Real Estate Tax Services News

Keeping you informed

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Government of Finland publishes draft bill amending Finnish tax treatment of Finnish and foreign real estate investment funds

In brief

On 19 September 2022, the Finnish Ministry of Finance published a draft bill which amends the Finnish tax treatment of Finnish and foreign real estate investment funds. According to the draft bill, real estate investment funds with fewer than 30 investors will no longer be able to obtain tax-exempt status for Finnish income tax purposes but will instead be considered fiscally transparent. The draft bill would introduce Finnish tax filing obligations for both the fiscally transparent fund and its investors, and it also contains complex provisions e.g., with respect to the calculation of taxable income at the level of the investors in such fiscally transparent funds.

The draft bill is currently subject to public consultation with the proposed rules expected to enter into force from fiscal year 2024. The final version of the government bill is currently expected to be released in the week commencing 14 November.

In detail

To date, Finnish and foreign real estate investment funds have benefitted from tax-exemption on their Finnish source income where such funds satisfy certain basic criteria as described in Section 20a of the Finnish Income Tax Act ("ITA"). The draft bill proposes that this is amended so that, where the Finnish or foreign real estate investment fund has fewer than 30 investors, it would instead be considered to be fiscally transparent for Finnish income tax purposes.

In order to understand the potential impact of the draft bill, certain key definitions and interpretations of the draft bill need to be explained.

- The concept of a real estate investment fund is defined in the draft bill as a Finnish contractual special investment fund within the meaning of the Finnish AIFM Act, or a corresponding foreign contractual special investment fund, which a) mainly invests in real estate or real estate securities within the meaning of the Finnish AIFM Act or b) whose assets are mostly (>50%) and either directly or indirectly comprised of real estate (the wording does not refer to Finnish real estate specifically).
- The reference to 30 investors technically refers to 30 investors calculated in accordance with the draft bill, meaning in practice that related parties (within the meaning of the draft bill) would be regarded as a single investor only.
- Foreign real estate investment funds subject to the proposed rules would only be considered fiscally transparent in relation to their Finnish source income (including non-real estate income and also including situations where the foreign real estate investment fund has Finnish investors) whereas Finnish real estate investment funds with fewer than 30 investors would be considered entirely fiscally transparent.
- While the wording of the suggested amendments presented in the draft bill cannot be considered entirely clear on this, the purpose of the fiscally transparent treatment is understood to only apply to foreign (and Finnish) real estate investment funds that would have otherwise qualified for tax-exempt status, meaning that a (foreign) real estate investment with fewer than 30 investors could be considered tax opaque but non-tax-exempt under the proposed rules.
- While the aforesaid tax treatment could technically apply to Finnish real estate investment funds, this is not expected as the rules for the tax-exempt status of real estate investment funds were drafted with Finnish real estate investment funds in mind.
- Lastly, the draft bill would not affect the tax treatment of non-contractual real estate investment funds with fewer than 30 investors (such as corporate funds), unless such funds would meet the criteria for tax exemption under Section 20 a of ITA and hence be eligible for the same tax-exemption as contractual real estate investment funds.

The draft bill also contains a number of other proposals, such as special rules to mitigate double taxation of profit distributions from real estate investment funds and rules concerning how e.g., tax depreciation on different assets held by real estate investment funds is to be determined for Finnish tax purposes. The draft bill would also introduce Finnish tax reporting obligations to foreign real estate investment funds subject to the proposed rules and their investors as well as potential tax liability considerations for unpaid tax for such foreign real estate investment funds.

Our view

The legislation proposed by the draft bill is considered to be extremely complicated. However, even the draft bill recognises that there are not likely to be many Finnish and/or foreign real estate investments funds that would be subject to the proposed legislation due to the 30 investor criterion. Therefore, while the rules and the tax treatment that follows are complex, as a starting point, we would expect the proposed legislation, if enacted, to only apply to a handful of foreign real estate investment funds.

As noted above, public comments on the draft bill are currently being collected, and the final bill is expected be published later this year. Therefore, the proposed rules may still be subject to change, and future developments should be monitored closely.

Your contacts

Global and regional contacts

Jeroen Elink Schuurman
Global Real Estate Tax Leader
Tax Partner, PwC Netherlands
Tel.: +31 6 53 98 48 10
jeroen.elink.schuurman@pwc.com

Ilona McElroy
EMEA Real Estate Tax Leader
Tax Partner, PwC Ireland
Tel.: +353 1 792 8768
ilona.mcelroy@pwc.com

Contacts – PwC Finland

Mikko Leinola
Real Estate Tax Leader
Tel.: +358 44 527 1617
mikko.leinola@pwc.com

Karin Svennas
Tax Partner
Tel.: +358 50 354 3906
karin.svennas@pwc.com

Petri Seppälä
Tax Partner
Tel.: +358 400 700 515
petri.seppala@pwc.com

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