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Agreement between Australia and Finland on the Avoidance of Double Taxation

Introduction

3.1 A new Taxation Agreement between Australia and Finland was signed on 20 November 2006. The proposed treaty action will replace both the 1984 Australia-Finland Agreement and First Protocol, and the 1997 Second Protocol.[1]

3.2 It is intended that the proposed treaty will update and enhance Australia's existing tax arrangements with Finland.[2]

Background

3.3 The entry into force of the 2001 Protocol amending the United States (US) Double Taxation Agreement[3] and the 2003 United Kingdom (UK) Double Taxation Convention[4] triggered the Most Favoured

1 NIA, para 2; Press Release, The Hon Peter Costello MP, Treasurer, p. 1.

2 Mr Michael Rawstron, *Transcript of Evidence*, 26 March 2007, p. 7.

3 *Protocol amending the Convention between the Government of Australia and the Government of the United States of America for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income;* see JSCOT Report 46.

4 *Convention between the Government of Australia and the Government of the United Kingdom of Great Britain and Northern Ireland for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and on Capital Gains, and associated exchange of notes*; see JSCOT Report 55.

Nation (MFN) obligation under the existing Australia-Finland Agreement, requiring Australia to enter into negotiations with Finland with a view to providing lower Withholding Taxation (WHT) rates for interest and royalty payments and to include rules that protect nationals and businesses from tax discrimination in the other countries.[5]

3.4 Australia's MFN obligations will be met when the new Treaty enters into force. The Treaty will enter into force when both countries advise that they have completed their domestic requirements. [6]

Purpose of the Agreement

3.5 It is proposed that the agreement will reduce rates of withholding taxes on dividends, interest and royalties and bring into line the treatment of capital gains tax with OECD practice and its improved integrity measures. [7] In particular, the Agreement includes rules to allow for the cross-border collection of tax debts and rules for the exchange of information on tax matters.[8]

3.6 The Agreement is expected to: meet Australia's most favoured nation obligations with Finland;[9] reduce barriers to trade and investment caused by overlapping taxing jurisdictions between Parties thus promoting closer economic cooperation with Finland; and help prevent tax evasion.[10]

Obligations

3.7 Key obligations under the Agreement with Finland are:

- The relief of double taxation on cross-border income (Article 22);[11]
- A general principle of non-discrimination, which requires each State to treat nationals of the other no less favourably than it treats its own nationals (Article 23);

5 NIA, para. 6.
6 NIA, para. 3.
7 NIA, para. 4; Organisation for Economic Cooperation and Development.
8 NIA, para. 4.
9 NIA, para. 3.
10 NIA, para. 5.
11 NIA, para. 16.

- Mutual agreement procedures for dispute resolution of issues that arise from the Treaty, including a mechanism for individuals to complain about the operation of the Treaty (Article 24);
- A specific obligation to gather and provide information upon request has been created between the two States (Article 25);
- Each State receiving information should treat it in the same manner as information obtained under its domestic laws (Article 25(2));
- Either State is allowed to decline to provide information requested in some circumstances, such as where to do so would be contrary to law or public policy (Article 25(3));
- Each State is obliged to take certain action to assist in the collection of taxes owed to the other State, (although the requirement to provide assistance is not absolute) subject to certain conditions and limitations (Article 26);[12] and

3.8 The Agreement does not impose any greater obligations on Australian residents than Australian domestic tax laws, and may actually reduce the obligations of Australians operating or investing in Finland (Articles 10 (*Dividends*), 11 (*Interest*), and 12 (*Royalties*)).

Entry into force and withdrawal

3.9 The Agreement will enter into force 30 days after the date of the last notification that Parties' domestic requirements have been met (Article 28). The provisions of the Treaty will generally have effect from 1 January or from the beginning of the year of income in the year following entry into force.[13]

3.10 Article 25 (exchange of information) will have effect from the date of entry into force, and the Parties must identify in an exchange of notes when Article 26 (assistance in collection of tax debts) will come into effect.[14]

12 NIA, paras 16-18.

13 NIA, para. 1.

14 NIA, para. 1.

Legislation

3.11 Prior to the Agreement coming into force in Australia, the *International Tax Agreements Act 1953* will be amended to include the treaty text as a schedule.[15]

Consultation

3.12 The Board of Taxation conducted a Review of International Taxation Arrangements on the direction of Australia's tax treaty policy. The Board's recommendations supported a move towards a more residence-based treaty policy (reflected in most of Australia's treaties, including the existing Australia-Finland Convention) in substitution for treaty policies based on the source taxation of income.[16]

3.13 Consultation with the business community occurred through the Tax Treaties Advisory Panel[17] and, more broadly, submissions from stakeholders and the wider community were invited in November 2003. Business and industry groups generally supported similar outcomes to those in the 2003 United Kingdom Tax Convention and the 2001 United States Protocol. The Convention provides similar outcomes to those treaties.[18]

3.14 State and Territory Governments were consulted via the Commonwealth-State/Territory Standing Committee on Treaties in October 2003.[19]

Costs

3.15 Costs associated with the Agreement are expected to be negligible.[20] Compliance costs are expected to be reduced through closer alignment with international treaty practice.[21] Administrative costs

15 NIA, para. 20.

16 NIA, Attachment A, para 1.

17 Members include: Business Council of Australia, CPA Australia, Corporate Tax Association, Institute of Chartered Accountants, International Fiscal Association, Investment and Financial Services Association, Law Council of Australia, Minerals Council of Australia, Taxation Institute of Australia. NIA, Attachment A, para 2.

18 NIA, Attachment A, para 3.

19 NIA, Attachment A, para 4.

20 NIA, para. 21.

21 NIA, para. 22.

associated with implementing the Agreement will be managed within the Australian Taxation Office (ATO) and Treasury Budgets.[22]

3.16 Treasury expects that the proposed interest withholding tax rate changes will reduce the effective cost of borrowing as Australian borrowers bear the burden of tax through “gross up” clause arrangements.[23]

3.17 As a result of the reduction in the cost of borrowing from Finland, Treasury expects that the Agreement could lead to an increase in economic activity and foreign investment in Australia. The increase in economic activity is likely to lead to increases in other forms of tax collection.[24]

Future double taxation treaties

3.18 The Department of Treasury informed the Committee that as part of Australia’s obligation under the *most favoured nation* clauses in other existing treaties there are a number of treaties which will come before the Committee at a future date.[25]

Conclusion and recommendation

3.19 The Committee accepts that the Agreement between Australia and Finland on the Avoidance of Double Taxation is a revised version of an existing treaty and is satisfied that the key changes to the treaty will further aid in the elimination of obstacles to investment as a result of international double taxation and will be beneficial in building better economic relationships between Australia and Finland.

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22 NIA, paras 23 and 24. There will be some second round impacts on taxation revenue, i.e. impacts that arise as the changes introduced by the treaty flow through to prices, wages and other economic activity. Treasury does not quantify the second round impact of minor policy proposals as the benefits are too small to measure with any degree of certainty.

23 NIA, para. 25.

24 NIA, para. 26.

25 Ms Lynette Redman, Transcript of evidence, 26 March 2007, p. 8.

Recommendation 2

The Committee supports the *Agreement between Australia and Finland on the Avoidance of Double Taxation* done at Melbourne on 20 November 2006 and recommends that binding treaty action be taken.