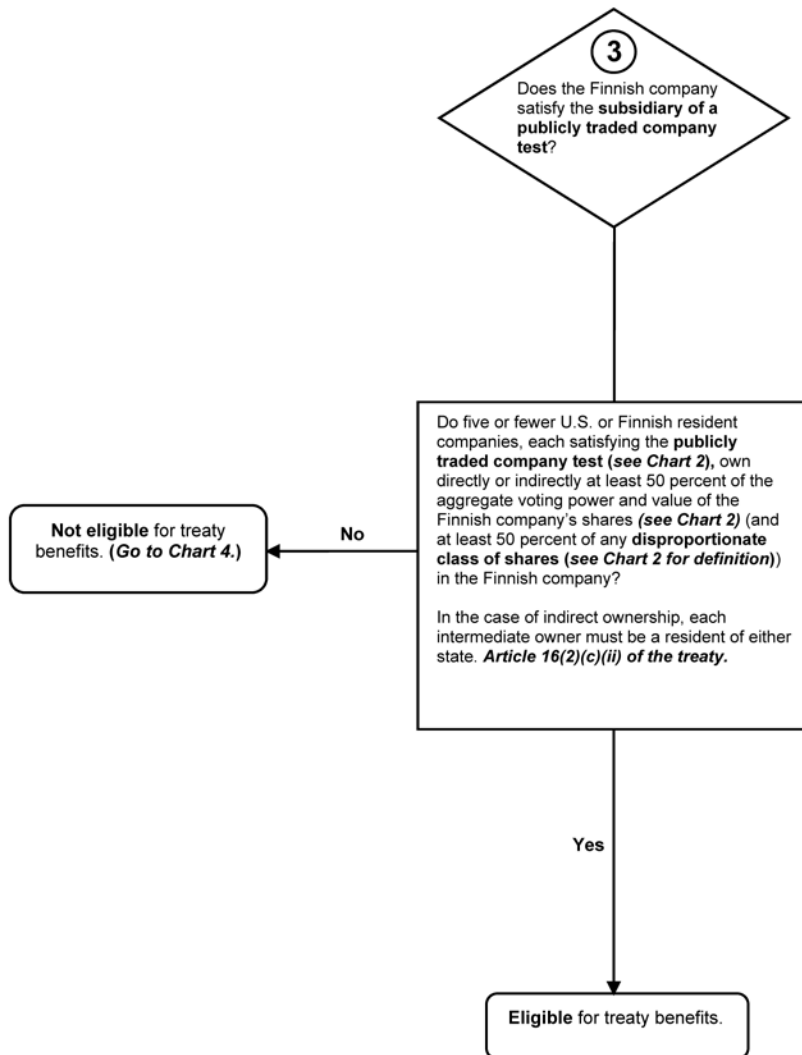
Stock of a Finnish company is “**primarily traded**” if the number of shares in the company’s **principal class of shares** that are traded during the taxable year on all **recognized stock exchanges** in Finland exceeds the number of shares in the company’s **principal class of shares** that are traded during the year on established securities markets in any other single foreign country. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*

A Finnish company’s **primary place of management and control** is in Finland only if executive officers and senior management employees exercise day-to-day responsibility for more of the strategic, financial, and operational policy decision making for the company (including its direct and indirect subsidiaries) in Finland than in any other state, and the staff conduct more of the day-to-day activities necessary for preparing and making those decisions in Finland than in any other state. *Article 16(7)(f) of the treaty.* Thus, the **primary place of management and control** test looks to the overall activities of the relevant persons to see where those activities are conducted. In most cases, it will be a necessary, but not a sufficient, condition that the headquarters of the company (that is, the place at which the chief executive officer and other top executives normally are based) be located in Finland. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*

For guidance regarding the persons who are considered “executive officers and senior management employees,” see *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*



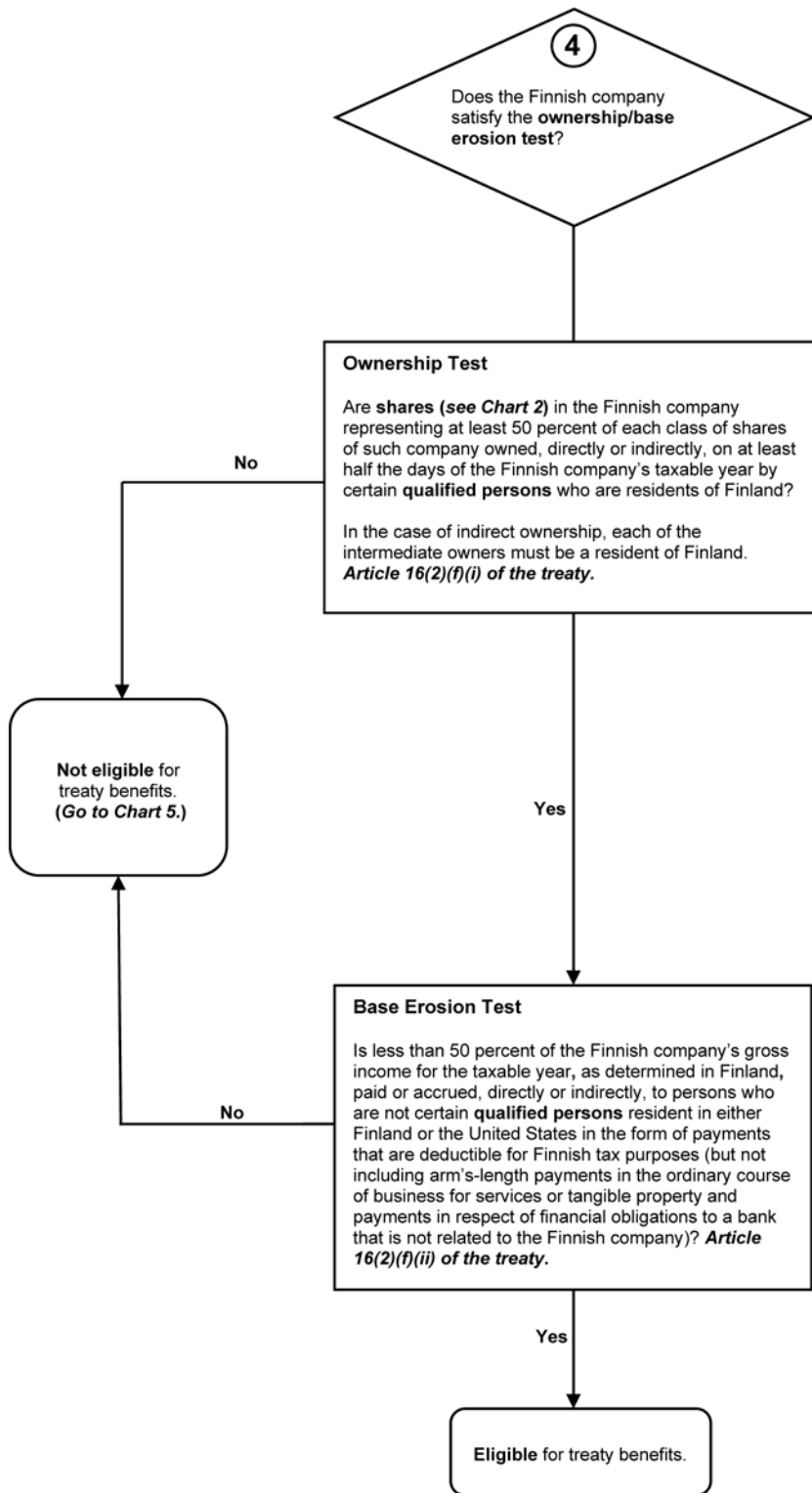
**Chart 3. Subsidiary of a Publicly Traded Company Test Under Article 16(2)(c)(ii) (LOB) of the Finland-U.S. Tax Treaty**



**Example**

A Finnish company, all the shares of which are owned by another Finnish company, would qualify for benefits under the treaty if the **principal class of shares** (see Chart 2 for definition) (and any **disproportionate classes of shares** (see Chart 2 for definition)) of the Finnish parent company are **regularly traded and primarily traded** (see Chart 2 for definitions) on the London stock exchange. However, a Finnish subsidiary would not qualify for benefits under the **subsidiary of a publicly traded company test** if the publicly traded parent company were a resident of Ireland, for example, and not a resident of the United States or Finland. Furthermore, if a Finnish parent company indirectly owned a Finnish company through a chain of subsidiaries, each such subsidiary in the chain, as an intermediate owner, must be a resident of the United States or Finland for the Finnish subsidiary to meet the **subsidiary of a publicly traded company test**. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*

**Chart 4. Ownership/Base Erosion Test Under Article 16(2)(f) (LOB) of the Finland-U.S. Tax Treaty**



**Qualified persons** for purposes of the **Ownership Test** are limited to residents of Finland that are:

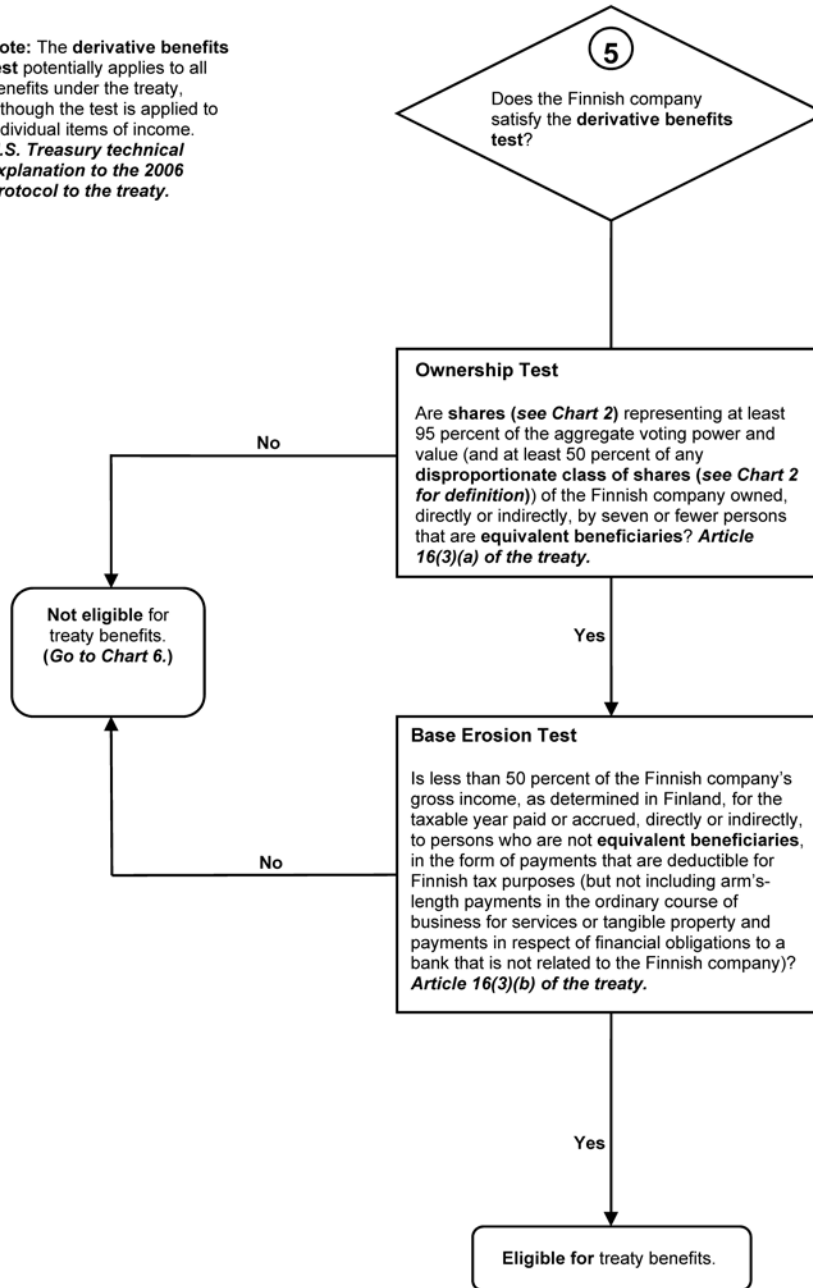
- A. individuals resident in Finland (see *article 16(2)(a) of the treaty*);
- B. Finland or any political subdivision, statutory body or local authority thereof (see *article 16(2)(b) of the treaty*);
- C. Finnish companies that satisfy the **publicly traded company test** (see *Chart 2*) (see *article 16(2)(c)(i) of the treaty*); and
- D. certain Finnish pension trusts and not-for-profit organizations organized in Finland (see *article 16(2)(d) and (e) of the treaty*).

**Qualified persons** for purposes of the **Base Erosion Test** are those described in A, B, C, and D, above, and corresponding U.S. residents.

For purposes of the **Base Erosion Test**, depreciation and amortization deductions, which do not represent payments or accruals to other persons, are disregarded. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*

**Chart 5. Derivative Benefits Test Under Article 16(3) (LOB) of the Finland-U.S. Tax Treaty**

**Note:** The derivative benefits test potentially applies to all benefits under the treaty, although the test is applied to individual items of income. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*



**“Equivalent Beneficiary” means:**

A resident of a member state of the EU or of any other European Economic Area state or of a party to the North American Free Trade Agreement, or of Switzerland but only if that resident:

(i)(A) would be entitled to *all* the benefits of a comprehensive income tax treaty between any EU member state or any other European Economic Area state or any party to NAFTA, or Switzerland and the United States under provisions analogous to the rules for certain *qualified persons* (see Chart 4, *Base Erosion Test, for definition*), provided that if the treaty does not contain a comprehensive LOB article, the person would be entitled to the benefits of the treaty by reason of status as a *qualified person* (see Chart 4, *Base Erosion Test, for definition*) if the person were a resident of one of the states under article 4 (residence) of the treaty; and

(B) with respect to insurance premiums and to income referred to in article 10 (dividends), 11 (interest), or 12 (royalties) of the treaty, would be entitled under the treaty to a rate of tax with respect to the particular class of income for which benefits are being claimed under the treaty that is at least as low as the rate applicable under the treaty; or

(ii) is a resident of either the United States or Finland that is a *qualified person* (see Chart 4, *Base Erosion Test, for definition*) entitled to the benefits of the treaty by reason of such status. **Article 16(7)(g) of the treaty.**

**Note:** For purposes of applying paragraph 3 of article 10 (dividends) of the treaty in order to determine whether a person owning shares, directly or indirectly, in the company claiming the benefits of the treaty is an **equivalent beneficiary**, the person shall be deemed to hold the same voting power in the company paying the dividend as the company claiming the benefits holds in the company. **Article 16(7)(g), flush language, of the treaty.**

**Note:** Under article 16(7)(g)(i), a company that satisfies the **subsidiary of a publicly traded company test** (see Chart 3) or the **ownership/base erosion test** (see Chart 4) is **not** an equivalent beneficiary.



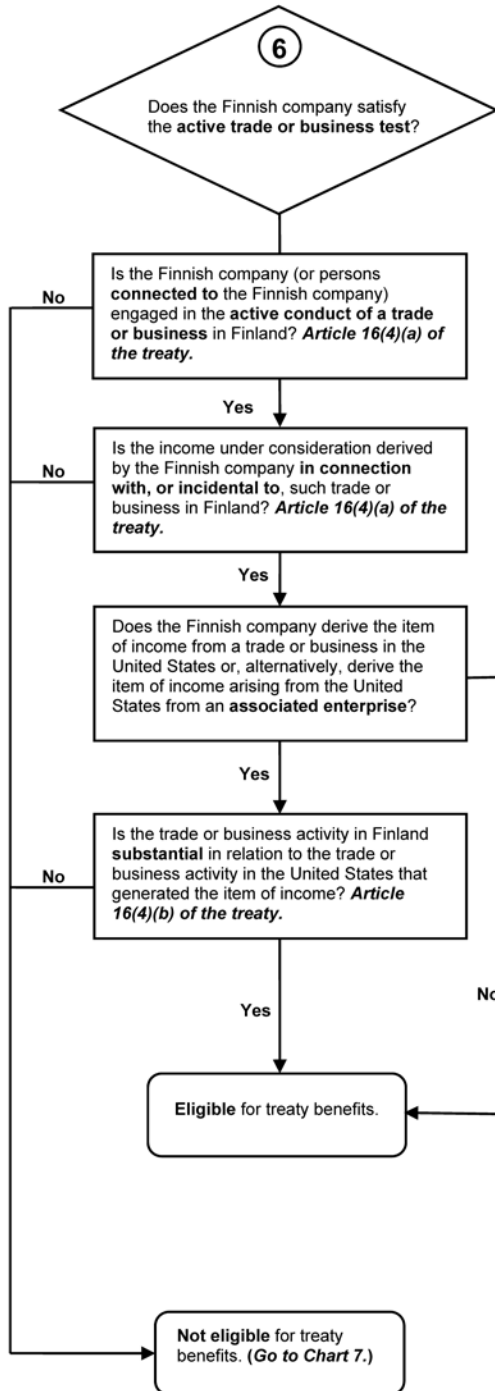
## Chart 6. Active Trade or Business Test Under Article 16(4) (LOB) of the Finland-U.S. Tax Treaty (Applies only if an item of income is derived in connection with or incidental to an active trade or business in Finland)

An item of income is derived "in connection with" a trade or business if the income-producing activity in the source state (in this case, the United States) is a line of business that "forms a part of" or is "complementary" to the trade or business conducted in Finland by the income recipient. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*

A business activity generally will be considered to "form a part of" a business activity conducted in the source state if the two activities involve the design, manufacture, or sale of the same products or type of products, or the provision of similar services. The line of business in the state of residence may be upstream, downstream, or parallel to the activity conducted in the source state. Thus, the line of business may provide inputs for a manufacturing process that occurs in the source state, may sell the output of that manufacturing process, or simply may sell the same sorts of products that are being sold by the trade or business carried on in the source State. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*

For two activities to be considered "complementary," the activities need not relate to the same types of products or services, but they should be part of the same overall industry and be related in the sense that the success or failure of one activity will tend to result in success or failure for the other. When more than one trade or business is conducted in the source state and only one of the trades or businesses forms a part of or is complementary to a trade or business conducted in the state of residence, it is necessary to identify the trade or business to which an item of income is attributable. Royalties generally will be considered to be derived in connection with the trade or business to which the underlying intangible property is attributable. Dividends will be deemed to be derived first out of earnings and profits of the treaty-benefited trade or business, and then out of other earnings and profits. Interest income may be allocated under any reasonable method consistently applied. A method that conforms to U.S. principles for expense allocation will be considered a reasonable method. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*

An item of income derived from the source state (in this case, the United States) is "incidental to" the trade or business carried on in Finland if production of the item facilitates the conduct of the trade or business in Finland. An example of incidental income is the temporary investment of working capital of a person in Finland in securities issued by persons in the source state. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*



The term "trade or business" is not defined in the Treaty. The U.S. Treasury technical explanation to the 2006 protocol to the treaty explains that the United States will refer to the regulations issued under section 367(a) for the definition of the term "trade or business." In general, therefore, a trade or business will be considered to be a specific unified group of activities that constitute or could constitute an independent economic enterprise carried on for profit. Furthermore, a corporation generally will be considered to carry on a trade or business only if the officers and employees of the corporation conduct substantial managerial and operational activities. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*

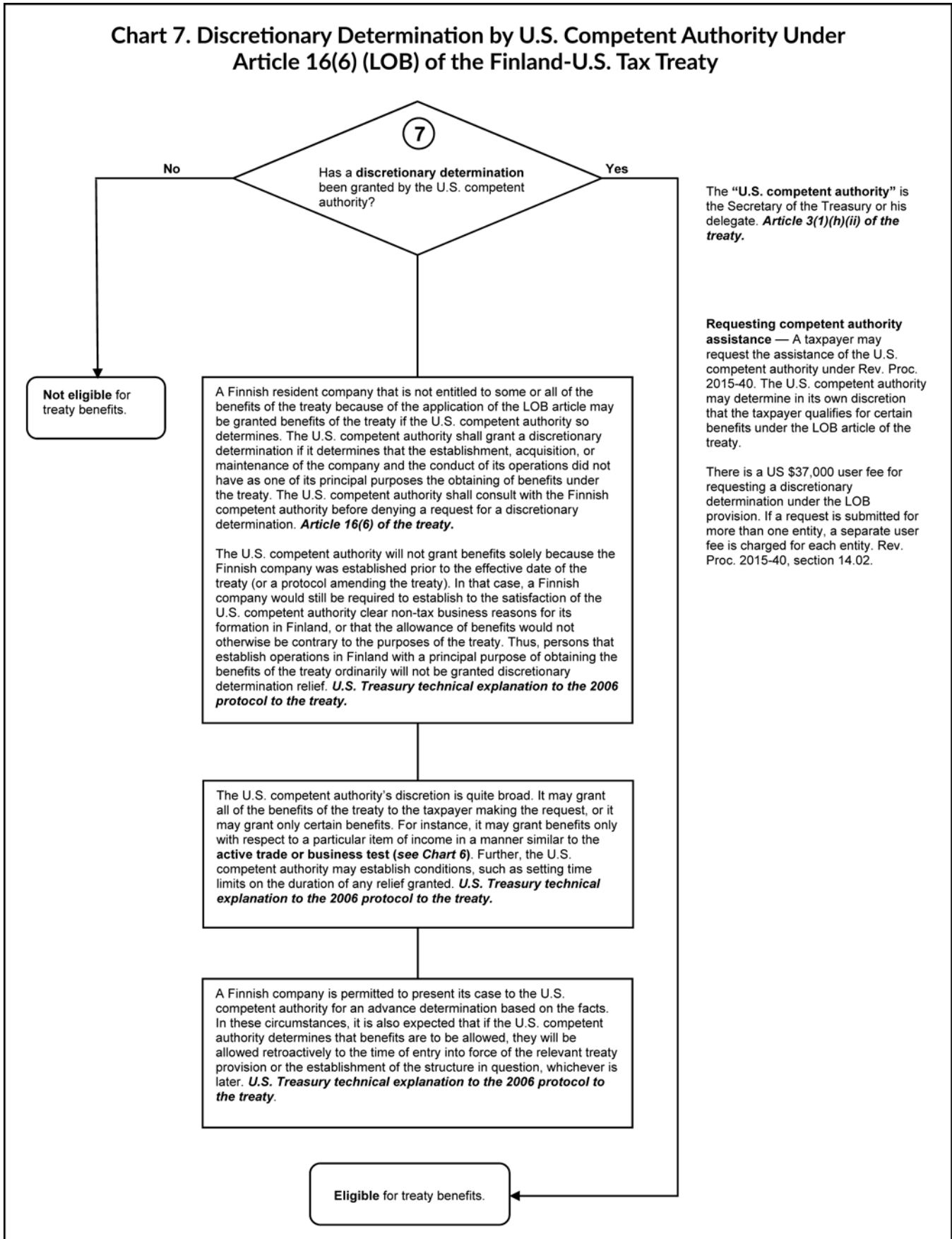
The active conduct of a trade or business does not include the business of making or managing investments for one's own account, unless these activities are banking, insurance, or securities activities carried on by a bank, insurance company, or registered securities dealer. *Article 16(4)(a) of the treaty.* Because a headquarters operation is in the business of managing investments, a company that functions solely as a headquarters company will not be considered to be engaged in an active trade or business for purposes of the active trade or business test. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*

In determining whether a person is engaged in the active conduct of a trade or business in a contracting state, activities conducted by persons connected to that person shall be deemed to be conducted by that person. A person shall be "connected to" another if one possesses at least 50 percent of the beneficial interest in the other (or, in the case of a company, at least 50 percent of the aggregate vote and at least 50 percent of the aggregate value of the shares (see Chart 2) in the company or of the beneficial equity interest in the company) or another person possesses, directly or indirectly, at least 50 percent of the beneficial interest (or, in the case of a company, at least 50 percent of the aggregate vote and at least 50 percent of the aggregate value of the shares (see Chart 2) in the company or of the beneficial equity interest in the company) in each person. In any case, a person shall be considered to be connected to another if, based on all the relevant facts and circumstances, one has control of the other or both are under the control of the same person or persons. *Article 16(4)(c) of the treaty.*

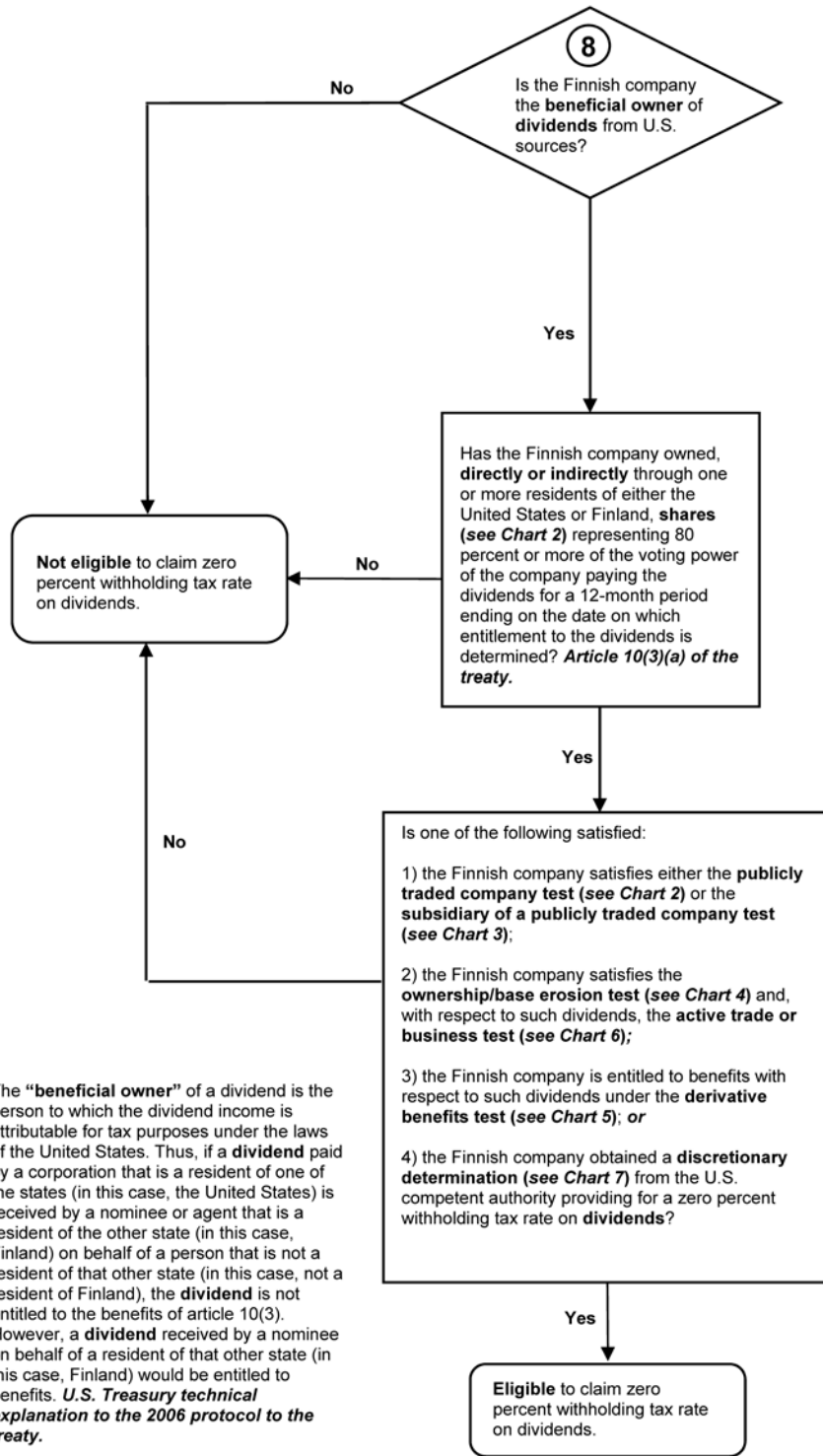
A Finnish company is "associated" with an enterprise of the United States if it participates directly or indirectly in the management, control, or capital of the U.S. enterprise or if any third person or persons participate directly or indirectly in the management, control, or capital of the Finnish company and the U.S. enterprise. *Article 9(1) of the treaty.*

Whether the Finnish company's trade or business (or the trade or business of a person connected to the Finnish company) is "substantial" in relation to the trade or business activity in the United States that generated the item of income is determined based upon all the facts and circumstances and takes into account: (i) the comparative sizes of the trades or businesses in each contracting state; (ii) the nature of the activities performed in each contracting state; and (iii) the relative contributions made to that trade or business in each contracting state. In any case, in making each determination or comparison, due regard will be given to the relative sizes of the U.S. and Finnish economies. The determination of substantiality is made separately for each item of income derived from the source state. It therefore is possible that a person would be entitled to the benefits of the treaty with respect to one item of income but not with respect to another. If a resident of a contracting state is entitled to treaty benefits with respect to a particular item of income under the active trade or business test, the resident is entitled to all benefits of the treaty insofar as they affect the taxation of that item of income in the source state. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*

**Chart 7. Discretionary Determination by U.S. Competent Authority Under Article 16(6) (LOB) of the Finland-U.S. Tax Treaty**



### Chart 8. Eligibility for Zero Percent Withholding Tax Rate on Dividend Under Article 10(3) of the Finland-U.S. Tax Treaty



The “beneficial owner” of a dividend is the person to which the dividend income is attributable for tax purposes under the laws of the United States. Thus, if a dividend paid by a corporation that is a resident of one of the states (in this case, the United States) is received by a nominee or agent that is a resident of the other state (in this case, Finland) on behalf of a person that is not a resident of that other state (in this case, not a resident of Finland), the dividend is not entitled to the benefits of article 10(3). However, a dividend received by a nominee on behalf of a resident of that other state (in this case, Finland) would be entitled to benefits. *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*

The term “dividends” means:

- (i) income from shares (see Chart 2) or other rights, not being debt claims, participating in profits;
- (ii) income from other corporate rights that is subjected to the same taxation treatment as income from shares by the laws of the state of which the company making the distribution is resident (here, the United States); and
- (iii) income from arrangements, including debt obligations, carrying the right to participate in profits, to the extent so characterized under the law of the state in which the income arises (here, the United States). *Article 10(5) of the treaty.*

The treaty defines the term “dividends” broadly and flexibly. The definition is intended to cover all arrangements that yield a return on an equity investment in a corporation as determined under the tax law of the source state (in this case the United States), including types of arrangements that might be developed in the future. The term includes income from shares, or other corporate rights that are not treated as debt under the law of the source state, that participate in the profits of the company. The term also includes income that is subjected to the same tax treatment as income from shares by the law of the source state. Thus, a constructive dividend that results from a non-arm’s-length transaction between a corporation and a related party is a dividend. In the case of the United States, the term “dividends” includes amounts treated as a dividend under U.S. law upon the sale or redemption of shares or upon a transfer of shares in a reorganization. See, e.g., Rev. Rul. 92-85, 1992-2 C.B. 69 (sale of foreign subsidiary’s stock to U.S. sister company is a deemed dividend to extent of the subsidiary’s and sister’s earnings and profits). Further, a distribution from a U.S. publicly traded limited partnership, which is taxed as a corporation under U.S. law, is a dividend for purposes of article 10. However, a distribution by a limited liability company is not taxable by the United States under article 10, provided the limited liability company is not characterized as an association taxable as a corporation under U.S. law. Finally, a payment denominated as interest that is made by a thinly capitalized corporation may be treated as a dividend to the extent that the debt is recharacterized as equity under the laws of the source state (in this case the United States). *U.S. Treasury technical explanation to the 2006 protocol to the treaty.*

Dividends received by a Finnish company from U.S. real estate investment trusts and U.S. regulated investment companies are not eligible for a zero percent withholding tax rate. *Article 10(4)(a) of the treaty.*