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Abbreviations

English	German	English	German
CC	UGB	Commercial Code	Unternehmensgesetzbuch
CITA	KStG	Corporate Income Tax Act	Körperschaftsteuergesetz
CITGI	KStR	Corporate Income Tax Guidelines	Körperschaftsteuerrichtlinien
ConvA	UmwG	Conversion Act	Umwandlungsgesetz
EU-MA	EU-VerschG	EU-Merger Act	EU-Verschmelzungsgesetz
FLG	BGBl	Federal Law Gazette	Bundesgesetzblatt
FTA	BAO	Federal Tax Act	Bundesabgabenordnung
ITA	EStG	Income Tax Act	Einkommensteuergesetz
MD	FRL	Merger Directive	Fusionsrichtlinie
RTA	UmgrStG	Reorganisation Tax Act	Umgründungssteuergesetz
RTGI	UmgrStRl	Reorganisation Tax Guidelines	Umgründungssteuerrichtlinien
SCEA	SCEG	Societas Cooperativa Europaea Act	Scoietas Cooperativa Europaea-Gesetz
SEA	SEG	Societas Europaea Act	Societas Europaea Gesetz
Sec.	§	Section	Paragraph
PE	BS	Permanent establishment	Betriebsstätte

Survey of the Implementation of Council Directive 90/434/EEC

(The Merger Directive, as amended)

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Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
<u>Overall state of implementation</u> The Merger Directive was widely implemented in before the accession of Austria to the EU in 1995 by the Austrian Reorganization Tax Act of 1991 in its original version BGBl 1991/699. With Austria's accession to the EU the Austrian RTA was adapted in order to comply with the Merger Directive by BGBl 1994/681. The Austrian Reorganization Tax Act has been amended several times in the following years. The tax changes regarding the Societas Europaea and cross border transfers required by the amendment of the Merger Directive have been included in the Tax Reform Act 2004 (AbgÄG 2004, BGBl I 2004/180). The Austrian Ministry of Finance has also issued Guidelines in order to interpret the Reorganization Tax Act. The original version was issued in 2002. The Guidelines have been updated several times since then. The SE Regulation (Nr. 2157/2001) has been implemented by the federal SE-Act ('SEG') BGBl I 67/2004 and has entered into force on October 8, 2004. The SCE Regulation (Nr 1435/2003) has been implemented by the federal SCE-Act ('SCEG') BGBl 2006/104 and has entered into force on August 18, 2006.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> The expression 'in which companies from two or more Member States are involved' has been interpreted as encompassing only the merging companies. In principle the Austrian RTA covers (a) all mergers based on the Austrian law (mergers between Austrian companies and mergers involving EU-companies); and (b) all mergers between non-Austrian companies which are based on comparable legal rules (dissolution of the transferring company without liquidation). The Austrian RTA does not explicitly mention the mergers of SEs or other EU-companies, but refers to legally permitted mergers. Due to the	Sec. 1(1) 4 RTA Sec. 29 RTGl

implementation of the SE-Act mergers including the mergers of SEs and the newly incorporated EU-Merger Act ('EU-VerschG') also cross-border mergers with EU-companies are now legally permitted and thereby fall within this provision. In order for the RTA to apply the involved companies must be comparable to Austrian corporate entities from a legal perspective regarding the corporate form. In addition the reorganization (e.g. merger) must be comparable from its legal requirements and consequences to Austrian corporate law (e.g. in case of a merger: dissolution of the transferring entity without liquidation ... as also described in the Merger Directive). In all cases the benefits of the RTA only apply if Austria's right to tax hidden reserves and goodwill is not restricted after the merger. However in case that the transferee is an EU-company or a comparable company resident in the EEA having a treaty regarding the recovery of taxes with Austria, the taxation of hidden reserves can be deferred upon request of the transferor until the assets are actually sold or transferred by the transferee. The same principles also apply to divisions and contributions under the RTA. Tax deferral is granted if Austria looses its taxing right in relation to other EU-member states (and certain EEA countries). The taxpayer has to apply for deferral with the tax return. If tax deferral is granted, the tax is assessed but not levied. Full tax deferral is not granted for hidden reserves in self-generated long term intangibles (e.g. good-will) if the state that receives the taxing right allows a capitalization of the intangible at entrance. At those intangibles costs deducted in the past when generating the intangible (estimated as 65% of the capitalized value if actual costs are not proved) will be taxed immediately – only the remaining portion will be deferred upon application. Summarizing, deferral is granted if the following criteria are met: (a) taxing right is lost in relation to an EU member state (or specific EEA countries); and (b) taxpayer applies for deferral; and (c) deferral is not fully granted for certain intangibles. Neither the wording of the RTA nor the RTGI refer to the parent companies in general. However in case of contributions of Austrian assets held by a non-resident that are contributed to a first-level Austrian company, the treatment depends on whether the contributor is resident in an EU/EEA Member State or a third state. Only in case of a resident in an EU/EEA Member State the contribution occurs at book value, otherwise hidden reserves are taxed. Please note that all corporate entities covered by the Directive are listed in an annex to the RTA. RTA also applies to comparable foreign mergers. This should normally encompass other EU-mergers. It is necessary that the merger is a	Sec.1 (2) RTA and Sec. 6 (6) IITA Sec. 16(2) RTA

dissolution of the transferring entity without liquidation. Payments to shareholders exceeding payments allowed to according to Austrian rules (max 10% of granted shares) might be harmful according to the RTGI.	

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
<u>**1.2 Foreign Member State and third state merger**</u> The RTA does not refer to the parent companies. The benefits of the RTA depend on whether the merger leads to a loss of the Austrian taxation right regarding the transferred assets. If Austria loses the taxation right, because the assets are transferred to an EU-company, the transferor can request a deferral of the taxation of hidden reserves. Thus a deferral of the taxation is granted in case of mergers with EU-companies, but not in case of mergers with non-EU companies if Austria thereby loses the taxation right. (please see 1.1) Thus it is not decisive where the parent companies of the merged companies are located. The same principles apply analogously to divisions and contributions under the RTA.	Sec. 1(2) RTA

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
<u>**2.1 The term 'securities'**</u> The RTA includes the requirement for an exchange of securities for contributions in Sec. 19 (1) RTA. The term securities is defined in the RTGI for contributions and comprises (a) shares (nominal capital); (b) participation rights according to the Banking Act and Insurance Regulatory Act; (c) profit participation rights (entitling the holder to a participation in all the profits and liquidation proceeds of the company). In case of mergers and divisions there is no definition in the RTA or in the RTGI. The requirement of issuing securities and their definition is included in the relevant corporate statutes (*'AktG' – 'Aktiengesetz',' GmbhG'* –	Sec. 19(1) RTA Sec. 1030 RTGI

'GmbHGesetz', 'SpaltG'- 'Spaltungsgesetz'). In both cases securities are interpreted as shares (nominal capital) in the commentaries.	

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
<u>**2.2 The term 'cash payments'**</u> For contributions the RTA provides that the issuance of securities is not necessary in so far as the transferee makes a cash payment for the purpose of rounding the holding percentage, if this cash payment does not exceed 10% of the total nominal capital of the newly issued shares. These cash payments are therefore only allowed for rounding the holding percentage and to round the total resulting nominal capital, but not for a cash buy-out of minority shareholders. The rule regarding cash payments in case of divisions can be found in Sec. 2(1)3 SpaltG, thus in the corporate statutes regarding divisions. In case of divisions cash payments of up to 10% of the newly issued the nominal capital are permitted. The rules regarding mergers are included in the corporate statutes of companies (*'AktG',' GmbHG'*). Cash payments are allowed, but may not exceed 10% of the shares granted by the receiving company. The 10% limit is calculated from newly issued shares and own shares used by the transferee to compensate the transferor. Also in case of mergers the purpose of the cash payments is seen in rounding the amount of the nominal share capital and the shareholding percentage. The 10% limit should avoid a cash-buy-out of minority shareholders. The 10% limit is therefore interpreted on an overall basis, but a cash buy-out is generally not permitted because of the purpose of the limited cash payment.	Sec. 19(2) 3 RTA Sec. 1052 RTGl Sec. 2(1) 3 SpaltG Sec. 224(4) AktG

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
<u>**2.3 Further types of merger**</u> Apart from mergers, contributions and divisions the RTA also includes the following types of reorganizations: (a) Conversions (*'Umwandlungen'*): There are two types of conversions according to Conversion Act (*'UmwG'*) which are both covered by the RTA. The first type is similar to a merger and allows transferring all assets and liabilities of a company to the majority shareholder (min. 90%) by a universal succession. The converted company ceases to exist without liquidation. This type of conversion is	Sec. 2 ConvA Sec. 5 ConvA

called 'merging conversion'.	
The second type is a conversion of a company into a partnership (also 90% majority required). All assets and liabilities of the company are transferred to a newly established partnership in a universal succession. 90% of the shareholders in the converted company must become partners in the newly formed partnership.	Sec. 7 RTA
The RTA provides that conversions are tax-neutral, if the hidden reserves and a goodwill remain subject to tax in Austria. If Austria loses the taxation right in case of a conversion to an EU-company, the taxation can be deferred until the transferee actually sells the transferred assets.	Sec. 23 RTA
(b) Formation of a partnership ('*Zusammenschluss*'):	
A partnership is formed in the meaning of the RTA, if qualifying assets are transferred only in exchange of shares to a partnership. Qualifying assets are businesses, business units and partnership interests. The transfer may generally occur at book value so that a taxation of hidden reserves or goodwill is avoided.	Sec. 27 RTA
If assets are transferred to a non-Austrian partnership, the same principle applies as to mergers. Thus if Austria loses the taxation right, a transfer at book value is generally not possible. However if the transferee is resident in the EU, a taxation of hidden reserves can be deferred until the assets are actually sold.	
(c) Partnership-division ('*Realteilung*'):	
A partnership-division is given if the assets of a partnership are transferred to the partners and the partnership is dissolved. The transfer generally occurs at book value under the RTA. Regarding the transfer to a non-Austrian successor the same principles apply as to mergers. Thus a transfer at book value is generally not possible. However if the transferee is resident in the EU, a taxation of hidden reserves can be deferred until the assets are actually sold.	
Please note that Austrian RTA was implemented prior to Austrian accession to the EU. Therefore the structure of the RTA does not exactly mirror the kinds of mergers listed in the Directive.	
Contributions would qualify as transfer of assets according to the Directive.	

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares The RTA covers the contribution of shares, if (a) the contributed shares constitute a minimum of 25% of the total nominal share capital; (b) the contributed shares together with already existing shares lead to or widen a majority of the transferee in the target company. According to the RTGI the RTA applies to contributions of even one share, if the transferee already owns the majority share in the target. The RTGI state that any minimum share which widens an existing majority is covered by the RTA. Thus according to the wording of the statute and the interpretation in the guidelines it is sufficient for the RTA to apply, if the contributed shares build-up an existing majority in the target company.	Sec. 12(2) 3 RTA Sec. 732 RTGI

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
2.5 Consolidation of qualifying holding No.	Sec. 12(2)3 RTA Sec. 732 RTGI

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
2.6 The term 'branch of activity' The RTA uses the term '*Teilbetrieb*' for a branch of activity and '*Betrieb*' for all branches of activities of a company. The wording of the RTA refers to the Income Tax Act regarding the definition of the term '*Betrieb*' and '*Teilbetrieb*'. Accordingly also the RTGI state that the term '*Teilbetrieb*' has to be interpreted in the same way as under the Income Tax Act and refer to the Income Tax Guidelines for the definition of a branch of activity. The	Sec. 12(2) 1 RTA Sec. 2(3) 1-3 IITA Sec. 714 RTGI Sec. 5501, 5578 ITGI

Income Tax Guidelines contain the following criteria which are based on several Supreme Court decisions: (a) part of a whole business; (b) organizational unit of the part within the whole business; (c) certain independence of the business part in comparison to the whole business; (d) independent viability of the business part. Part of a business means that it should not consist of single assets only, but that it does not constitute a whole business. A '*Teilbetrieb*' exists only if there are several coherent assets. The branch of assets must be separable from the remaining business without major organizational difficulties, thus it is required that a second branch of assets remains after the separation. A branch office does not automatically constitute a 'branch of activities', but there is a certain indication that a 'branch of activity' is given. The organizational independence of a branch of activity can be shown if several assets within a business form a unit (independent business function) and that an acquirer could continue the activity. For the criterion of the independence of the business part it is required that the business unit can be distinguished from the rest of the business activity. It is not sufficient that the independence is only given within the business – departments which only serve the whole business do not constitute a 'branch of activity' (e.g.: IT department, finance department, sales department etc.). The viability of the branch of activities requires that the acquirer receives the material basis for continuing the business. According to the Income Tax Guidelines the following elements indicate a branch of activity: (a) own fixed assets; (b) own stock of goods; (c) merchandise differs from other business unit; (d) local distance between the activities; (e) independent Organization; (f) own Administration; (g) own personnel; (h) own accounting and cost computation; (i) own invoices and letter head;	Sec. 714 RTGI

(j) own pricing; (k) own customers; (l) own marketing activity; (m) own trading license. The tax authorities look at the business as a whole so it would not be sufficient if for example only one of the above criteria is in existence. In the latest adaptation of the RTGI in August 2007 it was included in the guidelines that in case of cross-border contributions which fall within the scope of the Merger Directive the definition of a 'branch of activity' in the meaning of the Merger Directive is decisive. Thus, the newly applied concept for cross-border reorganizations is broader than the current concept for purely domestic reorganizations. Thus in cross-border contributions the interpretation of the Merger Directive prevails.	

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> The RTA generally applies to companies which are comparable to Austrian corporations and additionally requires in case of contributions that Austria has concluded a double tax treaty with the country in which the receiving company is located. The entities listed in the Annex to the MD are also listed in an Annex to the RTA. The current version of the Annex was amended after the accession of Bulgaria and Romania. The RTA refers to the Annex in the separate restructuring provisions.	Sec. 1(2) RTA, Sec. 7(2) RTA, Sec. 12(3) RTA

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>3.2 Transparent entities</u> Under Austrian tax law an entity is treated as a corporate entity, if it is comparable to an Austrian corporation from a corporate law perspective. The tax treatment in the other country as a corporate entity or as a transparent entity is not decisive in Austria. The criteria for the comparability from a corporate law perspective are: (a) the limited liability; (b) separate legal entity under foreign law; (c) the equity capital must be fixed and must belong to the company itself;	Sec. 29 RTGI, Sec. 551 CITGI

(d) one or more shareholders must own a share in the company's equity capital; (e) the shareholders have to be part of the decision making process. These criteria are set out in the Corporate Income Tax Guidelines; the Reorganization Tax Guidelines refer to this comparability test also for reorganization. Thus if a company listed in the annex to the Merger Directive is not included in the annex to the Austrian RTA and does not meet the comparability test, it will be treated as being transparent. Please note that a list with all entities in the scope of the Directive was included as annex to the RTA. All forms of entities listed in the annex to the RTA are treated as corporate bodies. Thus, they are treated opaque. According to our understanding the current list in the annex is up to date and complies with the consolidated version of the annex to the directive available at EUR-lex. Thus, our statements concerning transparent entities are not applicable to EU transactions at the moment. They are relevant in relation to third countries (potentially including EEA countries) and might be relevant in the future if Austria happens to miss a deadline for implementation if the list in the annex to the directive is extended.	

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
<u>3.3 Qualification of tax residency</u> A corporation is tax resident in Austria, if it has its place of management or its seat in Austria. In case of a double residency most of the Austrian double tax treaties provide that the company shall be deemed to be a resident only where the place of effective management is situated.	Sec. 1 CITA

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>3.4 Subject-to-tax clause</u> A subject-to-tax clause of Article 3 c of the Merger Directive as such has not been included in the RTA. In case of transfer of assets (contributions) the receiving entity must generally be subject to unlimited Austrian taxation (or must be an EU-company), otherwise the contribution is not within the scope of the RTA.	Sec. 12 (3) RTA

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>3.5 Shareholder requirements</u> The ownership of the companies is not relevant for the application of the RTA.	

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>4.1 The concepts of 'real values' and 'value for tax purposes'</u> (a) Real value: In case RTA does not apply, surrendering entities are qualified as being liquidated. Surrendered assets (and liabilities) are appraised at fair market value. (b) Value for tax purposes: The surrendering entity has to appraise the assets and liabilities at values used in current tax accounting (valuation rules of IITA and CITA for going concern purposes) at the time of the reorganization. The absorbing entity has to continue with these values. In case RTA is applicable, this concept ensures that accrued reserves are not taxed at reorganization. Please note that this concept is mainly applied to accrued reserves that remain subject to tax in Austria. In case another Member State assumes taxing rights in accrued reserved, accrued reserves are subject to tax but the tax is deferred (similar to the exit taxation). In case accrued reserves are transferred to the taxing power of a third state, gains are taxed immediately. According to our knowledge it was not discussed in Austria whether this is an infringement of the Directive. Taxation would not apply to hidden reserves attributable to a PE (or other asset) that remains subject to tax in Austria. Still, this might (also) be an issue concerning fundamental freedoms. Please note that in case intangible long-term assets are transferred to an EU/EEA country and capitalized in the other state, Austria taxes the accrued reserves without option for deferral. Article 4(2) of the Directive only asks for carry over of book value if the receiving entity continues with these book values. The specific regime for taxation of hidden reserves in long term intangible assets only applies if the other Member State capitalizes these assets (although they were not capitalized in Austria and thus meaning no continuity of book values).	Sec. 19 and 20 CITA Sec. 2(1) and 3(1), Sec. 8(1) and 9(1), Sec. 16(1), 17(1) and 18(1), Sec. 33(1) and 34(1) RTA

Thus, this could be in line with Article 4(2). Still, this might be an issue concerning fundamental freedoms. Please note, that in case a foreign state taxes gains at reorganization and the tax treaty applies the credit method, taxpayers are normally allowed to opt for taxation of those foreign gains in Austria to enable credit of foreign tax.	

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions Tax rules on divisions and partial divisions apply the principles explained above. RTA can only be applied if the de-merged assets are a business (‘*Betrieb*’), a branch of business (‘*Teilbetrieb*’), shares in a transparent partnership or a qualifying share in a company (a share of at least 25% or a share that achieves or widen a majority in voting at the recipient). Please note that in case of a partial division only the de-merged assets have to fulfill the criteria. In case of a division, all parts have to fulfill the criteria. In Austria a tax-neutral (partial) division is only possible if a business (‘*Betrieb*’), a branch of business (‘*Teilbetrieb*’), shares in a transparent partnership or a qualifying share in a company (a share of at least 25% or a share that achieves or widen a majority in voting at the recipient) are concerned. According to our knowledge it was not discussed in Austria whether this is an infringement of the Directive. De-merged assets refer to assets that were transferred in a (partial) division.	Sec. 32 et seq RTA

How have the Article 4(1)(b) concepts of ‘effectively connected’ and ‘permanent establishment’ been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of ‘effectively connected’ and ‘permanent establishment’ A permanent establishment is a fixed place of business. The definition is similar to the one used in the OECD model. Assets are effectively connected to a permanent establishment if they are attributable to the permanent establishment from an economic perspective (substance over form). According to our knowledge no specific definition or guideline is available for RTA purposes. The concept of continuing of tax book values (‘Buchwertfortführung’) is only applied if the Austrian taxing right in the accrued reserves (including good will) is not reduced. This will be the case if the assets (including hidden reserves and goodwill) are effectively connected to an Austrian	Sec. 1(2) RTA

permanent establishment. Otherwise capital gains are taxed. In case taxation right is shifted to EU countries or EEA countries that provide full mutual administrative and recovery assistance the levying of tax is deferred. The administration provides guidelines in which cases the taxing right is reduced (in case of mergers): (a) Shares are not attributable to an Austrian PE and the tax treaty does not allow taxation in Austria. (b) Shares do not belong to a permanent establishment and domestic law does not provide a taxing right. (c) Foreign assets (that were subject to tax in Austria due to the fact that no tax treaty exists in relation to the source state or it provides for the credit method) are transferred to a foreign entity. (d) Property subject to Article 8 of the OECD-Model Treaty will not be subject to tax in Austria any more due to the fact that the place of effective management of the business is transferred.	

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
<u>**4.4 Limitation of the scope of relief**</u> Confusion profits (profits resulting from the uniting of receivables and liabilities if the liability was depreciated) are taxable. According to our knowledge it was not discussed in Austria whether this is an infringement of the Directive. Taxation of confusion profits only means the recapture of earlier tax deductions (earlier depreciation of intercompany loans that cease to exist due to the merger). In case of existing loss-carry forwards at the level of the subsidiary and the fact that the parent claimed depreciation on their participation in the subsidiary, loss-carry forwards that are transferred to the parent are reduced by the depreciation in the participation to avoid a double-dip.	Sec. 3(3), 34(2) RTA Sec. 4(1) RTA

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment Gains are subject to tax. In relation to EU countries taxation might be deferred (see 4.3).	

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company Austria did not use the possibility to tax specific gains according to Article 7(2) MD. Gains are exempt.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral In case Austria's taxing rights are restricted in relation to EU Member States or EEA Member States that provide for full mutual administrative assistance and assistance in the recovery of tax claims, gains are subject to tax but the levying of tax is deferred (see 4.3). Please note that these rules were implemented before the decision in *'N'*.	

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities In general Austria applies the '*Typenvergleich*' (please see 10a). In case assets are transferred to Austria which were not subject to tax before the reorganization, Austria will grant a step up to fair market value.	Sec. 3(1)2, 9(1)3, 17(2), 18(1)3 RTA

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief A merger has to qualify as merger under company law to benefit from tax-neutral treatment (e.g. payments to (former) shareholders are only allowed up to 10%, the merger has to be filed with the commercial register within 9 months after the date for merger). If a reorganization does not have to be filed with the commercial register (e.g. contribution of shares), the reorganization has to be filed with the tax office within 9 months after the date of the reorganization. Furthermore, the transferred assets must have a positive fair market value.	Sec. 1(1), 7(1), 13(1), 32(1)

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
5.1 The term 'provisions and reserves' Austria applies the authoritative principle ('*Maßgeblichkeit*'). Provisions and reserves are basically defined in the commercial code ('*Unternehmensgesetzbuch*'). Not all provisions are tax deductible. Lump-sum provisions are not tax deductible (specific reasons for the allocation to provisions have to at hand at the end of the financial year). Provisions without an obligation in relation to third parties ('*Aufwandsrückstellung*') are not tax deductible. Long-term provisions can only be accrued at 80% for tax purposes (this shall be a kind of discounting). Furthermore, tax law provides for specific rules for the allocation to provisions for personnel costs (prerequisites for tax effective allocation, method of calculation, interest rate for discounting future claims etc.). The provisions should be transferred together with the business to which they are connected from an economic perspective (substance over form). For personnel costs they should be linked to the business in which the personnel are employed.	Sec. 198(8), 211 CC Sec. 9, 14 IITA

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments Austria taxes resident taxpayers on their world-wide income. Thus,	Sec. 1(2) IITA, Sec. 1(2) CITA.

provisions and reserves are also tax deductible or taxable (according to the rules laid down in 5.1) if they are attributable to a foreign PE. However, Austria applies the exemption method for business income according to most tax treaties. If such a tax treaty is applicable, allocations to reserves which are attributable to foreign PE are not tax deductible. Please note that if the foreign PE is in a loss-situation and the loss cannot be used abroad, the loss is deductible in Austria. A recapture rule applies. In the case of reorganizations the receiving entity generally inherits the tax book values of the surrendering entity. Thus, provisions and reserves are carried over to the receiving entity. However, this general rule does not apply if the right for taxation of units (e.g. branches) is restricted due to the reorganization. In that case all assets (and liabilities as well as provisions) are assessed at fair market value. The gains are taxable. In relation to other EU-Member States and specific EEA-countries taxation is deferred. Furthermore, a taxpayer may opt to assess assets and liabilities (including provisions) at fair market value (to enable the credit of foreign taxes) if gains are taxed abroad due to the reorganization and the tax treaty provides for the credit method. This means that a kind of exit taxation applies if Austria loses its taxation rights on certain units (branches etc). According to our knowledge it was not discussed in Austria whether this is an infringement of the Directive. This might also be an issue concerning fundamental freedoms.	

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves De-merged parts have to qualify as business units (*'Betrieb'*), branches (*'Teilbetrieb'*), shares in partnerships or qualifying shares in companies. Liabilities (including provisions and reserves) connected to the assets are also transferred to the absorbing entity. Furthermore, the surrendering entity may decide to retain certain assets (the de-merged parts still have to qualify as one of the above mentioned category of assets). In that case liabilities directly connected to these assets will also remain at the surrendering entity. It is also possible to retain passive assets (liabilities and provisions). De-merger refers to a partial division.	Sec. 32(2) and (3), Sec. 16 (5) RTA

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves In case of de-mergers ((partial) divisions) and contributions, the assets have to qualify as business units, branches, partnership shares or qualified participations in companies. Austria's taxation right should not be restricted to obtain a tax-neutral	Sec. 32(2), Sec. 12(2) RTA Sec. 1 (2) RTA

carry over of assets and liabilities (including provisions and reserves). We only listed the cases where further conditions are set up. The need for qualifying assets is relevant at transfers of assets ('contributions') and (partial) divisions ('de-mergers').	

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry-over of losses Austrian RTA provides specific rules for the carry over of tax loss carry forwards. In case reorganization is effected in accordance with the rules provided by the RTA and the reorganization results in a carry over of tax book values, tax losses occurred in the surrendering company can also be carried over to the receiving company. They can be used by the receiving entity starting with the tax year following the date of the reorganization. However, loss carry-over is restricted in certain cases. Losses are only transferred if the business unit, branch or other asset that caused the losses is transferred. The business unit, branch or other asset has to belong to the surrendering entity at the date of reorganization (and has to be transferred). Furthermore, loss carry forwards at the level of the absorbing entity are lost if the business unit, branch or other asset that caused the losses ceases to be owned by the receiving entity. Additionally, business units, branches or other assets have to exist in a comparable size to allow for future use of tax loss carry forwards. The Austrian tax administration interprets a reduction in size of the unit of 75% as being not comparable. The tax administration links the size of the unit to its revenue, volume of orders and production volume, long term assets, current assets, balance sheet total, number of employees. In the case of mergers between parent and subsidiary, the transferred losses of the subsidiary are to be decreased by tax effective depreciation of the participation in the subsidiary. Furthermore, changes of ownership rules are applied. If a substantial change of the shareholders coincides with a substantial change in the organizational (management) and economic structure, losses may be lost. Changes at transferring and the receiving entity are considered together when assessing whether substantial changes happened.	Sec. 4, 10, 21, 35

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment Tax loss carry forwards are attached to the units that created them. In case the unit (business unit, branch or other asset) is transferred, the loss is also transferred. In case the unit remains with the transferring entity, the tax loss carry forward remains with the transferring entity. If	Sec. 4, 10, 21, 35

the unit ceases to exist, the tax loss carry forward is lost.	

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets The above mentioned principles apply (please see 6.1 and 6.2).	

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses The abovementioned principles apply to all reorganizations. Please note that the Austrian Ministry of Finance published certain decisions that certain reorganization measures could be used to use foreign tax loss carry forwards in Austria. These opinions were repealed 2006. Therefore foreign losses cannot be pulled into Austria. At least if the loss carry forwards cannot be used abroad after the reorganization, this seems to constitute an infringement of the fundamental freedoms as interpreted by the ECJ in '*Marks & Spencer*'.	BMF 14. 2. 2002, EAS 1992; BMF 18. 11. 2002, EAS 2110; BMF 24. 7. 2003, EAS 2339; BMF 21. 12. 2006, GZ BMF-010221/0666-IV/4/2006

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Amended holding threshold Article 7 of the Merger Directive has not been implemented. Gains are not taxed.	Sec. 3(2), 9(2), 18(5), 34(2) RTA

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses Gains are not taxed. Losses are not deductible.	Sec. 3(2), 9(2), 18(5), 34(2) RTA

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
<u>8.1 Avoidance of economic double taxation at the level of the shareholder</u> Austrian law provides for the principle of double taxation at both levels. Accrued reserves are taxed at the level of the company if the assets are sold. Reserves accrued in the shares are taxed as soon as the shares are sold. This concept is also transposed to the RTA. Concept of double taxation at both levels: In case hidden reserves are accumulated in a corporation, this leads to hidden reserves being taxable at the level of the corporation. Furthermore they lead to gains in the participation (taxable at the level of the shareholder). Thus, these hidden reserves are subject to double taxation looking at both levels (company and shareholder). In principle, reorganizations subject to RTA provide for carry over of book values for assets transferred from the surrendering entity to the receiving entity as well as for carry over of acquisition costs/book value for shares in the transferring entity to shares in the absorbing entity. Gains are not taxed at reorganization but remain taxable in the future. In case Austria's taxing rights are restricted due to the reorganization, gains (fair market value – tax book value/acquisition costs) are taxed at the moment of the reorganization. In case taxing rights are restricted in relation to EU-Member States (or specific EEA-countries), the concept of deferred taxation is applied. Please see 4.1 for a description of the concept of tax deferral and for comments on a potential infringement of the Directive. In case of contributions (transfer of assets), gains in the assets and the participation have to remain taxable to allow for tax-neutral contribution. In case Austria gains taxing right, assets are assessed at fair market value at the time of the reorganization. Austria applies a split model at the taxation of gains in shares privately held by individuals. On disposal within 1 year after acquisition, gains are taxable at full tax rate ('*Spekulationsüberschuss*'). If shares are held for more than 1 year, gains are only taxable if the taxpayer holds a share of at least 1 percent. These gains are taxable at half the average tax rate. Gains are also taxable if the taxpayer holds less than 1% at alienation but held at least 1% within 5 years before the disposal. In case the participation falls below 1% due to reorganization, gains remain taxable at alienations within 10 years after the reorganization.	Entity level: Sec. 2 and 3, 8 and 9, 16, 17 and 18, 33 and 34 RTA Shareholder level: Sec. 5, 20, 36 and 37 RTA Sec. 1(2), 5(1), 7(2), 16 (1 and 2), 20(2)2, 36(3) RTA Sec. 16(2) RTA Sec. 3(1)2, 9(1)3, 17(2), 18(1)3 RTA Sec. 5(3), 20(5), 37(3) RTA

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>8.2 Computation of the capital gain</u> (a) Mergers: The acceptance of a compensation offer (‘*Abfindungsangebot*’) is deemed to be a disposal. A compensation offer is an offer for payment to minority shareholders to accept a cash payment instead of shares in the receiving company (squeeze out). (b) Conversions (‘*Umwandlungen*’): The payment of compensation payments is deemed to be a disposal. (c) Contributions (Transfers of assets): Compensation payments are allowed to achieve participations of the individual shareholder amounting to integral percentages. The payments may not surmount 10% of the nominal value of shares newly issued due to the contribution. Payments decrease the book value of the shares at the recipient. In case a shareholder would receive a share of 8.2% in consideration for the transferred assets it is allowed to arrange for a cash payment so that he will only receive a share of 8%. (d) Divisions: Payments are allowed up to 1/3 of the fair market value of the received shares. They are taxed as disposal proceeds for the recipient and are acquisition costs for the payer.	Sec. 6(3) RTA Sec. 11(2) RTA Sec. 20(2)3 RTA. Sec. 37(4) RTA

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>8.3 Further conditions for tax relief</u> No minimum holding periods apply except for the question of exemption from capital and stamp duty. Supply of equity to a corporation by a shareholder is subject to 1% capital duty (please note that certain exemptions are available like in case of all asset deals). Furthermore transfers of certain assets may trigger stamp duty. In general this is also true in case equity is supplied or assets are transferred due to reorganizations. However, the RTA provides for exemptions. Still, these exemptions normally require a minimum holding period of 2 years. No nationality requirements apply. Please see 8.1 concerning issues if the Austria’s taxation power is restricted or enlarged.	Sec. 1(1), 7(1) RTA

Mergers and conversions have to be effected in line with Austrian commercial law or comparable foreign provisions.	

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>**9.1 Avoidance of economic double taxation at the level of the transferring company**</u> Austria applies taxation at entity and at shareholder level. Economic double taxation is part of the Austrian system. Accrued reserves remain taxable at both levels at contributions. For further details please see 8.1. Accrued reserves in this context mean hidden reserves. This is the difference between book value and fair market value.	

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>**9.2 Further conditions for tax relief**</u> Tax-neutral contributions are possible if the following requirements are fulfilled: (a) The contributed assets have a positive fair market value. (b) The contributed assets qualify as one of the following categories: • business unit ('*Betrieb*'); • branch ('*Teilbetrieb*'); • shares in a transparent partnership ('*Mitunternehmeranteil*'); • qualifying shares in a company ('*Kapitalanteil*') if - a share of at least 25% is contributed, or - the shares lead to or widen the majority held by the recipient. (c) The recipient is • an Austrian company, or • an EU-company, or • a comparable foreign company if a tax treaty exists between Austria and the state of residence. The contribution has to be filed with the commercial register or the tax	Sec. 12 RTA Sec. 13 RTA

office within 9 months of the effective date. Please note that Austrian RTA was implemented prior to Austrian accession to the EU. Therefore the structure of the RTA does not exactly mirror the kinds of mergers listed in the Directive. Contributions would qualify as transfer of assets according to the Directive.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>9.3 Tax deferral</u> Austria taxes gains in the assets and/or the shares if Austria's taxation right is restricted due to reorganizations. If the taxing right is restricted in relation to other EU-Member States (or specific EEA-countries), levying of taxation is deferred (Please see 4.7 and 8.1).	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Loss recapture for permanent establishments in third Member States</u> No.	

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> In case an Austrian taxpayer contributes qualified assets (e.g. a PE) to a foreign company and this leads to a restriction of Austria's taxing rights, Austria would tax the reserves accrued in the assets at contribution. In case Austria's power to tax is restricted in relation to EU-Member States (or specific EEA-countries) the concept of tax deferral is applied. The question remains whether the contribution leads to a restriction of Austria's taxing power. Austria normally applies the exemption method for business income in its tax treaties. Thus, the contribution should not lead to a restriction of Austria's taxing power. Consequently gains would not be taxed at contribution. Please note, that the guidelines on the application of the RTA (RTGI) issued by the Austrian ministry of finance even apply the carry-over of book values in an example concerning a contribution of an Italian PE to an Italian company although the tax treaty AUT-ITA provides	Sec. 16(1) RTA Sec. 858 RTGI

for the credit method. Thus, it seems that gains would not be subject to tax if an Austrian taxpayer contributes its foreign PE to a foreign company resident in the EU Member State of the PE. Please see 4.1 for a description of the concept of tax deferral and for comments on a potential infringement of the Directive.	

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> Austria would only tax accrued reserves if the reorganization would restrict Austria's taxing power (please see 10.2). In case this would occur in relation to EU Member States (or specific EEA-countries), deferred taxation would apply. Please see 4.1 for a description of the concept of tax deferral and for comments on a potential infringement of the Directive.	Sec. 16(1) RTA, Sec. 858 RTGI

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
<u>10.4 Tax deferral</u> If Austria's taxing power is restricted in relation to EU-Member States (or specific EEA-countries), deferred taxation is applied. Thus, the amount of tax due would be assessed at the moment of the reorganization. However, levying taxes would be deferred until: (a) The assets are alienated or (b) a further transfer/reorganization would lead to a transfer of taxation power to a third state. Declines in value between reorganization and alienation would only be taken into account if they are not taken into account in the other Member State. Due to the absolute period of limitation of 10 years, a later event that in principle would trigger taxation should not lead to an effective levying of taxes. Due to the concept of deferral tax is assessed but not levied in the year of the reorganization (leading to a loss of Austrian taxing rights). Effective levying of taxes requires a reopening of the assessment. However, after the absolute period of limitation an assessment cannot be reopened anymore (even if new facts or additional information gets known that concerns this year). Thus, without possibility to reopen and re-assess this	Sec. 1(2) RTA Sec. 207 FTA

year, it should not be possible to levy tax for this year (including deferred tax). Please see 4.1 for a description of the concept of tax deferral and for comments on a potential infringement of the Directive.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies Hybrid entities should be entities that are qualified as transparent in one and as opaque in another state. Foreign entities are qualified as one or the other according to their comparability to Austrian entities from a corporate law perspective. Austria has not opted for implementing a specific rule for hybrid entities in RTA. Austria would strictly apply the rules that are applicable due to their characterization as corporate or partnership. However, please note that Austria has included a list with all entities in the scope of the Directive in the annex to the RTA. This should avoid characterization conflicts concerning these entities. (please see 3.2) For purposes of direct taxes, Austria ignores transparent partnerships and taxes at the level of the (non-transparent) shareholder. Austria treats foreign companies according to the '*Typenvergleich*' as transparent or non-transparent. 10a.1.1 Fiscally transparent transferring (surrendering) entity (a) Merger In case surrendering company would be qualified as transparent partnership, RTA for mergers might not be applicable (if the foreign corporate law rules enabling such a transaction would be qualified as not comparable to the Austrian merger rules). In that case it might be possible to qualify the transaction as transfer of assets (contribution) for Austrian purposes. As a transfer of assets (contribution) of business units, branches and shares in partnerships qualifies for a transfer of assets (contribution) according to the RTA, a tax-neutral transaction might be possible. Tax regimes are applicable in accordance with the characterization as corporate or partnership. There is no specific rule for hybrids included in the RTA. According to our knowledge there is neither in the published opinions of the tax administration nor in academic literature guidance on the treatment of hybrids. Thus, there is not sufficient foundation to give more precise answers.	

(b) Conversion The conversion is a transformation of a subsidiary into part of the property of the shareholder (or into a partnership if there is more than one shareholder). In case the subsidiary is already qualified as partnership, conversion is not possible. If there is more than one shareholder, and the entity is qualified as partnership, the assets are already partly owned by the shareholders for Austrian tax perspective. A further conversion should have no tax effect. If minority shareholders receive compensation payments in the course of the conversion (squeeze-out), this would be taxable as (potential) profit on the disposal of shares. In case the foreign entity is qualified as partnership, compensation payments would be taxable as (potential) profit on the disposal of partnership shares. (c) Transfer of assets (Contribution) In case the transferring entity (contributor) is transparent entity, Austria would link the question whether RTA is applicable to the shareholder of the partnership. Since there are no further requirements concerning the transferring entity (contributing taxpayer), the qualification of the transferring entity (contributor) as partnership (and the look-through to the next level) should not have adverse tax effects. RTA allows for tax-neutral transfer of assets (contribution) of shares in companies as well as of shares in partnerships. Thus, in case the transferred (contributed) assets would qualify as share in a partnership instead of a share in a company, a tax-neutral transfer of assets (contribution) should also be possible. Please note that the requirements for transferred (contributed) shares in companies are even tighter (a minimum share of 25% or it leads to or enlarges a majority) than in case of a transfer (contribution) of shares in a partnership. Thus, shares in companies qualifying for the benefits of RTA should also qualify for benefits if they are characterized as shares in a transparent partnership. Differences might arise due to the fact that capital gains in international holding participations are tax exempt by default whereas gains in (foreign) transparent partnerships are taxable (unless the tax treaty provides for the application of the exemption method). (d) Division In case the foreign entity is qualified as a partnership, the rules for divisions would not be applicable. However, Austrian RTA provides for a rule to divide partnerships (‘*Realteilungen*’). Tax consequences of ‘*Realteilungen*’ are comparable to those of divisions. Please note that assets that are de-merged of a company have to qualify as business unit (‘*Betrieb*’), branch (‘*Teilbetrieb*’), share in a partnership (‘*Mitunternehmeranteil*’) or qualified shares in companies (‘*Kapitalanteile*’). This is basically also true for de-mergers of parts of a partnership (‘*Realteilungen*’). However shares in a company are not eligible for beneficial treatment at ‘*Realteilungen*’. Furthermore additional requirements have to be met to qualify for tax-neutral ‘*Realteilung*’.	

<u>10a.1.2 Fiscally transparent receiving (absorbing) entity</u> (a) Merger In case one of the involved entities is qualified as partnership the transaction would not qualify as a merger. If the receiving entity is qualified as partnership the transaction this would lead to a taxation of the gains. However, please note that it might be possible to structure the transaction as conversion of the company to a partnership followed by a '*Zusammenschluss*' (merger rules for transparent partnership). Please note that this might be a possibility to achieve a tax-neutral treatment if specific requirements are met. However, additional requirements would apply. (b) Conversion A conversion of the surrendering entity is possible if the receiving entity is a company (main shareholder) or if the receiving entity is a partnership. (c) Contribution Supply of assets can only constitute a contribution if the receiving entity is a company. In case the receiving entity qualifies as a partnership, the supply of assets might be qualified as '*Zusammenschluss*'. A '*Zusammenschluss*' could also be tax neutral. However, please note that specific requirements have to be fulfilled. Furthermore, supply of shares in companies does not qualify for a tax-neutral '*Zusammenschluss*'. (d) Division A division requires a company as receiving entity. If the receiving entity is qualified as a partnership, this would lead to a taxation of gains. Depending on the facts and circumstances, it might be possible to qualify the transaction as up-stream de-merger and possibly as '*Zusammenschluss*' to a foreign partnership. According to our knowledge there is neither in the published opinions of the tax administration nor in academic literature guidance on the treatment of hybrid entities. However, please note that all entities that are covered by the scope of the Directive are listed an annex to the Austrian RTA. Thus, the qualification as hybrid should be avoided concerning these entities. De-merged assets refer to assets that were transferred in a (partial) division.	

How have the 'profits' of an <u>acquired</u> company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
<u>10a.2 Tax base for notional tax credit</u> N/A. There is no notional credit. Austria applies the advantages of the directive assuming the foreign entity	

is comparable to an Austrian corporate entity. According to our understanding it did not exercise the option not to apply the directive in that case. There is no discussion whether this is an infringement of the directive.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit N/A.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders N/A.	

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company N/A.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation There are no special regulations for the transfer of the registered office of an SE. The general exit taxation rules of Sec. 6 para 6 Austrian Income Tax Act apply.	Sec. 6 para 6 IITA

According to Sec. 6 para 6 IITA an exit tax is triggered if assets which have been subject to taxation in Austria are transferred to another business unit of the same taxpayer outside Austria and Austria thereby loses its taxation right regarding the hidden reserves and the good-will. The exit taxation can be deferred if the assets are transferred to another EU-Member State until the assets are sold or otherwise transferred (please see 1.1). There is no exit taxation if the assets and goodwill remain subject to taxation in Austria after the transfer of the registered office. Please note that in case intangible long-term assets are transferred to an EU/EEA country and capitalized in the other state, Austria taxes the accrued reserves without option for deferral. Thus if a registered office of an SE is transferred from Austria to another EU-Member State, this only triggers an exit taxation on hidden reserves and goodwill for which Austria loses the taxation right. An exit taxation can however be deferred upon request. According to our knowledge it was not discussed in Austria whether this is an infringement of the Directive. Taxation would not apply to hidden reserves attributable to a PE (or other asset) that remains subject to tax in Austria. Still, this might (also) be an issue concerning fundamental freedoms.	

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' There are no specific definitions for the term 'head office' in connection with SE.	

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency According to the Austrian Corporate Income Tax Act a corporation is subject to unlimited corporate income tax based on its world-wide income in Austria, if it has its place of management in Austria or its corporate seat in Austria. The general term of a head office/place of management is defined in Sec. 27 para 2 Federal Tax Act as the center of the top management ('Mittelpunkt der geschäftlichen Oberleitung'). This term is determined further in the Corporate Income Tax Guidelines as the place where the necessary and important business decisions are actually taken. The corporate seat is determined by corporate law or the statute of incorporations. The Austrian double tax treaties generally follow Article 4(3) OECD Model	Sec. 1 CITA Sec. 27 para 2 FTA Sec. 6 CITGl

Convention. Thus in case of a dual residency the place of effective management is decisive. Thus generally the concept of 'head office' should coincide with the criteria used to determine the tax residency.	

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>**10b.4 Assets and liabilities not effectively connected with a permanent establishment**</u> If assets are not connected to a permanent establishment in Austria and the registered office is transferred out of Austria, Austria loses the taxation right and therefore the exit-taxation is triggered on the hidden reserves of the transferred assets. This exit-taxation can be deferred in relation to other EU-Member States upon request of the tax payer. (please see 1.1).	

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
<u>**10b.5 Tax deferral**</u> As mentioned Sec. 6 para 6 IITA includes an exit taxation which can be deferred upon request, the request has to be included in the tax payer's annual tax return. Please note that this concept was already in place before the judgment in the 'N' case. However, in case intangible long-term assets are transferred to an EU/EEA country and capitalized in the other state, Austria taxes the accrued reserves without option for deferral. Furthermore, declines in value after exit from Austria are only recognized for Austrian tax purposes if they are not taken into account abroad (please see 1.1). According to our knowledge it was not discussed in Austria whether this is an infringement of the Directive. Taxation would not apply to hidden reserves attributable to a PE (or other asset) that remains subject to tax in Austria. Still, this might (also) be an issue concerning fundamental freedoms.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 The term 'comparable circumstances' There is no specific definition of 'comparable circumstances'. The question whether a remaining permanent establishment can continue to carry forward the tax loss carry forwards after the registered office has been transferred is not clarified in the Austrian law or in the guidelines. According to an opinion in the literature the transfer of the registered office outside Austria has no impact on the availability of Austrian tax loss carry forwards for the remaining permanent establishment. In general persons subject to limited taxation may offset tax loss carry forwards which were incurred by an Austrian permanent establishment. However there is a restriction: the tax loss carry forwards may only be offset if the tax loss carry forwards exceed the world-wide income of the tax payer. According to the literature this restriction should not apply to losses which were incurred before the transfer of a SE's registered office because these losses were incurred as tax loss carry forwards by the SE while it was subject to unlimited taxation in Austria. In addition this restriction does generally not apply if the relevant double tax treaty prohibits the discrimination of permanent establishments. Such an anti-discrimination clause is included in most treaties with EU-Member States. Otherwise the restriction of the use of tax loss carry forwards may constitute a violation of EU-law.	*Schindler*, ecolex 2004, 770 Sec. 102(2) 2 IITA

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Loss recapture for permanent establishments Losses incurred by a permanent establishment in a third Member State can be offset in Austria if the company is resident in Austria. This applies in case of a credit method or of an exemption method in the double tax treaty. In case that the double tax treaty provides for the exemption method, the tax losses used in Austria must be recaptured at the moment when the losses can be used in the other state by a tax loss carry forward. Please note that the transfer of residence does not trigger recapture of foreign losses that were deducted during the time the taxpayer was an Austrian resident. However, later foreign profits will trigger recapture even if the taxpayer is only subject to limited tax liability at that time.	Sec. 2(8) 3 IITA Sec. 98(3) IITA

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>10d.1 Deemed liquidation</u> There is no special rule regarding the shareholders in a SE and the transfer of the registered office. Thus, the general rules of exit taxation apply. The transfer should not give rise to a deemed liquidation according to the Austrian understanding because the SE is not dissolved. No different rules were implemented for SCE. At the level of the shareholders the transfer of the registered office does not give rise to taxation according to the literature, because there is no taxable event at the level of the shareholders. Please note that there are no legal provisions or guidelines regarding the treatment at the level of the shareholders. On the contrary, if the transfer of registered office as such leads to a liquidation and dissolution from a corporate law perspective, a liquidation would also be deemed given from a tax perspective.	

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>10d.2 Tax treatment of third country residents</u> The same principle should apply.	

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 *'Leur-Bloem'* and C321/05 *'Kofoed'*. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 *'Cadbury'*. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> The RTA provides that its benefits shall be denied if the restructuring measures serve the circumvention or the reduction of taxes. The RTA also refers to the general anti-abuse provision in Sec. 22 FTA according to which tax abuse is given if an unusual structure is entered into for tax avoidance purposes only with no business motive.	Sec. 44 RTA Sec. 22 FTA

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' (*'Kofoed'*, paragraph 46)?	Reference
11.2 General anti-abuse provision The RTA refers to the general anti-abuse provision (please see 11.1 – Sec. 22 FTA).	

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' There have been no changes in the national provisions regarding anti-abuse following the '*Cadbury*' judgment.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions No.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' The concept of valid commercial reasons is not included in the wording of the anti-abuse law, but is found in the Supreme Court practice. It is not considered abuse if valid commercial reasons are given justifying restructuring steps and the tax structure.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof From a theoretical point of view the burden of proof is generally on the tax authorities. However in fact the burden of proof is shifted to the taxpayer in case of a tax audit.	

BELGIUM

Abbreviations

English / Belgian	English / Belgian
B.S.	Belgisch Staatsblad
ITC	Income Tax Code 1992
RD	Royal Decree
DRD	Dividend Received Deduction
P&L	Profit & Losses
PE	Permanent Establishment
DTC	Double Tax Convention

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.

Overall state of implementation

The Merger Directive as such in not yet fully implemented. Various laws have brought the Belgian ITC to a certain extent in line with the Merger Directive.

The Law of 28 July 1992 (*B.S.* 31 July 1992)

The Law of 28 July 1992 (*B.S.* 31 July 1992) implemented a tax-free regime

(a) for the contribution of a universality (i.e. all assets and liabilities) of goods or one or more branches of activity in a company (Article 46 and 235, 2° ITC); and

(b) the contribution by a company of another EU Member State of a Belgian branch as a result of a tax-free merger, division or contribution of a universality of goods or one or more branches of activity (Article 231,§2 ITC).

This law became effective for contributions implemented as from 27 March 1992 and was amended by the Law of 21 December 1994, (*B.S.* 23 December 1994), the Law of 30 January 1996, (*B.S.* 30 March 1996), the Law of 16 April 1997, (*B.S.* 23 May 1997), the Law of 22 December 1998 (*B.S.* 15 January 1999), the Law of 14 January 2003, (*B.S.* 5 February 2003), the Law of 27 December 2004, (*B.S.* 31 December 2004) and the Law of 25 April 2007 (*B.S.* 8 May 2007).

According to this regime, capital gains realized or established upon the contribution of a universality of goods or one or more branches of activity are temporarily tax exempt provided that

(a) the contribution is effected for shares representing the statutory capital of the receiving company;

(b) the receiving company's statutory seat, principle establishment or management seat is located within a EU Member State; and

(c) the contribution is justified by sound economic or financial needs.

When the receiving company is located in another EU Member State the contributed assets and liabilities are deemed to be allocated and to remain allocated to a Belgian branch of the receiving company. When the concerned assets and liabilities are no longer used within the Belgian branch, the assets are deemed to be sold (and accordingly become taxable). This regime applies to Belgian companies subject to the corporate income tax (Article 46 ITC) and non-resident companies subject to the Belgian non-resident income tax for companies (Article 235, 2° ITC). The shares received in exchange for the contribution have the same value for tax purposes as the contributed assets and liabilities. In the hands of the receiving company a rollover regime applies.

In addition capital gains established upon the contribution by a company of another EU Member

State of a Belgian branch as a result of a tax-free merger, division or contribution of a universality of goods or of one or more branches of activity are tax exempt provided that the branch or the assets remain in Belgium (Article 231,§2 ITC). In the hands of the receiving company a rollover regime applies.

Guidance issued by the tax administration relevant for the interpretation of the implementation of the Merger Directive is included in the following publication:

(a) the general administrative guidelines on the income tax code (Commentaar op het Wetboek van de Inkomstenbelastingen 1992);

(b) the Circular of 30 April 1996 nr. Ci.D.19/483.966, Bull. nr. 761, p. 1041.

<u>The Law of 6 August 1993</u>

The Law of 6 August 1993 introduced a tax-free regime for domestic mergers and divisions (Article 211 ITC). This law became effective for transactions implemented as from 1 October 1993 and was amended by the Law of 21 December 1994 (*B.S.* 23 December 1994), the Law of 16 April 1997, (*B.S.* 23 May 1997), the Law of 22 December 1998 (*B.S.* 15 January 1999), the Law of 16 July 2001 (*B.S.* 20 July 2001; extending the tax free regime to partial divisions), the Law of 22 April 2003 (*B.S.* 9 May 2003) and the Law of 27 December 2004, (*B.S.* 31 December 2004).

From the preparatory works to the Law of 6 August 1993 it appears that the intention was to apply the tax-free regime for mergers and divisions as provided for in the Merger Directive to domestic mergers and divisions. The government explained that since under Company Law it was at that time not possible to have a cross-border merger or division with a Belgian company being the transferring entity, there was no need to implement a tax-free regime for cross-border mergers and divisions. However, since the new Company Law introduced by Law of 7 May 1999 (*B.S.* 6 August 1999; effective as from 6 February 2001) Belgian commentators take the position that this argument cannot be upheld anymore.

According to Belgian tax law, in principle a merger or (partial) division is treated as a deemed liquidation and accordingly all tax-free reserves and the capital gains realized or established as a result of the transaction are deemed distributed to the shareholders and become taxable (Article 210 ITC). However, Article 211 ITC provides a tax-free rollover regime according to which

(a) revaluation gains,

(b) tax-free reserves representing realized capital gains that benefit from a deferred taxation regime,

(c) tax-free reserves representing capital subsidies and

(d) capital gains realized or established as a result of the transaction, are not taxed provided that

- he receiving company is a Belgian company,
- the transaction is executed in accordance with the provisions of the Company Law and
- the transaction is justified by sound economic or financial needs.

In addition, the other tax-free reserves of the transferring company are not taxed only to the extent that the contribution resulting from the merger or (partial) division is effected for shares. This is not the case when the receiving company holds a participation in the transferring company or when the contribution is partly effected for cash. In the latter case certain tax-free reserves may become taxable. In the hands of the receiving company a rollover regime applies. When the conditions are met, the application of this tax-free rollover regime is obligatory.

Guidance issued by the tax administration relevant for the interpretation of the implementation of the Merger Directive is included in the following publication:

(a) the general administrative guidelines on the income tax code (Commentaar op het Wetboek van de Inkomstenbelastingen 1992);

(b) the Circular of 6 December 1993, nr. Ci.D.19/416.334, Bull. Nr. 734, p. 33;

(c) the Circular of 19 January 1995, nr. Ci.RH.421/461.318, Bull. nr. 747, p. 764 regarding the tax-free regime for domestic mergers and divisions introduced by the law of 6 August 1993.

The law of 30 January 1996 (B.S. 30 March 1996)

The law of 30 January 1996 (*B.S.* 30 March 1996) introduced a tax-free regime for the contribution of a Belgian branch into a Belgian company (Article 231, § 3 ITC). This law became effective for contributions implemented as from 30 March 1996.

Capital gains realized or established upon the contribution of a Belgian branch into a Belgian company are deemed tax exempt. In the hands of the receiving company a rollover regime applies.

Guidance issued by the tax administration relevant for the interpretation of the implementation of the Merger Directive is included in the following publication:

- the Circular of 30 April 1996 nr. Ci.D.19/483.966, Bull. Nr. 761, p. 1041.

Belgium has not implemented

(a) a tax-free regime for mergers or (partial) divisions where the receiving company is a company of a EU Member State,

(b) a tax-free regime for exchange of shares,

(c) a tax-free regime for capital gains realized on assets and liabilities allocated to a permanent establishment located in another EU Member State and whereby the permanent establishment is part of a branch of activity or universality of goods contributed in a company located in another EU Member State. Consequently, Belgian tax law still violates the Merger Directive.

For the sake of completeness, it should also be mentioned that the ITC provides for the application of a professional withholding tax of 33,99% to be withheld by the notary on capital gains realized by non-resident companies on the transfer of real estate located in Belgium. The Minister of Finance has declared that the professional withholding tax is due irrespective the application of one of the above tax-free rollover regimes. Such professional withholding tax is creditable against the non-resident income tax and the balance is reimbursable. Belgian commentators have taken the position that the professional withholding tax is not due when one of the above tax-free rollover regimes apply and in addition that this rule is contrary to the EU freedom of establishment as provided for in the EC Treaty.

Directive 2005/56/EG has not yet been implemented in Belgium. The transfer of the seat of a company (including a SE or SCE) is treated as a deemed liquidation and accordingly all tax-free reserves and the capital gains realized or established as a result of the transfer are deemed distributed to the shareholders and become taxable (Article 210 ITC). The ECJ has formally ascertained that Belgium has not implemented the Directive 2005/56/EG and consequently has

not complied with its duties under this Directive (ECJ dd. May 8, 2008, case C-392/07). Belgian commentators disagree on the question whether the Merger Directive has direct effect. Certain commentators take the position that based on the decision of the ECJ in the '*Sevic*' case dd. 13 December 2005 (C-411/03) the fact that the tax-free regime is limited to domestic mergers is contrary to the freedom of establishment as provided for in the EC Treaty. The Belgian Government has approved a draft bill regarding the implementation of the Merger Directive. This bill has been submitted to Parliament.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
1.1 Involved companies Belgian domestic law as such does not provide for the expression 'in which companies from two or more Member States are involved'. The tax-free restructuring regimes as provided for under Belgian domestic law apply whether or not the merging companies' parent companies meet the requirements of the Directive.	

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
1.2 Foreign Member State and third state merger The tax-free regime for domestic mergers and (partial) divisions applies irrespective the tax residence of the parent companies, i.e. Belgian, (foreign) Member State(s) or third (non-EU) state(s). However, the tax-free regime only applies when the receiving company is a Belgian company. The ITC defines a Belgian company as a company incorporated in Belgium or abroad and that has its statutory seat, principal establishment or seat of management in Belgium and is not excluded from the corporate income tax. Belgian commentators have taken the position that this condition violates the Merger Directive and the freedom of establishment as provided for in the EC Treaty. The tax-free regime for the contribution of a universality of goods or one or more branches of activity in a EU company applies irrespective the tax residence of the transferring company, i.e. Belgian, (foreign) Member State or third (non-EU) state. The tax-free regime for the contribution by a EU company of a Belgian	Article 211 ITC Article 46 and 235, 2° ITC Article 231,§2 ITC Article 231,§3 ITC

branch as a result of a tax-free merger, division or contribution of a universality of goods or branch of activity applies irrespective the tax residence of the receiving company, i.e. Belgian, (foreign) Member State or third (non-EU) state. The tax-free regime for the contribution of a Belgian branch into a Belgian company applies irrespective the tax residence of the contributing company, i.e. Belgian, (foreign) Member State or third (non-EU) state.	

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
<u>2.1 The term 'securities'</u> In general the term 'securities' ('*aandelen*') as such is not defined in the ITC. However, reference can be made to the meaning of the term 'securities' in the Company Law where it means a share in the registered equity in case of a 'Public Limited Liability Company' *('Naamloze Vennootschap' / 'Société Anonyme')* , the Closely held Limited Liability Company *('Besloten Vennootschap met Beperkte Aansprakelijkheid' / 'Société Privée à Responsabilité Limitée')*, the Limited Partnership with Shares *('Commanditaire Vennootschap op Aandelen' / Société Commandite par Actions')* and the Cooperative Company *('Coöperatieve Vennootschap' / 'Société Coopérative')* or the rights representing the membership in this legal entity in case of a Limited Partnership *('Gewone Commanditaire Vennootschap' / 'Société en Commandite Simple')* or the General Partnership *('Vennootschap Onder Firma' / 'Société en Nom Collectif')*.	Article 476, 232, 356, Companies Code Article 671/673/674/675 Companies Code Article 676 Companies Code
The ITC uses different language depending on the tax-free regime concerned.	Article 211 ITC
The tax-free regime for domestic mergers and (partial) divisions applies to transactions implemented in accordance with the Company Law provisions. The Company Law requires that a merger and a (partial) division are remunerated with 'shares in the receiving company'. The operation whereby all assets and liabilities of a company are transferred to another company, where all the shares of the first mentioned company are owned by the latter company and whereby consequently no shares are issued, is treated in the same way as a merger.	Article 46 ITC Article 231,§3 ITC
In addition the ITC provides that the merger and (partial) division are only fully tax exempt to the extent that the merger or (partial) division is effected by 'new shares issued at the occasion of the contribution' which is not the case when and to the extent that the contribution is partly remunerated with a cash payment or when and to the extent that the receiving company holds shares in the transferring company. In the latter case tax-free reserves other than (a) revaluation gains;	Ruling n° nr. 600.398 of 28 November 2006 Article 231,§2 ITC

(b) tax-free reserves representing realized capital gains that benefit from a spread taxation regime; (c) tax-free reserves representing capital subsides, may become taxable. This rule violates Article 5 of the Merger Directive. The tax-free regime for (a) a contribution of a universality of goods or one or more branches of activity into a company of a EU Member State and (b) for the contribution of a Belgian branch into a Belgian company, apply amongst others provided that the contribution is effected by 'shares representing the statutory capital of the company'. Since jouissance rights do not represent a company's statutory capital Belgian commentators take the position that such rights do not qualify as shares in the meaning of Article 46 ITC. The tax-free regime for the contribution of a Belgian branch (as part of a merger, (partial) division, contribution of a universality of goods or one or more branches of activity) into a company of a EU Member State does not explicitly refer to the term 'securities'; it applies to 'contributions'. The Belgian ruling commission reads the scope of Article 231,§2 ITC rather broadly and has issued a ruling in which it has confirmed that the tax-free regime also applies to the transfer of a Belgian branch as a result of the conversion of a German GmbH into a German GmbH & Co. KG.	

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
<u>2.2 The term 'cash payments'</u> The tax-free regime for domestic mergers and (partial) divisions applies to transactions implemented in accordance with the Company Law. According to the definition of the term merger and (partial) division as provided for in Company Law a cash payment not exceeding 10% of the face or par value of the shares issued is allowed. From this definition it follows that the 10% threshold applies on an overall basis. However, to the extent that the merger or (partial) division is remunerated in cash and not with new shares issued at the occasion of the transaction, certain tax-free reserves (other than the (a) revaluation gains, (b) tax-free reserves representing realized capital gains that benefit from a deferred taxation regime and	Article 671-675 Companies Code Article 211 ITC Article 678-680 Companies Code Comm.IB, 46/35

(c) tax-free reserves representing capital subsidies) may become taxable. This rule may violate Article 5 of the Merger Directive to the extent that no rollover regime is provided for the other tax-free reserves in case of a cash payment. Under the Belgian Company Law legal continuity only applies when the contribution of a universality of goods or a branch of activity is effected exclusively with shares of the receiving company. From a tax perspective, however, Belgian administrative guidelines clarify that a 'limited' cash payment does not prevent the application of the tax-free regimes. The notion 'limited cash payment' is not further defined by the Belgian administrative guidelines. In this respect, each transaction has to be assessed on an individual basis.	

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
<u>**2.3 Further types of merger**</u> The term 'merger' is not defined in Belgian tax law. Reference can be made to the definition of the term 'merger' as provided for in the Company Law. Although the scope of the definition as such of the term 'merger' includes mergers between companies located in Belgium, (foreign) Member State or third (non-EU) state, the Company Law further provides that the rules regarding mergers (procedure, legal continuity, etc.) only apply to companies with legal personality as provided for in the Company Law, the Agricultural Company *('Landbouwvennootschap' / 'Société Agricole')* or the Economic Interest Grouping *('Economisch Samenwerkingsverband' / 'Groupement d'Intérêt Economique')* being excluded. Since the application of the tax-free regime requires that the merger is executed in accordance with the Company Law, it will only apply to mergers between the concerned companies, i.e. the Public Limited Liability Company *('Naamloze Vennootschap' / 'Société Anonyme')*, the Closely held Limited Liability Company *('Besloten Vennootschap met Beperkte Aansprakelijkheid' / 'Société Privée à Responsabilité Limitée')*, the Limited Partnership with Shares *('Commanditaire Vennootschap op Aandelen' / 'Société Commandite par Actions')*, the Cooperative Company *('Coöperatieve Vennootschap' / 'Société Coopérative')*, the Limited Partnership *('Gewone Commanditaire Vennootschap' / 'Société en Commandite Simple')* and the General Partnership *('Vennootschap Onder Firma' / 'Société en Nom Collectif')*. In addition to the three types of merger as listed in Article 2(a) the Belgian Company Law assimilates with a merger (or division) a transaction defined as a merger (or division) without the transferring companies ceasing to exist. The scope of this provision is not very clear, but is seems to include a partial division.	Article 671-677 Companies Code Article 670 ITC Article 677 Companies Code

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
<u>**2.4 Qualifying exchange of shares**</u> Belgium has not implemented the tax-free regime for exchange of shares yet. In general, capital gains realized on shares are tax exempt provided that the acquired company meets the subject to tax condition. Such subject to tax condition is as such not provided for in the Directive and consequently, this condition is not compliant with the Directive. There are no minimum holding requirements.	Article 192 ITC

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>**2.5 Consolidation of qualifying holding**</u> In this respect please see 2.4.	

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 *'Andersen og Jensen'*. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>**2.6 The term 'branch of activity'**</u> The ITC provides a tax-free rollover regime for the contribution (i.e. transfer in exchange for shares) of one ore more 'branches of activity' ('*bedrijfsafdeling of tak van werkzaamheid*') into an EU company. The term 'branch of activity' is not defined in the ITC. The ITC clarifies that financial fixed assets and share investments as such do not constitute a branch of activity, but can only be a part of a branch of activity. According to Belgian literature, the latter exclusion is not in compliance with the Directive, as Article 2 of the Directive does not provide a condition with respect to the nature (character) of the activities of a branch of activity. The administrative guidelines on the ITC define the term 'branch of activity' ('*bedrijfsafdeling of tak van werkzaamheid*') as the totality of assets and liabilities of a division of an enterprise that is capable of functioning by its own means. Assets/liabilities not essential for the branch of activity may be held back.	Article 46 ITC Article 680 Company Law Comm.IB 46/36. Comm.IB 46/36.1 and CommIB (old) 105/64 ECJ C-497/01 ZITA MODES, dated 27

The tax authorities take the position that the real estate wherein the activity is carried out needs to be transferred together with the branch of activity except if the real estate is also used by the other branches of activity. This point of view may be contrary to the Directive since the Directive does not explicitly require that the concerned real estate is transferred. Note that the definition of the term 'branch of activity' ('*bedrijfstak*') in Company Law requires that all assets and liabilities are transferred upon the contribution, as a whole, which exercises an independent business from a technical and organizational point of view and is capable of functioning by its own means. The Belgian tax authorities in principle focus on the perspective of the transferring company in order to determine whether the autonomy test is met. According to recent case law regarding the application of the tax-free regime for transfer taxes one should, however, refer to the receiving company. In general, Belgian commentators take the position that the definition of 'branch of activity' according to Article 46 ITC is more or less similar to the definition under the Merger Directive and is even broader since assets/liabilities not essential for the branch of activity may be held back.	November 2003

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> The tax-free regime for domestic mergers and (partial) divisions applies provided that the receiving company is a Belgian company. The ITC defines a Belgian company as a company incorporated in Belgium or abroad and that has its statutory seat, principle establishment or management seat in Belgium and is not excluded from the corporate income tax. In addition, the tax-free regime requires that the merger and (partial) division is implemented in accordance with the Company Law. The Company Law merger and (partial) division provisions apply on all companies with legal personality and are incorporated in a form as provided for in the Company Law, except for (a) the Agricultural Company ('Landbouwvennootschap' / 'Société Agricole') and (b) the Economic Interest Groupings ('Economisch Samenwerkingsverband' / 'Groupement d'Intérêt Economique'). Companies with legal personality as provided for in the Company Law are: (a) the General Partnership ('Vennootschap onder Firma' / 'Société en Nom Collectif'); (b) the Limited Partnership ('Commanditaire Vennootschap' / 'Société Commandite');	Article 211 ITC, Article 2 ITC Article 670 Company Law Article 2 Company Law Article 46 ITC Article 2 ITC Article 231, §2 ITC, Article 2 ITC.

(c) the Closely held Limited Liability Company ('Besloten Vennootschap met Beperkte Aansprakelijkheid' / 'Société Privée à Responsabilité Limitée'); (d) the Cooperative Company ('Coörperatieve Vennootschap' / 'Société Coopérative'); (e) the Public Limited Liability Company ('Naamloze Vennootschap' / 'Société Anonyme'); (f) the Limited Partnership with Shares ('Commanditaire Vennootschap op Aandelen' / 'Société Commandite par Actions'); (g) the Economic Interest Grouping ('Economisch Samenwerkingsverband' / 'Groupement d'Intérêt Economique'); (h) the Agricultural Company ('Landbouwvennootschap' / 'Société Agricole'). Consequently, the Belgian tax-free regime for domestic mergers and (partial) divisions only applies to the following types of companies: (a) the General Partnership ('Vennootschap onder Firma' / 'Société en Nom Collectif'); (b) the Limited Partnership ('Commanditaire Vennootschap' / 'Société Commandite'); (c) the Closely held Limited Liability Company (Besloten Vennootschap met Beperkte Aansprakelijkheid / Société Privée à Responsabilité Limitée); (d) the Cooperative Company (Coörperatieve Vennootschap / Société Coopérative); (e) the Public Limited Liability Company (Naamloze Vennootschap / Société Anonyme; (f) the Limited Partnership with Shares (Commanditaire Vennootschap op Aandelen / Société Commandite par Actions). Therefore excluding companies with a foreign legal form. Belgian commentators have taken the position that this limited scope violates the Merger Directive and the freedom of establishment as provided for in the EC Treaty. The types of companies to which the tax-free regime for domestic mergers and (partial) divisions apply are included in the Annex to the Directive. However, said Annex provides that also other companies incorporated under Belgian law and subject to the Belgian corporate tax are entitled to the Directive's provisions. The latter wording implies that the Agricultural Company (Landbouwvennootschap / Société Agricole) and the Economic Interest Groupings (Economisch Samenwerkingsverband / Groupement d'Intérêt Economique) should also benefit from the provisions under the Directive. Notwithstanding the latter, both types of companies are	Article 231, §3 ITC

excluded from the tax-free regime for domestic mergers and (partial) divisions. This exclusion is not compliant with the Directive. The tax-free regime for the contribution of a universality of goods or one ore more branches of activity into a company of a EU Member State does not refer to the types of entities listed in the Annex of the Merger Directive. The receiving company should qualify as a company of a EU Member State. The term company is defined in Article 2 ITC as 'any company, association, institution or establishment, which is regularly incorporated, has legal personality and exercises a business or engages in activities with a profitable nature'. Consequently, as regards the type of legal entities concerned the scope of application of Article 46 ITC is broader than the Merger Directive. The tax-free regime for the contribution by a company of a EU Member State of a Belgian branch as a result of a tax-free merger, division or contribution of a universality of goods or branch of activity does not refer to the types of entities listed in the Annex of the Merger Directive. The receiving company should qualify as a company of a EU Member State. The term company is defined in Article 2 ITC as 'any company, association, institution or establishment, which is regularly incorporated, has legal personality and exercises a business or engages in activities with a profitable nature'. Consequently, as regards the type of legal entities concerned the scope of application of Article 231, §2 ITC is broader than the Merger Directive. The tax-free regime for the contribution of a Belgian branch into a Belgian company applies irrespective the type of the contributing entity. Consequently, as regards the type of legal entities concerned the scope of application of Article 231, §3 ITC is broader than the Merger Directive.	

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>**3.2 Transparent entities**</u> In general an entity without legal personality under the *lex societatis* is treated as being tax transparent. For the application of the Belgian non-resident income tax an entity is treated as transparent if it has no legal personality and has a legal form that is not comparable to the legal form of a Belgian entity having legal personality according to Belgian Company Law. Guidance regarding the application of this provision is very limited. The Belgian ruling commission has decided, based on the facts and circumstances that a German '*GmbH & Co. KG*' was to be deemed comparable to a Belgian entity having legal personality. But in another case it ruled that a German '*Kommanditgesellschaft*' and a Danish K/S could not be deemed comparable to a Belgian entity having legal personality. The Ruling commission also decided that a UK LLP is a company with legal personality that is subject to non-resident income tax.	Article 227 ITC. Ruling n° 600.398 dd. 28 November 2006; Ruling n° 300.303 dd. 30 June 2005; Ruling n° 500.232 dd 27 October 2005; Ruling n° 500.199 dd. 20 October 2005.

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency A company is deemed to have its tax residence in Belgium provided that it has its registered seat, principle establishment or management seat in Belgium. The criteria 'registered seat, principal establishment or management seat' are considered as alternative criteria by the tax authorities, implying that e.g. as long as the registered seat is situated in Belgium, a company is in principle subject to corporate tax in Belgium. However, according to case law of the Belgian Supreme court, the wording 'principal establishment' and 'centre of management' express the same concept of effective seat of management, which should prevail on the mere formal 'registered seat' as mentioned in the Articles of association. The tax-free regime for the contribution of one or more branches of activity or a universality of goods applies provided that the receiving company is a company having its registered seat, principal establishment or management seat within a EU Member State. Belgian commentators have taken the position that this rule is not in line with Article 3 of the Merger Directive that refers to the tax laws of the concerned Member State to determine the tax residence. The tax residence tiebreaker criterion in the Belgian Model Double Tax Convention and in far most of the tax treaties concluded by Belgium is the 'place of effective management'.	Article 2,§1,5°,a) ITC Article 46 ITC Article 4,§3 Belgian Model Double Tax Convention

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject-to-tax clause The subject-to-tax clause of Article 3(c) as such has not been implemented in Belgium national legislation.	

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
3.5 Shareholder requirements No specific requirements for shareholders.	

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
4.1 The concepts of 'real values' and 'value for tax purposes' According to Belgian domestic tax law a merger and (partial) division in principle qualifies as a deemed liquidation and the capital gains realized or established as a result of that deemed liquidation are in principle taxable. In general the ITC qualifies a realized capital gain as the difference between the consideration received or the sales price (i.e. the 'real value') minus, on the one hand, the costs related to the transfer or the sale, and, on the other hand, the acquisition or investment value minus reductions in value or depreciations that have been accepted for tax purposes (i.e. 'the value for tax purposes'). The administrative guidelines clarify that in order to compute the capital gains established or realized at the occasion of a liquidation the 'real value' to be taken into account equals the fair market value. The tax-free regime for mergers and (partial) divisions provides that capital gains as computed according to the rule set out above are not taxable.	Article 210 ITC Article 43 ITC; Comm.IB 208/11 Article 211, §1, 1° ITC

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions The valuation of assets and liabilities in case of a (partial) division follows the same rule applicable for mergers. No specific guidance has been issued. Belgian Company Law and tax law do not require that the transferred assets and liabilities qualify as a branch of activity neither that the assets and liabilities that are retained by the transferring company upon a partial division qualify as a branch of activity. Certain authors read in an answer of the Minister of Finance to a parliamentary question that the qualification of the transferred assets and liabilities upon a partial division as a branch of activity might be an element to be taken into account when analyzing whether the transaction is justified by sound economic or financial needs, which is required in order to benefit from the tax-free regime. The notion 'sound economic or financial needs' as such is not defined by the Belgian Income Tax Code. The tax authorities generally take the position that the merging companies should be able to demonstrate that the merger is to the benefit of the concerned companies and will have a positive economic and/or financial impact on the concerned companies. This point of view is not compliant with the Directive to the extent that if the merging companies are not able to demonstrate this positive effect, the merger will be deemed taxable also when tax evasion or tax avoidance is not the principal or one of the principal objectives of the merger. This	Parliamentary Q. dd. 18 October 2001

will for instance be the case if the merger is to the economic/financial/personal benefit of the shareholders; the Belgian tax authorities do not take into account business motives in the hands of the shareholders. Also economic reasons that apply to each merger (e.g. simplification of the group structure) are not considered sufficient by the tax authorities to meet this condition. This point of view is not compliant with the Directive. Recently, the Belgian Supreme Court ruled that the notion 'legitimate financial or economic needs' should be read in line with the Directive. It is not clear, however, whether the tax authorities will change their position.	

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' Article 4(1)(b) has not been implemented in Belgian national legislation within the framework of mergers or (partial) divisions. This concept is relevant, however, within the framework of the tax-free rollover regime for the contribution of a universality of goods or one or more branches of activity into a company of a EU Member State. When the receiving company is located in another EU Member State the contributed assets and liabilities are deemed to be allocated and to remain allocated to a Belgian branch of the receiving company. This concept is not implemented as a condition for the application of the tax-free regime but rather as a consequence thereof. When the concerned assets and liabilities are no longer used within the Belgian branch, the assets are deemed to be realized and, accordingly, become taxable in the hands of the receiving company. The tax-free rollover regime makes reference to the concept of 'Belgian branch' the scope of which is broader than the concept of 'permanent establishment' in the OECD Model Treaty and for instance includes an office, a warehouse and a stock of goods. The tax-free rollover regime for the contribution by a company of another EU Member State of a Belgian branch as a result of a tax-free merger, division or contribution of a universality of goods or on ore more branches of activity requires that the branch or the assets remain in Belgium. No further guidelines have been issued regarding this condition.	Article 211 ITC Article 46 ITC Article 229 ITC Article 231,§2 ITC

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief The Belgian tax authorities do not seek to limit the scope of relief.	

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
<u>4.5 Assets and liabilities not effectively connected with a permanent establishment</u> According to Belgian domestic tax law a merger and (partial) division in principle qualifies as a deemed liquidation and the capital gains realized or established at the occasion of that deemed liquidation are taxable. Since no tax-free regime for cross-border outbound mergers or (partial) divisions is provided for in Belgian tax law, capital gains realized on assets and liabilities at the occasion of such a transaction are taxable irrespective whether or not the assets are effectively connected with a Belgian permanent establishment. The ordinary corporate income tax rate applies (33,99%). Since the Directive does not require the application of a tax-free regime for assets and liabilities not effectively connected with a permanent establishment, the taxation of such assets and liabilities is not contrary to the Directive (however see 4.7). On the other hand, the taxation of assets and liabilities that are effectively connected with a permanent establishment is contrary to the Directive. Within the framework of the tax-free rollover regime for the contribution of a universality of goods or one or more branches of activity into a company of a EU Member this concept is not implemented as a condition for the application of the tax-free regime but rather as a result thereof. When the concerned assets and liabilities are no longer used within the Belgian branch, the assets are deemed to be realized and, accordingly, become taxable in the hands of the receiving company. For the calculation of the taxable capital gain, the sales value at that time should be taken into account (Administrative Circular dd. January 15, 1993). (cf. also see above 4.3). The tax-free rollover regime for the contribution by a company of another EU Member State of a Belgian branch as a result of a tax-free merger, division or contribution of a universality of goods or one or more branches of activity requires that the branch or the assets remain in Belgium. When this condition is not met, the capital gains realized or established at the occasion of the transaction become taxable in the non-resident corporate income tax at the ordinary rate of 33,99%.	Article 211 ITC Article 46 ITC Article 231,§2 ITC

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
<u>4.6 Tax treatment of shares of the receiving company</u> In case the receiving company has a holding in the transferring company, the capital gain realized by the receiving company upon cancellation of the shares is in principle a taxable profit. However, to the extent that the capital gain accounted for corresponds to the capital gain for tax purposes, such capital gain is considered as a dividend, which can be	Article 202 ITC

deducted from the taxable profits of the Receiving company for 95% (Dividend Received Deduction - DRD), provided all the other conditions for DRD are met, including : (a) a minimum participation of 10% in the share capital of the transferring company, or if less, a minimum acquisition value of EUR 1.2 million; (b) the shares must have the nature of fixed financial assets; (c) the shares must have been held for an uninterrupted period of at least one year in full property; (d) the 'subject to tax' requirements must be fulfilled. 5% remains taxable at the ordinary income tax rate of 33,99%. As the 5% rule is not included in the Merger Directive Belgian commentators have taken the position that this provision in incompliant with Article 7(1) of the Merger Directive insofar as the receiving company holds a qualifying participation in the transferring company (currently 15%, as from 2009 10%). In addition the Directive does not provide for the above mentioned minimum holding requirements and consequently these requirements are not in line with the Directive. To the extent that the capital gain for accounting purposes exceeds the capital gain for tax purposes, the excess (accounting) of the capital gain is deemed either to originate from non-realized capital gains existing within the transferring company or to be a capital gain realized upon the contribution to the receiving company. Such capital gains are fully exempt, provided they are accounted for on an unavailable reserve account and are not taken into account for computing amongst others any distribution to the shareholders of the receiving company.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>**4.7 Tax deferral**</u> The *'N'* case has no impact on the authorities' point of view. Also with respect to cross-border mergers (which are currently not possible under a tax-free regime) no account has been taken of the Case law of the ECJ. In tax literature, however, authors take the point of view that Belgian domestic law is not compliant with the freedom of establishment. In this respect, one can also make reference to the ECJ '*Sevic*' case.	Article 210 ITC Article 192 ITC

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities Article 4(2) has not been implemented in Belgian national legislation. We make reference to 3.2. Income derived by transparent entities is treated as income of the partnership's members or partners.	

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief Article 4 has not been implemented in Belgian national legislation. There is no tax-free roll-over regime for cross-border mergers, divisions or partial divisions.	

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
5.1 The term 'provisions and reserves' The term 'provision' follows Belgian GAAP which is set out in Article 50 and following of the Royal Decree dd. 30 January 2001. Under the accounting law 'provisions' should cover clearly identified losses or expenses which are at the end of the accounting year probable but of which the amount cannot be established. For tax purposes provisions are only tax exempt if they meet the requirements of Article 48 ITC. According to Belgian tax law, provisions for risks and charges can be tax exempt provided that the charges they cover are clearly described and to the extent the probability that the charges will occur appears from specific circumstances arising during the taxable period and still exist at the end of the taxable period. The term 'reserve' follows Belgian Company Law and GAAP. Reserves can only be created with taxable effect if specifically mentioned in the ITC. Following reserves are in principle created with a taxable effect: the legal reserves (i.e. minimum reserve as provided for in the Company Code), the reserves not available for distribution, and the reserves available for distribution. Tax-free reserves are amongst others: (a) revaluation gains (representing registered but non-realized capital gains on certain assets);	Article 50 Royal Decree 30 January 2001

(b) tax-free reserves representing realized capital gains that benefit from a deferred taxation regime; (c) tax-free reserves representing capital subsidies.	

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments Article 5 is not implemented in Belgian tax law. The exclusion of provisions and reserves derived from permanent establishments abroad' has not been implemented.	

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves Under the tax-free regime for domestic (partial) divisions, the rules are as follows. Taxable reserves are allocated to the receiving companies in proportion to the net fiscal value of the assets and liabilities contributed to the receiving company. Tax-free reserves (other than revaluation gains) are allocated to the receiving companies in proportion to the net fiscal value of the assets and liabilities contributed to the receiving company but tax-free reserves representing realized capital gains that benefit from a deferred taxation regime are to be allocated by priority to the company to which the reinvestment assets are contributed or that takes over the reinvestment commitment and tax-free reserves representing capital subsidies are to be allocated by priority to the company to which the subsidized assets are contributed. Revaluation gains are to be allocated to the company to which the concerned assets are contributed. The allocation of provisions is free, i.e. one can determine freely to what company the existing provisions are transferred. The administrative guidelines on the ITC provide, however, that if a provision is allocated to a receiving company whereas the actual expense which is covered by the provision is ultimately borne by the other receiving company, the expenses will not be deemed tax deductible in the hands of the latter receiving company. As regards the transfer of assets, in principle reserves remain with the transferring company. However, under the tax-free regime for the contribution of a universality of goods or a branch of activity into a company of a EU Member State tax-exempt reserves representing realized capital gains that benefit from a deferred taxation regime are allocated to the receiving company to the extent that the reinvestment assets or the	Article 213 ITC Comm.IB 211/48-63 Comm.IB, 211/62,c) Article 192,§2/ 190 ITC and 362, al.2 ITC Article 46,§2,al.2 ITC

reinvestment commitment is transferred to the receiving company and an unavailable reserve is accounted for in the amount of the exempt reserve. Also tax-exempt capital subsidies are transferred to the receiving company to the extent that the subsidized assets are contributed to the latter. The allocation of provisions is free, but when the provision is transferred to the receiving company such transfer is tax-neutral.	

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves To the extent that the merger or (partial) division is not entirely remunerated with shares (i.e. to the extent that the receiving company holds a participation in the transferring company or to the extent that the transaction is remunerated with a cash payment not exceeding 10%) the transferring company's equity is deemed to be reduced for the same amount. When the receiving company holds a participation in the transferring company the withdrawal is deemed to take place proportionally on the effectively paid in share capital and the reserves (first the taxed reserves and subsequently the tax-free reserves). In the event of a cash payment for tax purposes a withdrawal is deemed to take place first out of the taxed reserves, then out of the exempt reserves and finally out of the effectively paid in share capital. To the extent that the withdrawal takes place on tax-free reserves other than revaluation gains, tax-free reserves representing realized capital gains that benefit from a spread taxation regime, tax-free reserves representing capital subsides, the reserves become taxable at the ordinary corporate income tax rate of 33,99%. Belgian commentators take the position that this rule violates Article 5 of the Merger Directive.	Article 211 ITC

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry-over of losses Article 6 is not implemented in Belgian tax law. In general, tax losses carried forward remain within the legal entity that has incurred the losses. However, the tax regime for domestic mergers and (partial) divisions provides that losses carried forward of the transferring company are transferred to the receiving company in proportion to the fiscal net value of the contributed assets and liabilities to the fiscal net value of the assets and liabilities of the receiving company increased with the fiscal net value of the assets and liabilities of the contributing company. On the other hand, the losses carried forward of the receiving company are partly lost, i.e. in proportion to the fiscal net	Article 206 ITC Article 231,§2 ITC Parliamentary Q.

value of the assets and liabilities of the receiving company to the fiscal net value of the assets and liabilities of the receiving company increased with the fiscal net value of the assets and liabilities of the contributing company. Belgian commentators have taken the position that the fact that the above regime (i.e. transfer of losses) does not apply to the contribution by a company of another EU Member State of a Belgian branch as a result of a tax-free merger or division is contrary to the Merger Directive and the freedom of establishment as provided for in the EC Treaty. The Minister of Finance has confirmed that based on the non-discrimination principle embedded in the double tax treaty Belgium/Netherlands the above regime should apply to the division of a Dutch company having a permanent establishment in Belgium.	dd. 12 June 1998

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment We make reference to 6.1.	

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets As regards domestic (partial) divisions the same rules as for mergers apply (please see 6.1). The ITC also provides that before the application of the above mentioned rules the tax losses carried forward of the transferring company should first be allocated to the receiving companies in proportion to the net fiscal value of the assets and liabilities contributed to the concerned company. In addition, the tax free regime for the contribution of a universality of goods or one or more branches of activity into a company of a EU Member State provides that when a Belgian company receives such universality of goods or one or more branches of activity, its tax losses carried forward are partly lost, i.e. in proportion to the fiscal net value of the assets and liabilities of the receiving company to the fiscal net value of the assets and liabilities of the receiving company increased with the fiscal net value of the assets and liabilities of the contributing company. Since the same regime applies to internal restructurings, this rule is compliant with the Directive.	Article 206 ITC Article; 206 ITC

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
<u>6.4 Further conditions for carry over of losses</u> In this respect we make reference to 6.1.	

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
<u>7.1 Amended holding threshold</u> Belgian domestic law does as such not provide for the above threshold, but instead provides for a different regime, implying various other conditions and thresholds. In case the receiving company has a holding in the transferring company, the capital gain realized by the receiving company upon cancellation of the shares is in principle a taxable profit. However, to the extent that the capital gain accounted for corresponds to the capital gain for tax purposes, such capital gain is considered as a dividend, which can be deducted from the taxable profits of the Receiving company for 95% (Dividend Received Deduction - DRD), provided all the other conditions for DRD are met, including : (a) a minimum participation of 10% in the share capital of the transferring company, or if less, a minimum acquisition value of EUR 1.2 million; (b) the shares must have the nature of fixed financial assets; (c) the shares must have been held in full ownership for an uninterrupted period of at least one year; (d) the 'subject to tax' requirements must be fulfilled. 5% remains taxable at the ordinary income tax rate of 33,99%. As the 5% rule is not included in the Merger Directive this provision in incompliant with Article 7(1) of the Merger Directive insofar as the receiving company holds a qualifying participation in the transferring company (currently 15 per cent, as from 2009 10%). In addition, the above mentioned minimum holding requirements are not provided for in the Directive and, consequently, these conditions are not compliant with the Directive. To the extent that the capital gain for accounting purposes exceeds the capital gain for tax purposes, the excess (accounting) of the capital gain is deemed either to originate from non-realized capital gains existing within the transferring company or to be a capital gain realized upon the contribution to the receiving company. Such capital gains are fully exempt,	. Article 202 §1, 2° and §2 ITC Article 203 ITC Article 190 ITC

provided they are accounted for on an unavailable reserve account and are not taken into account for computing amongst others any distribution to the shareholders of the receiving company.	

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses In case of a capital loss, the difference between the book value of the shares and the book value of the assets received is allocated to the assets the market value of which exceeds the book value. In case the loss is not attributable to specific assets, the difference is considered as goodwill. If the loss is neither attributable to specific assets, nor to be considered as goodwill, the difference is taken as a loss in the P & L account. The attribution to specific assets or to goodwill are not recognized for tax purposes, i.e. there is no step up in basis and a corresponding deemed unrealized capital gain has to be accounted for on an unavailable reserve account, i.e. not available for distribution and not to be taken into account for computing amongst others any distribution to the shareholders of the receiving company. This entry may be organized via a debit of the P & L account or via entries within the capital account. In both cases, a disallowed expense has to be declared in the tax return for an amount corresponding to the capital loss on shares, which is indeed not tax deductible. To the extent that the loss is accounted for as a debit on the P & L account, such charge is not tax deductible.	Article 78, §6 RD implementing Companies Code/ art 211/212 ITC Article 212 and 190 ITC Article198, 7° ITC

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder 8.1.1 In case of an exchange of shares (contribution of shares) 8.1.1.1 In the hands of the acquiring company: The acquired shares are accounted for at the value agreed by the parties, i.e. normally the market value (no economic double taxation). 8.1.1.2 In the hands of the shareholder of the acquired company: The shares received in exchange are accounted for/valued at market	Article 192 ITC Article 203 ITC/192

value. In the hands of a Belgian corporate shareholder the realized capital gain is tax exempt provided that the subject-to-tax condition is met. Basically the 'subject to tax ' condition implies that either the company the shares of which are disposed of is subject to corporate tax at a sufficient rate (15% normally) and neither benefits from 'tainted income' (e.g. untaxed offshore income), nor redistributes such income. These latter conditions are not provided for in the merger directive. Consequently, no economic double taxation occurs. The same is valid if the shares are connected to a Belgian branch of a foreign company (EU Member State or third state). <u>8.1.2 In case of a merger, division, partial division</u> <u>8.1.2.1 In the hands of the acquiring company</u> The acquired assets keep the book value they had within the transferring company. <u>8.1.2.2 In the hands of the shareholder of the transferring company</u> A Belgian resident corporate shareholder accounts for: the shares received at the same value as the initial shares held in the transferring company; subsequently realized capital gains are exempt provided that the subject-to- tax condition is met (no economic double taxation). The same is valid if the shares are connected to a Belgian branch of a foreign company.	ITC Article 78 §2 RD implementing the Companies Code Article 41 §1 RD implementing the Companies Code, Article 192 ITC

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>8.2 Computation of the capital gain</u> According to the Belgian Companies Code, the cash payment made upon a merger, division or partial division may not exceed 10% of the face or par value of the shares issued. Should the threshold of 10% be exceeded, the merger, division or partial division would not be carried out in compliance with the Companies Code and hence may not be effectuated under tax-neutrality. The payment in cash is deemed to be withdrawn from the equity of the transferring company and it is therefore considered for tax purposes as a dividend distribution to the extent that it is deemed to be withdrawn from the retained earnings and reserves of the transferring company. The General meeting of shareholders, which decides on the merger, also decides on the elements from which the cash payments will be withdrawn. Cash payments may only be withdrawn from distributable reserves. For tax purposes however the withdrawal is deemed to take place first out of the taxed reserves, then out of the exempt reserves and finally out of the effectively paid in share capital. Certain exempted reserves may not be	Article 671, 672,673, 674, 677 Companies Code Article 211 §1,2° (2°) ITC Article 78 §5 RD implementing Companies Code Article 211 §2 ITC Article 269, 2°bis ITC Article 106 §§5 and

affected though (e.g. revaluation reserves). To the extent the cash payment is deemed to be withdrawn from exempt reserves, corporate tax is due at the normal rate (33.99%). In addition, a withholding tax of 10% is due on the amount that is considered as a dividend. For corporate shareholders, an exemption of withholding tax may be available under Belgian domestic law (available for Belgian, EU Member States and treaty countries corporate shareholders) or the parent-subsidiary directive, as implemented in Belgian tax law. In the hands of a corporate shareholder, the cash payment is considered as a dividend to the extent that it is treated as a dividend in the hands of the transferring company. The 95% DRD may be applied if the conditions are met. To the extent that the payment in cash proportionally corresponds to share capital of the transferring company, arguably the received amount is fully exempt without further conditions (although an answer of the Minister of Finance to a question asked in Parliament would imply that this latter amount should also be comprised in the DRD, i.e. 5% would be taxable). In the hands of the acquiring company the amount of the paid in share capital and the reserves taken over from the transferring company are reduced to the extent as explained above in the 1st paragraph. There is no particular treatment with respect to a cash payment upon an exchange of shares. The cash payment is part of the capital gain realized on shares, which will normally be exempt in the hands of a Belgian corporate shareholder, always provided the 'subject to tax' condition is met in the hands of the company the shares of which are transferred. In the hands of the acquiring company the cash payment is part of the acquisition value of the shares received. To the extent that Belgian tax law takes into account the cash payment when taxing the transferring company, domestic law is non-compliant with directive, since under the directive this is only allowed when taxing shareholders.	6 RD ITC Article 202 §1, 2° ITC Article 192 ITC

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>8.3 Further conditions for tax relief</u> To the extent that the Belgian resident corporate shareholder is deemed to have received a dividend (see above), the DRD may be applicable, i.e. 95% of such dividend is deductible from the taxable profit. To that effect however several conditions must be fulfilled: (a) At the time of the deemed distribution, a minimum shareholding of 10% in the share capital or, if less, with an acquisition value of at least EUR 1.2 million; (b) The shares must have the nature of fixed financial assets;	Article 202/203/209 ITC

(c) The shares must have been held for an uninterrupted minimum duration of one year ; (d) The shares must have been held in full property during that period; (e) The transferring company must comply with the 'subject to tax' requirements. As in principle a merger, division or partial division is considered as a liquidation under Belgian tax law, a 10% dividend withholding tax would in principle be applicable on the deemed distribution exceeding the effectively paid in share capital. However, an exemption of withholding tax is provided for in case of a tax-neutral merger, division or partial division. This implies that the conditions thereto must be fulfilled, i.e. (a) the acquiring company must be resident for tax purposes in Belgium; (b) the merger, etc must be implemented in accordance with Belgian company law; (c) the operation must be justified by sound economic or financial needs Alternatively an exemption of withholding tax (available for Belgian, EU Member States and treaty countries corporate shareholders) may be applicable under the parent-subsidiary directive as implemented (and extended) in Belgian tax law, obviously also provided the conditions thereto are fulfilled, i.e. amongst other things, a minimum participation of 15% (10% as from 1 January 2009) and a holding period of at least one year. As a conclusion it may be stated that Belgian domestic law is non-compliant with the merger directive where corporate tax is imposed on deemed distributed reserves of the merged company under the DRD system and where the exemption of withholding tax is subject to conditions set in domestic law for tax-neutral treatment of the merger, which conditions are in itself not fully compliant with the directive. With respect to the notion sound economic or financial needs we make reference to 4.2.	Article 269, 2°bis ITC Article 264,2° ITC Article 106 §5,§6 and 6bis/ Article 117 §4 and 5 RD implementing ITC

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>**9.1 Avoidance of economic double taxation at the level of the transferring company**</u> According to Belgian Company law the contribution of all or one or more branches of activity is accounted for under a continuity scheme, i.e. the assets and liabilities are taken over by the acquiring company at the book value they had within the transferring company and the latter will account for the shares at net assets value the branch or business had within the transferring company prior to the operation. Accordingly, no capital gains will be expressed in the accounts, neither with the transferring company, nor with the acquiring company. In view of determining the subsequent capital gains and losses on the shares received as remuneration for the contribution, the fiscal value, which had the contributed assets, is taken into account. Subsequent capital gains realized by the transferring company on the shares are in principle tax exempt provided that the subject-to-tax condition is met. Accordingly, in principle, no economic double taxation should occur. The conditions for tax-neutral treatment are that the receiving company is established within the EU and that the operation is justified by sound economic or financial needs. In principle, Belgian domestic law is therefore compliant with the merger directive. Please note however that the Belgian tax authorities are very reluctant in accepting that a contribution of assets has been done for sound economic or financial purposes when the shares received in exchange are sold shortly afterwards. In case the tax authorities take this position, capital gains realized upon such a contribution could become taxable although the assets would remain accounted for at their book value which they had in the hands of the transferring company, thus resulting in an economic double taxation. With respect to the notion sound economic or financial needs we make reference to 4.2.	Article 41 and 80 RD implementing the Companies Code Article 46§3 ITC Article 192 ITC Article 46§1 ITC

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>**9.2 Further conditions for tax relief**</u> The contribution must be justified by sound economic or financial needs (see also comments on 9.1 and 11.1).	Article 46§1 ITC

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>**9.3 Tax deferral**</u> Belgian tax law does not include a specific provision according to which a capital gain on qualifying shares would become taxable upon a corporate tax payer transferring its residence outside Belgium. However, in general the transfer of a Belgian company's tax residence abroad is treated as a deemed winding up and, accordingly, all assets and liabilities are deemed to be realized (including capital gains on shares). Capital gains deemed realized on shares will in principle be tax exempt according to the general participation exemption for capital gains on shares provided that the subject to tax condition is met (there is however no minimum holding requirement). There is no system imposing the provision of a guarantee; if the subject to tax condition is not met taxation is due immediately. Besides, Belgian tax authorities have agreed to no longer apply tax on capital gains realized by individuals upon the alienation of shares belonging to a substantial interest (>25%) in a Belgian company to a foreign company if the acquiring company is established within the E.U. (Order of the Court in Case C-268/03 '*J-C DE BAECK*').	Article 210 ITC, Article 192 ITC Article 90,9° ITC

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>**10.1 Loss recapture for permanent establishments in third Member States**</u> In principle, a Belgian head office can offset losses made by its foreign permanent establishment from its Belgian profit. There is no such recapture rule in Belgian domestic tax law. However, under most DTC a recapture of losses may take place to the extent that the foreign losses that have previously been offset with Belgian profits are now compensated in the country of the permanent establishment with the PE losses. Upon a tax-neutral operation such	

compensation should not take place though, since no gains are realized, and, consequently, this rule can be deemed to be compliant with the Directive.	

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>**10.2 Permanent establishment in the Member State of the receiving company**</u> The situation where a Belgian resident transferring company contributes a branch of activity or its universality of goods including a foreign (permanent) establishment, to a foreign (EU) company is as such not specifically regulated in Belgian domestic tax law. In principle capital gains realized or recognized on foreign assets are taxable as part of the world wide income of the transferring company. The domestic law exemption would not be applicable since this requires that the contributed assets remain allocated to a Belgian establishment, which condition could obviously not be met. However, in principle, under the relevant DTC any capital gain realized or recognized on a foreign permanent establishment should be exempt in Belgium. In some tax treaties concluded by Belgium (e.g. with The Netherlands) a 'subject to tax' condition is provided for. In such case the question has risen whether, on the basis of the DTC, this would preclude exemption in the State of the transferring company in case the State of the establishment grants an exemption. A defensible position would be to argue that if the relevant capital gain has been subject to its normal tax regime, albeit an exemption, the subject to tax requirement would be met. This position is supported by case law provided by the Belgian Supreme Court, by scholars and administrative commentaries. In case a foreign company contributes a branch of activities, including a (permanent) establishment situated in Belgium, to a company resident in Belgium in exchange for shares issued by the latter, the following applies: (a) All capital gains realized or established upon such contribution are exempt. (b) The operation is tax neutral, i.e.: • depreciation, deductions for investment, capital gains and losses will be computed in the hands of the acquiring Belgian resident company as if the transaction did not occur; • tax exempt capital gains and provisions that are present within the Belgian branch remain untaxed provided these items are resumed in the accounts of the acquiring company. The same applies to roll over reserves (such as capital gains and grants subject to deferred taxation). (c) Tax losses incurred in the branch are however not transferred to the acquiring Belgian company.	Article 46 ITC Cass. 15 September 1970, Bull. 489, p. 1679 Article 231 §3 ITC Article 231 §2 ITC

(d) The amount of the effectively paid in share capital of the Belgian company is increased with an amount equal to the net equity value of the branch for tax purposes, after deduction of the taxed reserves and the tax exempt reserves other than revaluation reserves , reductions in value and exempt provisions (the latter items are as such transferred to the Belgian company). (e) Please note that it is not required that the transferring company is established within the EU. (f) The law does not require that the operation is justified by sound economic or financial needs (unlike pure internal contributions or mergers). (g) The establishment does not necessarily need to be a qualifying branch of activity. Please note that if a Belgian branch belongs to the assets, which are transferred at the occasion of a merger, division or contribution of one or more or all branches of activity by a company established within the EU and such transfer has been operated under a tax neutrality scheme, all capital gains that are established at the occasion of such an operation are exempt in Belgium provided that a branch is maintained in Belgium. In this event there is no step up in basis within the branch i.e. the receiving company computes any new depreciation and any gains or losses in respect of the assets and liabilities transferred according to the rules that would have applied to the transferring company if the transaction had not taken place. However, losses carried forward of the branch are in principle not transferred (please see 6.1). As a conclusion it may be stated that the Belgian domestic law is not fully compliant with the merger directive, where Belgium as the State of the transferring company does not provide for an exemption in case a foreign branch is contributed to a EU company, irrespective though the fact that in most cases an exemption by virtue of a DTC will prevail.	

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> There is no such legislation in Belgium.	

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
<u>10.4 Tax deferral</u> N/A.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
<u>10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies</u> There is no legislation in Belgium implementing art 10a of the Directive. Consequently, the tax treatment, in the hands of the partners, of an operation whereby a foreign transparent entity, lacking legal personality, is either the acquired or the transferring company, will be established in function of the features presented by the partners (shareholders) and/or the kind of assets present in the transparent entity. Accordingly, (a) In case of an exchange of shares (contribution of shares): The capital gain realized on the units by a Belgian resident company would be taxable (i.e. not a capital gain on 'shares'), unless such units are attributable to a foreign permanent establishment situated in a country with which Belgium has concluded a DTC. (b) In case of a contribution of assets: The portion of the capital gain attributable to the partner, being a Belgian resident company, would be taxable, unless attributable to a PE situated in country with which Belgium has concluded a DTC. Note that in principle the company may be deemed to have a permanent establishment as a result of its participation in the transparent entity. However, to the extent the realized capital gain would relate to qualifying shares, such capital gain should be exempt. Capital gains realized on shares are fully exempt from Belgian corporate income tax on the sole condition that potential dividends as regards those shares would meet the subject-to-tax condition as laid down in the participation exemption for dividends, regardless of the holding quantity or period. In case the foreign company has legal personality, but is fiscally transparent, the analysis would be the same in case of a share exchange, i.e. as far as Belgian corporate shareholders is concerned, the capital gain on such shares will not be exempt in Belgium since the transparent taxed	Article 24 ITC Article 24:, 183 and 192 ITC Article 24/ 183 ITC Article 192 ITC Article 192 ITC

entity is as such not subject to tax. In case of a contribution of assets, the Belgian resident corporate shareholder should not be taxable in Belgium on capital gains realized upon such contribution operated by the foreign transparent (legal) entity.	

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit N/A.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit N/A.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders Article 10a has not been implemented. The Belgian taxation scheme would be as follows. In case a Belgian resident company would contribute one or more or all branches of activity either to a Belgian resident or foreign resident transparent entity, without legal personality, no tax-neutral treatment would apply, since a tax-neutral contribution of one or more or all branches of activity may only be operated to a company with legal personality and to the extent that the contribution would be deemed to be made to the various (EU resident) corporate partners of the transparent entity, the contribution would not qualify either since Belgian domestic tax law requires that the contribution is made to one single company. Such a contribution to a company with legal personality, albeit fiscally transparent, should qualify for tax-neutral treatment (provided the other conditions – business purpose – are fulfilled). In case of an exchange of shares, irrespective whether the non resident acquiring company has legal personality or not the capital gain would be exempted provided that realized on qualifying shares. Regarding the notion qualifying shares, we make reference to section 10a.1.	Article 46 ITC Article 192 ITC

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
<u>10a.5 Comparison with a resident fiscally transparent company</u> See answer to question 10a.4.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
<u>10b.1 Exit taxation</u> The transfer of the registered seat or the principal establishment or the seat of effective management outside Belgium is treated as a liquidation for tax purposes. This principle is valid for all companies, irrespective whether an SE/SCE or not. Hence, all latent capital gains present upon the transfer will be taxed at the normal corporate tax rate (33.99%), also in case a permanent establishment would be maintained in Belgium. Furthermore, the equity will be deemed distributed and, in principle, dividend withholding tax is due at the rate of 10% on the amount of net equity exceeding the effectively paid in share capital. Obviously, the Belgian domestic tax law is not compliant with the merger directive to the extent no exemption is available for the transfer of the 'registered office' of a SE or SCE.	Article 208/209 and 210 §1, 4° ITC

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
<u>10b.2 The term 'head office'</u> Regulation 2157/2001 has been implemented in Belgian Company law. Article 10b of the Directive has not been implemented yet. Article 876 Companies Code solely provides that if it is established that merely the 'head office' ('hoofdbestuur') is established in Belgium, the Public Prosecutor will immediately inform the Member State where the registered seat of the SE is established. The term 'head office' is not defined in the Companies Code, but in its general meaning it is 'the effective seat of management '. According to the 'International Private Law Code' (law of 1 October 2004 – art 110) a legal entity is governed by	Article 874 to 948 Companies Code Article 2 §1,5° (b)

the law of the state where its 'principal establishment' is situated and Article 4 §3 of the same Code stipulates that the 'principal establishment' of a legal entity is determined, particularly, taking into account the 'centre of management', as well as the centre of its business or activity and in secondary order, its statutory (registered) seat. This implies that in Belgium law the term 'head office' has a factual meaning, i.e. the place as from where the company is led in fact. Please note that as long as the registered seat of a company is situated in Belgium the tax authorities apply a presumption that the company is resident in Belgium and thus remains formally subject to Corporate tax (and not to corporate tax for non-residents), unless the tax payer demonstrates that the effective seat of management is located abroad.	and 179 ITC

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
<u>10b.3 Head office and tax residency</u> As defined above (10b.2) the term 'head office' coincides with 'principal establishment', 'centre of management' or 'effective seat of management,' which is the criterion for determining tax residence under the tiebreaker rule as provided for in most of the DTCs concluded by Belgium. The criteria 'registered seat, principal establishment or seat of management' are considered as alternative criteria by the tax authorities implying that e.g. as long as the registered seat is situated in Belgium, a company is in principle subject to corporate tax in Belgium. According to case law of the Belgian Supreme court, the wording 'principal establishment' and 'centre of management' express the same concept of effective seat of management, which should prevail on the mere formal 'registered seat' as mentioned in the Articles of association. In any event, Belgium may not be allowed to effectively tax if by virtue of the tiebreaker rule provided for in the relevant DTC the other State is allowed to tax on the ground that the effective seat of management of the company is situated in that latter state.	Article2 §1,5° ITC

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>10b.4 Assets and liabilities not effectively connected with a permanent establishment</u> Under current Belgian tax law capital gains established on such assets are taxed, like capital gains established on any other assets, except for capital gains realized on qualifying shares.	

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
<u>10b.5 Tax deferral</u> Since Belgian tax law still provides for an 'exit tax' in all events, also in an EU context, no account has been taken with the ECJ case law on freedom of establishment.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
<u>10c.1 The term 'comparable circumstances'</u> After a company (SE, SCE or other) would have transferred its seat abroad, under Belgian tax laws, losses incurred prior to such transfer are not available anymore for offsetting profits realized within the permanent establishment after the transfer of the seat. Losses carried forward may however be offset against capital gains recognized upon the transfer of the seat.	

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
<u>10c.2 Loss recapture for permanent establishments</u> There is no recapture provision in Belgian domestic law for losses incurred in a third state PE. To the extent that the net capital gain established upon the transfer of the seat would be attributable to the PE in the third country, such capital gain may not be taxed in Belgium under the DTC concluded with that third state. Recapture of losses under that DTC would take place where the capital gain would be compensated in the country of the PE with losses, such losses which were previously deducted in Belgium.	

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
10d.1 Deemed liquidation See answer to question 10b1. There may be an exemption of dividend withholding tax under domestic law or the EU parent-subsidiary directive as implemented in Belgian tax law and provided the conditions thereto are fulfilled (minimum participation and minimum holding period).	

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
10d.2 Tax treatment of third country residents Belgium has extended the dividend withholding tax exemption as provided for under the parent-subsidiary directive to all parent companies established in a country (whether EU or not) with which Belgium has concluded a DTC provided that this DTC or any other treaty with that state includes a clause of exchange of information, necessary for the application of the domestic laws of the contracting states. Such a clause is provided for in far most of the DTC Belgium has concluded The dividend withholding tax exemption applies: provided the (deemed) distributing and receiving company are respectively a parent company and a subsidiary, i.e. (a) have a legal form as listed in the annex to the parent-subsidiary directive or a similar form provided for by the laws of the country with which Belgium has concluded a DTC; (b) both companies are resident for tax purposes in their respective states both by virtue of domestic law and by virtue of the DTCs concluded with third states; (c) both companies must be subject to corporate or a similar tax without being subject to a tax scheme that deviates from the commonly applicable tax system; (d) provided that the parent company holds a minimum participation in the subsidiary for an uninterrupted period of at least one year, the minimum participation being 15% (10% for distributions as from 1 January 2009).	

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 *'Leur-Bloem'* and C321/05 *'Kofoed'*. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 *'Cadbury'*. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> The tax-free regimes for mergers, divisions, partial divisions or contributions of one or more or all branches of activity requires the transaction to meet sound financial or economic needs. According to the tax authorities this requirement is in line with Article 11(1)a of the Directive. The notion 'sound economic or financial needs' as such is not defined by the Belgian Income Tax Code. The tax authorities generally take the position that the merging companies should be able to demonstrate that the merger is to the benefit of the concerned companies and will have a positive economic and/or financial impact on the concerned companies. The following arguments have been accepted as valid: (a) the realization of economies of scale; (b) the consolidation of financial structures; (c) the contribution of operational real estate; and (d) to obtain bank guarantees. In our opinion, however, the tax authorities' point of view is not compliant with the Directive to the extent that if the merging companies are not able to demonstrate this positive effect, the merger will be deemed taxable also when tax evasion or tax avoidance is not the principal or one of the principal objectives of the merger. This will for instance be the case if the merger is to the economic/financial/personal benefit of the shareholders; the Belgian tax authorities do not take into account business motives existing in the hands of the shareholders. Also economic reasons that apply to each merger (e.g. simplification of the group structure) are not considered sufficient by the tax authorities to meet this condition. This point of view is not compliant with the Directive. Recently, the Belgian Supreme Court (Cour de Cassation/Hof van Cassatie: decision dated 13 December 2007) has held that, where art 211, §1 ITC (tax-neutral mergers, divisions, etc) has been introduced in view of implementing the EU merger directive, as a general rule, any merger, division, partial division and exchange of shares must benefit from tax neutrality, irrespective of the reason (financial, economic or solely for tax purposes) why the operation has been carried out. Consequently, the Supreme Court holds that any merger, division, etc is in principle deemed to have been carried out for sound business reasons. The Court explicitly	Article 46, 211 ITC Article 231 §3 ITC Article 192 ITC

referred to the decision of the ECJ in '*Leur-Bloem*'. Where the Directive authorizes the Member States to deny the benefit of tax neutrality in the event that it appears that the operation has as its principal objective or as one of its principal objectives tax evasion or tax avoidance, the tax authorities must prove that there is a lack of business justification, although the tax payer has the duty to cooperate (i.e. by providing evidence showing the business purposes). It is not clear whether as a result the Belgian tax authorities will change their interpretation of the notion financial or economic needs. Please note that the contribution by a foreign company (whether EU or not) of its Belgian PE into a Belgian company has (so far) not been made subject to the fulfillment of this condition (see above, answer to 10.2). The exemption of capital gains realized on shares, i.e. upon an exchange of shares, is not subject to this condition either.	

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
<u>**11.2 General anti-abuse provision**</u> From the answer to the previous question may appear that Article 11(1)(a) of the Directive has not been implemented as such in Belgian tax law. The 'business purpose' has indeed been inserted as an independent condition in order for a merger, division, etc to be eligible for tax-neutral treatment, where in the Directive the lack of business purposes is formulated merely as an indication justifying a presumption (subject to counter – evidence) that the operation aims at tax evasion or avoidance, which may allow a Member State to deny tax neutrality. The Belgian tax authorities state, however, that the above condition i.e. the business purpose condition, is the transposition of Article 11(1)(a) of the directive into Belgian law and the Supreme Court (see the precedent question) has given an interpretation to this condition so that, technically, it works in the same way as provided for in the Directive (i.e. tax-neutrality is the rule and denial is the exception, provided the tax authorities prove the intention of tax evasion or avoidance) Within this framework the tax authorities should thus not rely on other provisions or principles regarding abuse of rights, tax evasion or avoidance. Besides, in Belgium it is generally accepted that the application of a general principle of 'abuse of law' or 'abuse of right' in tax matters would be contrary to the Belgian Constitution ('No tax except by law' principle) There is a general 'anti-abuse' provision though, stipulating that the tax authorities are not bound by any legal qualification given by parties to an act or series of acts implementing one single operation, if it can be evidenced that such qualification aims at avoiding tax, except if the tax payer is able to demonstrate that the qualification given is justified by sound financial or economic needs.	

The above provision refers to a 'legal qualification' (i.e. the qualification according to civil law' and not to an 'act' as such, meaning that the tax authorities may give another legal qualification to an 'act' (a transaction) perpetrated by parties, provided they respect the legal (and other) consequences of such act. It may hardly be conceived that this provision could be applied for denying the advantage of tax neutrality, since this would imply that tax authorities would state that the transaction as such (and not merely its legal qualification) would aim at tax avoidance. Finally, tax authorities could in principle invoke 'simulation' in order to challenge an operation. However, this could hardly be applied here since 'simulation' implies that the parties in reality would have effectuated another transaction than the apparent operation, which would obviously not be the case here.	

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
<u>**11.3 The concept of 'wholly artificial arrangement'**</u> The case law given by the Belgian Supreme Court in its decision of 13 December 2007 indicates that art 211 §1 ITC must be interpreted in conformity with the Merger directive, but so far neither the Courts nor the tax authorities have explicitly stated that even though a transaction may be tax driven, it must be accepted as long as it is not a 'wholly artificial arrangement'.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
<u>**11.4 Specific anti-abuse provisions**</u> The Belgian tax authorities, through the policy of the Ruling Service, try to give a more precise content to the condition that the merger, division or partial division must be justified by sound economic or financial needs without explicitly relying on Article 11.1 (a) of the Directive.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' Please see 11.1 and 11.2.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof See above, answer to 11.1.	

BULGARIA

Abbreviations

English	Bulgarian	English	Bulgarian
CITA	ЗКПО	Corporate Income Tax Act	Закон за корпоративно подоходно облагане
CA	ТЗ	Commerce Act	Търговски закон
GAAP	ОПСП	Generally Accepted Accounting Principles	Общоприети счетоводни принципи
IAS	МСС	International Accounting Standard	Международен счетоводен стандарт
IFRS	МСФО	International Financial Reporting Standards	Международни стандарти за финансово отчитане
MD	ДС	Merger Directive	Директива за сливанията
SE	ЕД	Societas Europea	Европейско дружество
SG	ДВ	State Gazette	Държавен вестник
TSSPC	ДОПК	Tax and Social Security Procedural Code	Данъчно-Осигурителен Процесуален Кодекс
NASSME	НССМСП	National accounting standards for small and medium enterprises	Национални счетоводни стандарт за малки и средни предприятия

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
<u>Overall state of implementation</u> The Merger Directive has been implemented with the new Corporate Income Tax Act of December 2006, (promulgated in the State Gazette No 105, dated 22 December 2006), which entered into force on January 1, 2007. Further amendments to the provisions of CITA, governing the implementation of Directive 90/434/EEC (MD) were supplemented at the end of 2007 (promulgated in State Gazette No 110, dated 21 December 2007), and entered into force on 1 January 2008. In its initial format the provisions of CITA fully implemented the MD clauses regarding all types of mergers, namely: merger (fusion), merger by the formation of a new company, division, partial division, transfer of assets and exchange of shares or interests, and applying both to resident companies, as well as in which companies from two or more EU Member States are involved. The SE Regulation (No 2157/2001) has been implemented with the CITA of December 2006. The SCE Regulation (No 1435/2003) has been implemented with the CITA of December 2006. As of May 2008, the Bulgarian National Revenue Agency has not issued any guidelines relevant for the interpretation and/or the implementation of the MD.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> The expression 'in which companies from two or more Member States are involved' has been interpreted as comprising only the companies directly involved in the transaction and not the parent companies. The transferring and the receiving companies must be companies established in accordance with the legislation of a Member State. So far, no reference is in place in CITA to the applicability thereof to EEA Agreement. The registered office and the place of management of the transferring company and the receiving company must both be located within the EU although not necessarily within the same Member State.	Article 125 of CITA Article 135 of CITA Article 137 of CITA

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
<u>**1.2 Foreign Member State and third state merger**</u> The Bulgarian CITA enacting the MD does not interpret 'companies involved' in this scenario as including parent companies. CITA applies also to foreign merger if both merging companies are from EU Member States or from one Member State. Bulgarian CITA would not apply if one of the merging companies is from a third (non EU Member) State.	Article 125 of CITA

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
<u>**2.1 The term 'securities'**</u> With respect to securities ('*Акции*' or '*Дялове*'), in the meaning of CITA reference can be made to the definitions contained in the Bulgarian corporate law and in particular the Commerce Act. Securities mean in case of a limited liability and/or joint-stock company a share in the registered equity and in case of any form of a company – the rights representing the interest held in the company's equity. In case of a transfer or a division/partial division, CITA refers to securities of the receiving company, which can either be new shares of the receiving company or existing shares of the receiving company, which it holds. In case of an upstream merger (under Article 2 (a), third indent of MD, i.e. a company, on being dissolved without going into liquidation, transfers all its assets and liabilities to the company holding all the securities representing its capital) it is possible that no new shares are issued. In case of a transfer of assets and an exchange of shares, CITA refers to issuing of securities of the newly formed/receiving/acquiring company, whereby issue of securities for the purposes of this section of CITA is defined as the event where newly issued or held own shares or interests are provided by a newly formed, receiving or acquiring company.	Article 117 of CA Article 175 of CA Article 133 of CITA

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' According to the provisions of CITA the possibility to allow a 10% cash payment for reorganization at book value has been implemented for all types of reorganization as per the MD and it applies on per shareholder basis. The current wording of the Article 132 CITA suggests that cash payments are performed only for the purpose of achieving a parity of exchange; therefore it excludes a cash buy-out of minority shareholders.	Article 132 (1) of CITA

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger The Bulgarian CITA has implemented only the three types of merger provided under Article 2(a) of the MD.	Articles 126 and 127 of CITA

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares To determine whether or not the contribution is a qualifying exchange of shares i.e., one that qualifies for the relief, all contributions forming part of a single transaction (contribution in kind to establish the acquiring company or one and the same increase of the registered capital of the acquiring company) will be included in determining the exchange as a qualifying exchange. An exchange will be a qualifying exchange if the conditions are met with respect to the acquiring shareholder after that transaction.	Article 131 of CITA

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>2.5 Consolidation of qualifying holding</u> There are no specific conditions for granting relief. If the acquiring company already owns a majority holding any further exchanges of shares (including the contribution of non-voting shares) would be treated as a qualifying exchange of shares.	Article 131 of CITA

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 *'Andersen og Jensen'*. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>2.6 The term 'branch of activity'</u> Although the wording of the Bulgarian definition of the term 'branch of activity' is not exactly the same as the wording of the MD, we may conclude that the Bulgarian CITA reproduces in full the provision of Article 2(i) of the MD. According to Bulgarian tax law 'Branch of activity' shall be an aggregation of assets and liabilities of a company by the virtue of which from an organizational, functional and financial point of view, an independent business can be carried out'. Therefore in order to fall within the definition, the branch of activity must be capable of working on its own, the transferred business should consist of related assets and liabilities, which should be able to form an entire business.	Article 134 of CITA,

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> No, according to Bulgarian CITA the MD applies only to the entities listed in Annex 3 and subject to the taxes listed in Annex 4.	Article 137 of CITA Annex 3 to Article 137, item 1, Annex 4 to Article 137, item 3

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
3.2 Transparent entities All entities are treated as corporate entities. Bulgarian tax law does not know the concept of tax transparent entities.	Article 2 of CITA

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency 3.3.1 Tax residency under domestic law A company is tax resident of Bulgaria if established under the laws of Bulgaria, or companies established under Regulation No 2157/2001 and cooperatives, established under Regulation 1435/2003, having their statutory seat in Bulgaria, and they are duly registered in a Bulgarian register. 3.3.2. Tax residency under Double Taxation Treaties Bulgarian Double Taxation treaties provide for the following tiebreaker criterion to determine the tax residency of companies: Where by reason of tax residency on grounds of place of management or any other criterion of a similar nature a person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident only of the State in which its place of effective management is situated. However, some of the treaties use the place of incorporation as the tiebreaker rule. 3.3.3. Statutory seat under domestic company law Under Bulgarian domestic company law, the statutory seat of a company is the place of effective management. In accordance with the provisions of Article 8 of the SE Regulation and Article 7 of the SCE Regulation, amendments to the Bulgarian Commerce Act were introduced as of 1 January 2008, where the statutory seat of a SE is the place of its effective management.	Article 3 of CITA Article 137, item 2 of CITA Article 12, Paragraph 1 of CA Article 281, Paragraph 2 of CA

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject-to-tax clause According to Article 137, item 3 of CITA, a company will fall within the scope of the MD if its profits are subject to a tax covered under Annex 4 to CITA (i.e. the types of taxes listed in Article 3 (c) of the MD) or to a similar profits tax and the company has no option or the possibility of being exempt from the levy of such tax. No administrative guidance has been issued so far by the Bulgarian tax administration.	Article 137, item 3

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
3.5 Shareholder requirements The ownership of a company by EU or EEA nationals or residents is not relevant for the application of the CITA.	Article 137 of CITA

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
4.1 The concepts of 'real values' and 'value for tax purposes' 4.1.1 Real value Bulgarian CITA does not use the term 'real value' but rather accepts the definitions thereof of the applicable accounting standards. The applicable accounting standards in Bulgaria are IAS and NASSME, which provide for similar accounting treatment. Pursuant to these standards the transferred assets, liabilities and equity should be measured at their fair value at the date of exchange. The fair value is defined as the amount for which as asset could be exchanged, a liability settled or an equity instrument granted could be exchanged between knowledgeable, willing parties in an arm's length transaction. 4.1.2 Value for tax purposes 'Value for tax purposes' has been interpreted as the tax book value of the assets in the books of the transferring company at the time of the reorganization.	Article 143 (1), CITA Article 140 (3) CITA Paragraph 1, items 8,10 of the Additional provision of TSSPC IFRS 3 IFRS - definitions

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions No specific guidance has been issued in respect to divisions and partial divisions by the Bulgarian National Revenue Agency.	

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' The Bulgarian CITA and the tax practice do not contain a reference to the concept of 'effectively connected' as a result of which currently the interpretation of the provision of Article 139 of CITA 'assets and liabilities subject to reorganisation' is rather inconsistent. To be taxable in Bulgaria the assets of a foreign company must be allocated to a permanent establishment of the receiving company in Bulgaria, i.e. related to its activity following domestic tax rules, as well as the applicable double taxation treaty (if any). As long as the concept of 'permanent establishment' is concerned, CITA refers to TSSPC, which defines permanent establishment as a fixed place (whether owned, rented or used on other grounds) where through a non-resident carries on business inside the country, wholly or partly, such as: a place of management; a branch; a representative office registered in the country; an office; a bureau; a studio; a plant; a workshop (factory); a retail shop; a wholesale storage facility; an after-sales service establishment; an installation project; a building site; a mine; a quarry; a prospecting drill; an oil or gas well; a water spring or any other place of extraction of natural resources; conduct of business inside the country by persons authorized to contract on behalf of non-resident persons, with the exception of the business of agents of independent status; sustained effecting of commercial transactions with a place of performance inside the country, even where the non-resident person has no permanent representative or fixed base. So far no administrative guidance on the interpretation and implementation of the above concepts of 'effectively connected' and 'permanent establishment' has been issued by the Bulgarian National Revenue Agency. However, the double taxation treaties of Bulgaria strictly follow the OECD Model Tax Convention in respect of the permanent establishment concept and respectively the tax administration follows the Commentary to the OECD Model Tax Convention, when interpreting and applying this concept.	Article 139 of CITA Paragraph 5 TSSPC

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
<u>**4.4 Limitation of the scope of relief**</u> No limitation of the scope of relief is envisaged ex lege under CITA, nor is sought currently by the Bulgarian tax authorities.	Article 140 CITA

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
<u>**4.5 Assets and liabilities not effectively connected with a permanent establishment**</u> Where the transferred assets and liabilities are not effectively connected with a permanent establishment after the reorganization, they are deemed realized at market prices and written off. CITA defines 'market price' as the amount, net of value added tax and excise duties, which would be paid under the same conditions for identical or similar goods or services under a transaction between unrelated parties. In this case upon determination of corporate tax base of the transferring company, the taxable profit of the latter shall be increased with the gain and shall be decreased with the loss arrived at as a difference between the market price of the asset or liability and the accounting value thereof at the date of reorganization.	Article 142

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
<u>**4.6 Tax treatment of shares of the receiving company**</u> Bulgarian CITA provides that the share of the merger profit equal to the holding of the receiving company in the transferring company would follow the rules applicable for the taxation of capital gains from the disposal of shares. As a result such portion of the merger profit would be tax exempted.	Article 148 of CITA

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*	Reference
4.7 Tax deferral Please see 4.5 above. It should be noted that Bulgarian CITA has implemented the concept of deferring the taxation to the date of the disposal for newly acquired shares only. No further legislative amendments was made, following the judgment in Case C-470/04 'N'.	Article 149 of CITA

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities Article 4(2) of the Merger Directive is not implemented in the Bulgarian CITA because there are no tax transparent entities under Bulgarian tax legislation.	

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief 4.9.1 Concept The receiving company shall inherit the tax attributes regarding the valuation of assets, the depreciation method, the reserves reducing the profits for tax purposes, etc. of the transferring company. 4.9.2 Conclusion The implementation is in accordance with Article 4 of the Merger Directive.	Article 140, Paragraphs 2 and 5 of CITA

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
5.1 The term 'provisions and reserves' Provisions are only defined in the IFRS followed by Bulgaria and do not have tax effects. The notion of reserves also follows the IAS framework, and reserves are recognized for tax purposes in very specific situations.	IAS 37; § 1, item 19 of the AP of CITA, Article 45 of CITA, Article 140, Paragraphs 4 of CITA

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments Provisions and reserves are excluded from the tax-neutral carry over only if the permanent establishment is located in a non EU Member State. However, also with non EU Member States Bulgaria has concluded several tax treaties applying for permanent establishment profits, in principle, the exemption method, which again excludes the respective assets from taxation. Accordingly, in practice such issue would arise with permanent establishment in non EU countries having no tax treaty with Bulgaria or treaties in which Bulgaria applies credit method. In such cases, excluded from the tax-neutral carry over would be assets (including tax effective reserves) which economically belong to each such permanent establishment. There is no guidance on how such assets are further determined.	Article 142, Paragraphs 1 and 2 of CITA

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves Please see 5.2.	Article 140 CITA

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves No conditions other than these stipulated above.	Article 138

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry-over of losses The concept of 'loss' has not been specifically defined for the purposes of implementing the MD. Therefore, the general principles applied under	Article 144 and 146 of CITA

domestic tax legislation will apply, and a loss is deemed to arise when the expenses exceed the related income. The rule set under CITA is, that in case of reorganization (except for merger, as a result of which a permanent establishment of a company from another Member State is created for the first time in the country) the receiving companies shall not have the right to carry forward the tax losses formed by the transferring companies. The above rule applies also with regard to the interest expense portion added back to the taxable profit following the application of the thin cap rules, carried forward as a timing difference under the thin capitalization rules (should the debts of a company to shareholders, third parties and/or to banks of the debtor's group of companies or from bank loans guaranteed by related party, exceed three times the Company's equity, then thin capitalization related interest tax deductibility restrictions are triggered). Specifically, for tax purposes interest expenses exceeding interest income are limited to 75% of EBIT (accounting result before interest expenses and interest income). In case the EBIT is a loss, the entire amount of the interest expense is considered non-deductible. The thin capitalization add-back is a timing difference and the Bulgarian thin capitalization rules allow for a 5-year carry forward of such portion of the interest. However no carry over is permissible upon a local or cross-border merger, where the acquiring entity is different.	

What method is applied to allocate losses to the permanent establishment?	Reference
<u>6.2 Allocation of losses to the permanent establishment</u> Losses are allocated to a permanent establishment the same way as income is allocated (see 5.2 above). However carry over of losses incurred by a permanent establishment is not possible (see 6.1 above). The only exception to carry over of losses is the cases of a merger, as a result of which a permanent establishment of a company from another Member State of the European Community is formed in the country and the said company has not had a permanent establishment in the country before the reorganization. In these cases the entire loss is carried forward to the permanent establishment of the receiving/the new company. Furthermore, no guidance exists for carry over of such loss. However, according to our interpretation, the reasoning of that would be that contrary to the general rules, where the carry over of losses is not permissible, the change of the legal form of operations of the company, e.g. from subsidiary to permanent establishment should not suffer tax disadvantages, unless the acquiring company maintained another permanent establishment in which case the disallowance of the loss carry over is assimilated with the disallowance of the loss carry over in local mergers.	Article 144, Paragraph 2 CITA Article 146, Paragraph 2 CITA

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
<u>**6.3 Specific legislation for divisions/partial divisions/transfer of assets**</u> The carry over is not allowed in case of division, partial division or transfer of assets.	Article 144, Paragraph 1 of CITA and Article 146, Paragraph of 1 CITA

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
<u>**6.4 Further conditions for carry over of losses**</u> Yes, please see 6.2 above (i.e. merger with formation of a permanent establishment in the country). In our view the conditions are compliant with EU law, since they still facilitate change in the legal form of establishment in the country, in line with the freedom of establishment, while the carry over of losses is completely prohibited in domestic reorganisations.	Article 144, Paragraph 2 of CITA ; Article 146, Paragraph 2 of CITA

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
<u>**7.1 Amended holding threshold**</u> The CITA provides that any profit or loss in connection with the cancellation of the holding in this case shall not be taxed. This applies irrespective of the percentage held.	Article 148 CITA

Article 7(1) covers <u>gains</u> accruing on the cancellation of a holding. It does not cover <u>losses</u> that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
<u>**7.2 Treatment of losses**</u> Where a receiving company has a holding in the capital of a transferring company, the accounting profits or losses in connection with the write-off of the said holding in the capital shall not be recognized for tax purposes.	Article 148 CITA

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
<u>**8.1 Avoidance of economic double taxation at the level of the shareholder**</u> All shares received by the acquiring company will be valued for tax purposes at fair value in accordance with accounting rules. Indeed contrary to the obligation of the shareholders of the acquired company to form a temporary tax difference from subsequent valuation no tax difference is stipulated for the shares received by the acquiring company.	Article 18, per argumentum a contrario Chapter 8, and Article 143 of CITA

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>**8.2 Computation of the capital gain**</u> There is no related guidance issued by the Bulgarian tax authorities. According to CITA unlike the share compensation, the cash payments would be subject to capital gain taxation.	

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>**8.3 Further conditions for tax relief**</u> The relief under Article 8 of the Merger Directive to non-resident shareholders which are legal entities has been made subject to their obligation to submit annually to the Sofia Territorial Tax Office a declaration that they have not disposed of the shares received in exchange. Failure to submit such a declaration leads to the presumption of disposition of the shares received in exchange. In our view this condition can only be seen as compatible with EU law if this presumption is refutable.	Article 149, Paragraphs 6 and 7 of CITA

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
9.1 Avoidance of economic double taxation at the level of the transferring company Avoidance of economic double taxation at the level of the transferring company is provided only in case the newly acquired shares are held for an uninterrupted period of at least five years. The gain or loss arising from the transfer of the assets are disregarded for tax purposes at the moment of the transfer and form a temporary tax difference from subsequent revaluation of the assets, attributed to the shares acquired in return for the transferred assets. In the event that the newly acquired shares are transferred before the lapse of the 5 year period, the temporary tax difference will be reversed, i.e. the gain will be taxed at the moment of the disposal of the shares. If the shares are held uninterruptedly for at least five years, the temporary tax difference shall not be recognized for tax purposes, hence there shall be no taxation at the level of the transferring company.	Article 150 of CITA

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
9.2 Further conditions for tax relief Please see 9.1.	Article 150 of CITA

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
9.3 Tax deferral There is no taxation in Bulgaria triggered by the change of the place of effective management of a company from Bulgaria to another country, even if this would imply (in situations where the relocating of the place of effective management is effected to tax treaty country) the loss of the tax residence status.	Article 154 CITA

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>**10.1 Loss recapture for permanent establishments in third Member States**</u> Generally, Bulgaria applies the exemption method with tax treaties countries. This also applies for EU countries, with the exception to the Czech Republic, Slovak Republic, Cyprus and Estonia, for which the credit method applies. In the above cases, where the credit method applies, it is allowed that the tax losses of a permanent establishment be offset against domestic profits and upon a merger, a division, a partial division or a transfer of assets any losses offset should be recaptured.	Article 14 and 145 CITA Article73 CITA

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>**10.2 Permanent establishment in the Member State of the receiving company**</u> Similar treatment as in 10.1.	Article 145/CITA

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>**10.3 Concept of worldwide taxation/tax credit system**</u> Bulgaria has not opted for any taxation under Article 10(2).	Article 142, Paragraphs 1 and 2 of CITA

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
<u>**10.4 Tax deferral**</u> Bulgaria has not opted for any taxation under Article 10(2).	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies This provision is not relevant for Bulgaria as it treats all entities as corporate tax liable persons.	Article 2 of CITA

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit N/A. Please see 10a.1.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit N/A. Please see 10a.1.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders N/A. Please see 10a.1.	

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company N/A. Please see 10a.1.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation Pursuant to Bulgarian legislation, transfer of the registered office abroad cannot be effected, unless the Bulgarian company is liquidated; therefore, final corporate income tax returns must be submitted to the Bulgarian Tax Authorities and the corporate income tax paid. However, in the case of SEs and SCEs, this provision is not applicable, (i.e. the transfer of the registered office of an SE or SCE would not give rise to exit taxation under Bulgarian legislation) for the business that the SE or SCE continues in Bulgaria through its Bulgarian permanent establishment.	Chapter 21/CITA

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' The term 'head office' is not explicitly defined in the Bulgarian tax legislation. Article 3/CITA stipulating the criteria for Bulgarian tax residency refers to Bulgarian company law, i.e. the Commerce Act. Under Bulgarian company law, the head office is the registered office. The concept of the registered office is also applied under Bulgarian double taxation treaties when defining Bulgarian tax residency of a legal person.	Article 3 of CITA Articles 12 and 14 of CA

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency Yes. Please see our comments to 10b.2 above.	

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>**10b.4 Assets and liabilities not effectively connected with a permanent establishment**</u> As noted above, the transfer of the registered office could be effected upon liquidation of the company's activity in Bulgaria for corporate income tax purposes; therefore, final corporate income tax returns would have to be submitted (please see 4.5). However, in the case of SEs and SCEs, this provision is not applicable, (i.e. the transfer of the registered office of SE or SCE would not give rise to exit taxation according to Article 153/CITA) provided that the SE or the SCE continues its activities in Bulgaria through its Bulgarian permanent establishment. Should assets and liabilities not effectively connected with the permanent establishment, any gain on such assets is taxable as the preferential treatment for SEs and SCEs is not applicable. These assets and liabilities are deemed realized at market prices and written off.	Chapter 19, Section III/CITA

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
<u>**10b.5 Tax deferral**</u> Please, see section 10b.1.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
<u>**10c.1 The term 'comparable circumstances'**</u> The term has not been defined in the law, nor has it been developed in administrative guidelines.	

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
<u>10c.2 Loss recapture for permanent establishments</u> Such losses cannot be offset against domestic profits. Please see our comments in 10.1 above.	Article 145/CITA

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>10d.1 Deemed liquidation</u> The Bulgarian tax legislation does not contain any provisions on this matter. The transfer of registered office of an SE/SCE should not result in any taxation on the shareholder level.	

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>10d.2 Tax treatment of third country residents</u> There are no specific provisions regulating the tax treatment of third country residents under these circumstances. Thus, the transfer of registered office of an SE/SCE should not result in any taxation on the shareholder level.	

Article 11 – Anti-abuse provisions

	Reference
11.1 Transposition of anti-abuse provisions The beneficial tax treatment provisions of Section II and Section III of Chapter 19 of CITA will not apply where the transformation has as its objective tax evasion or tax avoidance. Tax evasion shall be presumed, inter alia, where the transformation is not carried out for valid commercial reasons or where certain assets are in essence sold, although concealed through the share compensation, with the sole purpose to benefit from the tax relief provided by the Merger Directive, resulting in the non-taxation of the sale of the assets.	Article 151/CITA

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' (*'Kofoed'*, paragraph 46)?	Reference
11.2 General anti-abuse provision Capital gain tax and withholding taxes are not within the scope of the general anti-abuse provision. There are no special anti-avoidance rules covering capital gain tax and withholding taxes either.	Chapter 4/CITA

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' The concept of 'wholly artificial arrangement' has not been developed in the Bulgarian legislation or case law or administrative guidelines.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions The specific anti-abuse provisions discussed in 11.1 above have not been applied yet by the tax authorities.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' No guidelines have been issued in this respect.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof According to the Ex Oficio principle of Article 5 of the Bulgarian Tax and Social Security Procedure Code the revenue authorities shall be liable to establish all facts and circumstances relevant to the assessment and collection of public receivables, which also includes the application of any tax relief provided for in the law.	Article 5/TSSPC

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Abbreviations

English	Greek	English	Greek
ACT Law		The Assessment and Collection of Taxes Law of 1978 to 199 (as amended)	Ο περί Βεβαιώσεως και Εισπράξεως Φόρων Νόμος (Αρ. 4/1978, όπως τροποποιήθηκε)
Circular		Tax Circular issued by the Inland Revenue Department	Εγκύκλιοι Τμήματος Εσωτερικών Προσόδων
CGT		Capital Gains Tax, a transactional tax levied on gains from a disposal of property	Φόρος Κεφαλαιουχικών Κερδών ο οποίος επιβάλλεται πάνω στο κέρδος από διάθεση ιδιοκτησίας
CGT Law		The Capital Gains Tax Law of 1980 to 1999 (as amended)	Ο περί Φορολογίας Κεφαλαιουχικών Κερδών Νόμος (Αρ. 52/1980, όπως τροποποιήθηκε)
CIT		Corporate Income Tax, a direct tax levied on profit	Εταιρικός Φόρος, ο φόρος ο οποίος επιβάλλεται πάνω στο εισόδημα κάθε εταιρείας
Companies Law		The Companies Law, Chapter 113 of the Laws of Cyprus (as amended)	Ο περί Εταιρειών (όπως τροποποιήθηκε) Νόμος Κεφάλαιο 113
Defence Tax		Special Contribution for the Defence of the Republic, a direct tax levied on certain types of income	Έκτακτη Εισφορά για την Άμυνα της Δημοκρατίας
EU		European Union	Ευρωπαϊκή Ένωση
IFRS	ΔΛΠ	International Financial Reporting Standards	Διεθνή Λογιστικά Πρότυπα
IRD	ΤΕΠ	Inland Revenue Department	Τμήμα Εσωτερικών Προσόδων
ITL		Income Tax Law of 2002 No. 118(I) of 2002 (as amended)	Ο περί Φορολογίας του Εισοδήματος Νόμος (Αρ. 118(I)/2002, όπως τροποποιήθηκε)
MD		EU Merger Directive	Οδηγίας της ΕΟΚ σχετικά με το κοινό φορολογικό καθεστώς για τις συγχωνεύσεις, διασπάσεις, εισφορές ενεργητικού και ανταλλαγές μετοχών

		που αφορούν εταιρείες διαφορετικών κρατών μελών
SDC Law	Special Contribution for the Defence Fund of the Republic Law of 2002 No. 117(I) of 2002 (as amended)	Ο περί Εκτάκτου Εισφοράς για την Άμυνα της Δημοκρατίας Νόμος (Αρ. 117(I)/2002, όπως τροποποιήθηκε)
SE	Societas Europaea	Ευρωπαϊκή Εταιρεία
Stamp Duty	Stamp Duty, a transaction tax levied on instruments relating to immovable property situated in Cyprus or to any matter or thing performed or done in Cyprus.	Τέλος Χαρτοσήμου το οποίο επιβάλλεται σε έγγραφον εάν αφορά σε οποιονδήποτε περιουσιακό στοιχειό που βρίσκετε στην Δημοκρατία ή σε ζητήματα η πράγματα τα οποία θα εκτελεστούν ή θα γίνουν στην Δημοκρατία ανεξάρτητα από τον τόπο σύνταξης του.
Stamp Law	Stamp Law of 1963 (as amended)	Ο περί Χαρτοσήμων Νόμος (Αρ.19/1963, όπως τροποποιήθηκε)

Survey of the Implementation of Council Directive 90/434/EEC

(The Merger Directive, as amended)

CYPRUS

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
<u>Overall state of implementation</u> Cyprus joined the EU on May 1, 2004. Before accession, Cyprus thoroughly revised its tax regime to make the Cypriot tax legislation compatible with EU requirements by changing the laws of taxation of income and gains. Consequently, there were no specific tax acts or amending laws to implement the MD in the existing Cypriot CIT legislation. The ITL came into force on January 1, 2003 and specifically states that it is issued among others for the purpose of harmonization with the MD. The ITL includes a section regarding company reorganizations which is aimed at implementing the MD. The principal Stamp Law was amended twice in 2002 in the EU law harmonization process by laws 121(I)/2002 and 222(I)/2002. These law amendments came into force on January 1, 2003 and brought about (among others) the introduction of exemptions from stamp duty in case of company reorganizations, in order to comply with the MD. The CGT Law excludes transfer of property in case of reorganization from the definition of 'disposal of property'. Cyprus levies capital duty in the form of registration fees at a rate of 0.6% upon establishment of a Cypriot company and upon increase of the registered authorized share capital. Such registration fees are also payable in case of qualifying company reorganizations. Recently, regulations were incorporated into the Companies Law allowing cross border legal merger transactions.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> The ITL defines company reorganizations as merger, division, partial division, transfer of assets, exchange of shares, and transfer of the registered office, involving companies that are resident in Cyprus and/or companies not resident in Cyprus. Since the definition does not include a jurisdictional restriction to 'two or more Member States' (except in case of a transfer of registered office whereby an SE or an SCE must transfer its registered office from one Member State to another Member State), it has not been relevant in practice to interpret the word 'companies' as either comprising only the companies directly involved in the transaction or also the parent	Article 30 ITL Article 2 ITL Article 2 CGT Law Article 10(h) CGT Law Article 2 Companies Law First Schedule to the ITL

companies. Considering the above, we have not identified any incompatibility issues with the implementation of Article 1 of the Merger Directive. It is understood that the expression 'involving companies' is interpreted as comprising only the companies directly involved in the transaction and not the parent companies but no or limited interpretation or implementation policy has been released / published by the competent authorities. The term 'company' has the meaning assigned to this term by the Companies Law and includes any body with or without legal personality, or public corporate body, as well as every company, fraternity or society of persons, with or without legal personality, including any comparable company incorporated or registered outside Cyprus and a company listed in the First Schedule, but it does not include a partnership.	

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
<u>**1.2 Foreign Member State and third state merger**</u> There are no jurisdictional restrictions for the application of the company reorganization relief rules (other than in case of a transfer of registered office whereby an SE or an SCE must transfer its registered office from one Member State to another Member State). The rules apply to the listed reorganizations involving companies resident in Cyprus or outside Cyprus. As long as the merging companies from the single (foreign) Member State or from the third state(s) can be considered to be 'companies', i.e. are comparable to Cypriot companies or are companies listed in the First Schedule, the benefits of the reorganization relief rules would be applied. We refer to our comments below in 3.1.	Article 30 ITL

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
<u>**2.1 The term 'securities'**</u> Securities are defined in the ITL as shares, bonds, debentures, founders' shares and other titles of companies or other legal persons, incorporated under a law in Cyprus or abroad and options thereon. Under current tax practice certain instruments such as investment units and investment certificates of investment funds which do not have legal personality are considered not to qualify as securities (unless the investment funds are	Article 2 ITL Article 30 ITL

body corporates listed in the First Schedule). However it is also our understanding that the current tax practice, about which participation instruments do and do not qualify as 'securities', is under discussion and may be reconsidered (broadened). It is relevant to note that the company reorganization relief rules in the ITL, in defining the qualifying transactions, refers to shares and not to securities (except for the definition of the partial division which was added at a later stage by amending law 2(b) of 80(I) 2007). This may be found to be incompatible with the implementation of the Merger Directive.	

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
<u>**2.2 The term 'cash payments'**</u> The company reorganization relief rules allow cash payment not exceeding 10% of the nominal value of the shares, or, in the absence of a nominal value, of the accounting value of those shares in case of merger, division, partial division and exchange of shares. There are no specific rules or guidelines as to whether the 10% cash payment applies on a per shareholder basis or on an overall basis. The form IR88, which is used to apply for the issue of a certificate of exemption from the payment of taxes because of reorganization, may point towards the latter. The form requires the applicant to specify the consideration in shares and cash on an overall basis. A detailed list of the shareholders of the receiving and transferring companies needs to be attached to the form including full name, tax code and number of shares, class/category of shares and participation percentage (but not cash payment per shareholder).	Article 30 ITL Form IR88

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
<u>**2.3 Further types of merger**</u> No. The company reorganization relief rules cover the same three types of merger.	Article 30(a) ITL

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
<u>2.4 Qualifying exchange of shares</u> Article 30(d) of the ITL reads: 'Exchange of shares shall mean an operation whereby a company acquires a holding in the capital of another company such that it obtains a majority of the voting rights in that company, or, holding such a majority, acquires a further holding, in exchange for the issue to the shareholders of the latter company, in exchange for their shares, of shares representing the capital of the former company, and, if applicable, in exchange for a cash payment not exceeding ten per cent (10%) of the nominal value or, in the absence of a nominal value, of the accounting par value of the shares issued in exchange.' As a result, the company reorganization relief rules could not only be applied in respect of an exchange that leads to the acquisition of a majority holding but could also be applied in case of a gradual increase in an existing majority stake of the target company.	Article 30(d) ITL

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>2.5 Consolidation of qualifying holding</u> No. We refer to the text of the ITL quoted above (please see 2.4).	Article 30(d) ITL

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 *'Andersen og Jensen'*. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>2.6 The term 'branch of activity'</u> 'Branch of activity' is defined in the ITL as 'all the assets and liabilities of a division of a company which, from an organizational point of view, constitute an independent business, that is to say an entity capable of functioning by its own means'. There are no further laws or guidelines regarding this definition.	Article 30(i) ITL

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> Yes and no. As explained above, the ITL states that the term 'company' has the meaning assigned to this term by the Companies Law and includes any body with or without legal personality, or public corporate body, as well as every company, fraternity or society of persons, with or without legal personality, including any comparable company incorporated or registered outside Cyprus and a company listed in the First Schedule, but it does not include a partnership. The Companies Law states that 'company' means a company formed and registered under the Companies Law or an existing company. The First Schedule provides a list of companies primarily based on the list annexed to the EU Parent Subsidiary Directive. The companies listed in the First Schedule mainly are the same as those listed in the Annex of the MD but some small differences exist: in the First Schedule, the lists of companies under Czech-, Greek-, Spanish-, Austrian- and Slovak law are more elaborate whereas the list of companies under Hungarian law covers one type of company less than the Annex to the MD ('*Közhasnú Társaság*') and the list of companies under the law of Lithuania is specified. Moreover, companies registered in the new EU Member States Bulgaria and Romania are not included in the First Schedule yet. The list of companies as taken up in the First Schedule is primarily based on the list annexed to the Parent Subsidiary Directive but also in this respect, some small differences exist: in the First Schedule, the list of companies under Czech- and Slovak law cover one extra type of company while the list of companies under the law of Lithuania is specified and –as mentioned above– companies registered in the new EU Member States Bulgaria and Romania are not included in the First Schedule yet. As a result, based on the broad definition given in the ITL and the fact that the First Schedule is based on the list annexed to the Parent Subsidiary Directive which appears to be slightly more elaborate than the Annex to the MD, the company reorganization relief rules may apply to more types of entities than those listed in the Annex to the MD. However, as mentioned above on the other hand some small differences exist between the Annex to the Merger Directive and the First Schedule which may cause the company reorganization relief rules to apply to less types of entities than those listed in the Annex to the MD. Most importantly one type of Hungarian company and the companies registered in the new EU Member States Bulgaria and Romania are not included (yet) in the First Schedule enclosed to the ITL. If such companies not on the list in the First Schedule can still qualify as a 'company' under the general wording of Article 2 ITL, no disparity would occur. However, a disparity may occur if there are cases where a Hungarian '*Közhasnú Társaság*' or a Bulgarian or Romanian body corporate is included in the annex to the Merger Directive but is not considered to be a 'company' which is 'incorporated or	Article 2 ITL Article 2 Companies Law First Schedule to the ITL

registered' based on domestic rules. If such cases indeed exist, this may be found to be a limitation to the implementation of the Merger Directive.	

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
3.2 Transparent entities Entities listed in the First Schedule are regarded as companies from a Cypriot tax perspective and are therefore not regarded as being tax transparent. A disparity may occur for legal corporate bodies from countries not included in the First Schedule yet (the Hungarian '*Közhasnú Társaság*', Romanian corporate bodies and Bulgarian corporate bodies) which are included in the list but are –based on domestic law– not considered to be a company which is 'incorporated or registered'.	First Schedule to the ITL

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency Cypriot tax residency is based on management and control. A Cypriot tax resident company is a company that is managed and controlled from Cyprus. Where a company is considered to be resident of more than one country, Cypriot double tax treaties generally also refer to the place of effective management as a tiebreaker clause.	Article 2 ITL

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject-to-tax clause The subject-to-tax clause is not part of the company reorganization relief rules.	Article 30 ITL

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
3.5 Shareholder requirements No.	Article 30 ITL

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>4.1 The concepts of 'real values' and 'value for tax purposes'</u> The ITL does not refer to the concepts of 'real values' and 'value for tax purposes'. The ITL states that assets and liabilities, including provisions and reserves, which are transferred under a reorganization, shall not give rise to profits liable to tax for the transferring company. Consequently, we have not identified any incompatibility issues with the implementation of Article 4 of the Merger Directive.	Article 26 ITL

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
<u>4.2 Specific guidance for divisions/partial divisions</u> No specific guidance has been issued in respect of divisions and partial divisions.	N/A.

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>4.3 The concepts of 'effectively connected' and 'permanent establishment'</u> The concept of 'permanent establishment' has been defined in the ITL as a fixed place of business through which the business of an enterprise is wholly or partly carried on. This definition is in practice used as a starting point taking into account specific provisions under the double tax treaties concluded by Cyprus with other countries and taking into account the commentary to the OECD Model Tax Convention. There are no specific laws or guidelines in Cyprus on the concept of 'effectively connected' but in principle a functional approach is taken.	Article 2 ITL

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
<u>4.4 Limitation of the scope of relief</u> The IRD does not seek to limit the scope of relief by for instance recapture of depreciation on the assets transferred. The receiving company must compute any new depreciation and any profits or losses in respect of the	Article 26 and 27 ITL

assets, liabilities, provisions and reserves transferred according to the conditions that would have applied to the transferring company or companies if the reorganization had not taken place. However, carry over of losses is restricted to domestic situations.	

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
<u>**4.5 Assets and liabilities not effectively connected with a permanent establishment**</u> Cyprus has no rules that govern and ensure the domestic taxation of undisclosed reserves in case of a company ceasing to be a taxpayer in Cyprus except in case of trading stock. As a result, in case Cyprus would lose the right to tax the gain on the disposal of the transferred assets with the receiving corporate entity or such right would be limited, the respective transferred assets do not need to be re-valued at fair market value in the closing balance sheet of the transferring company. In case of trading stock, being property sold in the ordinary course of trade or materials used in the manufacture, preparation or construction of such property, re-valuation should in principle take place unless the balance sheet values may be carried over under the company reorganization rules as explained above. There is no requirement in the law that a permanent establishment would need to remain in Cyprus in a merger transaction where the Cypriot company is to be the disappearing entity.	Article 12 ITL

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
<u>**4.6 Tax treatment of shares of the receiving company**</u> Based on the ITL, where the receiving company, resident in Cyprus or, if not resident in Cyprus having a permanent establishment in Cyprus, has a holding in the capital of the transferring company, any profits accruing to the receiving company on the cancellation of the holding shall not be liable to tax.	Article 28 ITL

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>**4.7 Tax deferral**</u> Case law of the ECJ has not had any impact on the Cypriot tax legislation or interpretation thereof (in the (general) absence of exit tax provisions in domestic tax law).	N/A.

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
<u>4.8 Criteria to determine tax transparent entities</u> An entity is considered to be transparent when it is not considered to be a company (in accordance with Article 2 ITL and the First Schedule) i.e. a partnership, a trust or a fund in a legal form not qualifying as 'company'. There are no specific laws or guidelines on Article 4(2) MD. Since Cypriot tax legislation refers to the First Schedule which is based on the annex to the EU Parent Subsidiary Directive for its definition of a company, it is unlikely that there would be a case where an entity would have access to the company reorganization rules whilst it is considered tax transparent. We also refer to 3.1 and 3.4 above.	Article 2 ITL

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
<u>4.9 Further conditions for tax relief</u> No.	N/A.

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>5.1 The term 'provisions and reserves'</u> The term 'provisions and reserves' have not been defined in Cypriot tax legislation or in administrative guidelines. However, determination of the taxable income for (Corporate) income tax purposes is generally based on accounts prepared in accordance with International Financial Reporting Standards, subject to certain adjustments and provisions. Therefore IFRS could be used as a guideline for defining the term 'provisions and reserves'. Further definition of the term requires an audit analysis. As preliminary high level background information we refer to IAS37 regarding provisions (e.g. for warranties, obsolete stock, etc). Capital reserves include share premium reserve, fair value reserve and retained profit reserve. As a general rule, for CIT purposes expenses are allowed in as far as they are incurred wholly and exclusively for the production of (taxable) income. Business expenses incurred in relation to tax exempt holding activities, such as interest paid to finance the acquisition of share investments, will be disallowed i.e. are not tax deductible in Cyprus. For double taxation purposes, expenses incurred for the production of the income are not tax deductible. Generally speaking, provisions should be	N/A.

tax deductible and capital reserves should not be tax deductible. Certain specifically listed provisions are tax deductible provided that the conditions are met. For example the amount of any specific provision for doubtful debts is tax deductible if the IRD is satisfied that it has or will eventually become irrecoverable.	

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments The Cypriot tax legislation does not distinguish between provisions and reserves derived from permanent establishments abroad and other provisions and reserves. As mentioned in 4.3, the definition of a permanent establishment has been codified in the ITL as a fixed place of business through which the business of an enterprise is wholly or partly carried on. In addition where a person other than an agent of an independent status is acting on behalf of an enterprise and has, and habitually exercises, in Cyprus an authority to conclude contracts in the name of the enterprise, that enterprise shall be deemed to have a permanent establishment ('Agency PE') in Cyprus in respect of any activities which that person undertakes for the enterprise, unless the activities of such person are limited to those which, if exercised through a fixed place of business, would not make this fixed place of business a permanent establishment. In the absence of additional guidance by the IRD, the latter generally interpret the abovementioned conditions for the presence of a PE in line with the Commentary to Article 5 of the OECD Model Tax Convention. Profit allocation is generally made in line with the Commentary to Article 7 of the OECD Model Tax Convention, meaning that the profits shall be attributed to the PE which it might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a PE, and allowing for expenses that were incurred for the purposes of the PE. In principle a functional approach is taken as mentioned above (please see 4.3).	N/A.

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
<u>5.3 Allocation method for provisions and reserves</u> There are no specific rules or guidelines for the allocation of provisions and reserves. We refer to our general comments above (please see 5.2).	N/A.

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
<u>5.4 Further conditions for carry-over of provisions and reserves</u> No.	N/A.

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
<u>6.1 The concept of carry-over of losses</u> There are no rules or guidelines with respect to the definition of 'loss' for the purpose of the company reorganization relief rules. However, the definition of loss is generally believed to be a tax loss calculated on the basis of Cypriot tax accounting rules, taking into account specific exemptions and restrictions of expense deductions. Generally speaking, any tax loss incurred by a Cypriot tax resident company during a tax year that cannot be offset against income from any other source during the same tax year may be carried forward indefinitely and be offset against profits from future years, without any limitation. No carry back of tax losses is allowed. Group loss relief is available between group companies which are tax resident in Cyprus, group being defined as companies one of which is at least 75% owned by the other company or where two companies are both owned by another company at least to the extent of 75%.	Article 13 ITL

What method is applied to allocate losses to the permanent establishment?	Reference
<u>6.2 Allocation of losses to the permanent establishment</u> There are no rules or guidelines with respect to the allocation of losses to a permanent establishment. However, the allocation of losses is generally believed to be determined on the basis of Cypriot tax accounting rules, taking into account specific exemptions and restrictions of expense deduction.	N/A.

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
<u>6.3 Specific legislation for divisions/partial divisions/transfer of assets</u> The ITL contains a general provision regarding carry over of losses, stating that accumulated losses of the transferring company which is resident in Cyprus or has a permanent establishment in Cyprus shall be transferred to the receiving company in Cyprus or having a permanent establishment in Cyprus. There are no specific rules or guidelines with respect to divisions, partial divisions and transfer of assets.	Article 27 ITL

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
<u>6.4 Further conditions for carry over of losses</u> No. The provisions applying for set-off or carry forward of losses in domestic situations apply accordingly to losses carried over under the company reorganization relief rules. It may be relevant to note that no carry over of (foreign) losses is allowed for losses incurred by a non resident disappearing entity not having a permanent establishment in Cyprus in the situation of a cross border merger where the Cypriot company is the surviving entity.	Article 13 ITL

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
<u>7.1 Amended holding threshold</u> Capital gains or losses realized by a Cypriot tax resident upon a sale of shares are exempt or not tax deductible in Cyprus. Capital gains or losses realized by a non Cypriot tax resident upon a sale of shares in a Cypriot company are not subject to tax in Cyprus. Moreover, the ITL states specifically that in case of a reorganization, any profits accruing to the receiving company on the cancellation of the holding shall not be liable to tax. The Cypriot tax legislation does not contain any threshold. Section 2 mentioned above was not included in the company reorganization relief rules. The exemption is granted unconditionally. Considering the above, no incompatibility problems have been identified with the implementation of Article 7 of the Merger Directive.	Article 8(22) ITL Article 28 ITL

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses There are no specific rules or guidelines regarding losses that may be realized on the cancellation of a holding on a reorganization. Generally speaking, losses realized on the cancellation of a holding are not tax deductible for CIT purposes.	N/A.

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder No. The ITL states that the allotment of shares representing the capital of the receiving or acquiring company to a shareholder of the transferring or acquired company in exchange for shares representing the capital of the latter company shall not, of itself, give rise to any profits or benefits liable to tax in respect of that shareholder. The ITL furthermore states that the shares received shall have the same value for tax purposes as the shares exchanged had immediately before the reorganization.	Article 29(2) ITL

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
8.2 Computation of the capital gain There are no rules or guidelines on the computation of a capital gain in case shareholders receive a cash payment upon a qualifying company reorganization. However, as mentioned in section 7.1, (cash) capital gains realized by a Cypriot tax resident shareholder upon a sale of shares are exempt or not tax deductible in Cyprus. Capital gains realized by a non Cypriot tax resident upon a sale of shares in a Cypriot company are not subject to tax in Cyprus (unless the company holds immovable property situated in Cyprus).	N/A.

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
8.3 Further conditions for tax relief No.	N/A.

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
9.1 Avoidance of economic double taxation at the level of the transferring company No. As mentioned above, the ITL states that assets and liabilities, including provisions and reserves, which are transferred under a reorganization, shall not give rise to profits liable to tax for the transferring company. Since reorganization is defined as merger, division, partial division, transfer of assets, exchange of shares, and transfer of the registered office involving companies resident in Cyprus, no separate Article like Article 9 MD is required to apply this provision to transfer of assets. No specific rules are provided for valuing the shares received by the transferring company in the receiving company for tax purposes. However, in the form which must be filed in order to claim tax exemptions in case of company reorganizations (form IR88), in the section regarding transfer of one or more business sections, the net value of the assets being transferred as per the balance sheet must be reported to the tax authorities and the nominal value of the shares issues in exchange. Consequently, it appears that in practice the shares received in exchange for the assets by the transferring company should be considered to have been received at the nominal/tax book value of the assets transferred and no step up in value is provided for.	Article 26(1) ITL Article 30 ITL

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
9.2 Further conditions for tax relief No.	N/A.

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>9.3 Tax deferral</u> Case law of the ECJ has not had any impact on the Cypriot tax legislation or interpretation thereof (considering that Cypriot tax law generally does not contain exit tax provisions).	N/A.

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Loss recapture for permanent establishments in third Member States</u> Cypriot tax legislation provides for loss recapture with respect to permanent establishments situated outside Cyprus if such permanent establishment starts to generate taxable profits. Such profits derived from a permanent establishment situated outside Cyprus are not exempt from tax and must be included in the taxable income if and in as far as deductions for losses were allowed in previous years. However, there is no explicit provision regarding recapture of losses at once in case a permanent establishment is sold, converted into a company or transferred under a company reorganization in a situation as envisaged in Article 10 of the MD (Cypriot company being the transferring company). This means that in practice there is no tax loss recapture if a PE is transferred in the course of a reorganization. Consequently, no incompatibility issues have been identified with the implementation of Article 10 of the Merger Directive.	Article 36(3) ITL

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> We refer to 10.1 above. There is no loss recapture if a PE is sold, converted into a company or transferred under a company reorganization. In this respect it is irrelevant if the PE is situated in Cyprus or outside Cyprus.	Article 36 ITL

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
10.3 Concept of worldwide taxation/tax credit system Cyprus does not tax unrealized capital gains. Moreover, Cyprus applies an exemption for profits from a permanent establishment situated outside Cyprus provided that certain conditions are met. Therefore Cyprus does not have specific rules or guidelines regarding taxation of profits of a permanent establishment abroad in case of a company reorganization.	Article 36 ITL

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
10.4 Tax deferral Case law of the ECJ has not had any impact on the Cypriot tax legislation or interpretation thereof.	N/A.

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies There are no specific rules or guidelines implementing Article 10a. It may be relevant to note that Cyprus normally does not tax income and capital gains from share investments and thus the relevance of this right for the IRD may also be limited. As mentioned, the only corporate bodies that are considered fiscally transparent from a Cypriot tax perspective are partnerships and trusts. Since these corporate bodies do not fall under the definition of 'companies' they do not qualify for application of the company reorganization relief rules and thus it is unlikely that a situation could occur in which the right granted under Article 10a of the MD could be exercised. One could say that Article 10a has implicitly been implemented through the definition of companies. A disparity may occur if there are cases where a Hungarian '*Közhasnú Társaság*' or a Bulgarian or Romanian body corporate is included in the annex to the Merger Directive but is not considered to be a 'company' which is 'incorporated or registered' based on domestic rules. If such cases indeed exist, the IRD may wish to invoke its right under Article 10a without having the Article implemented.	Article 2 ITL

However, as mentioned above, the relevance of this right for the IRD may be limited since Cyprus normally does not tax income and capital gains from share investments.	

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit As mentioned above there are no specific rules or guidelines implementing Article 10a.	N/A.

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit As mentioned above there are no specific rules or guidelines implementing Article 10a.	N/A.

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders As mentioned above there are no specific rules or guidelines implementing Article 10a.	N/A.

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company As mentioned above there are no specific rules or guidelines implementing Article 10a.	N/A.

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation No. As mentioned above, Cyprus has no rules that govern and ensure the domestic taxation of undisclosed reserves in case of a company ceasing to be a taxpayer in Cyprus except in case of trading stock.	N/A.

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' There are no specific rules or guidelines that define the term 'head office' but it is generally considered to be the place where effective management and control of an entity is exercised.	N/A.

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency Yes.	N/A.

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
10b.4 Assets and liabilities not effectively connected with a permanent establishment Cyprus generally does not have exit taxation provisions (except for revaluation of trading stock) but a transfer of registered office is considered to be a company reorganization qualifying for application of the company reorganization relief rules.	Article 30 ITL

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
10b.5 Tax deferral Case law of the ECJ has not had any impact on the Cypriot tax legislation or interpretation thereof.	N/A.

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 The term 'comparable circumstances' There are no specific rules or guidelines regarding the term 'comparable circumstances'.	N/A.

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Loss recapture for permanent establishments Cypriot tax legislation provides for loss recapture with respect to permanent establishments situated outside Cyprus if such permanent establishment starts to generate taxable profits. Such profits derived from a permanent establishment situated outside Cyprus are not exempt from tax and must be included in the taxable income if and in as far as deductions for losses were allowed in previous years. However, there is no explicit provision regarding recapture of losses in case a permanent establishment is transferred under a company reorganization in a situation as envisaged in Article 10c (Cypriot company being the transferring company). This means that in practice there is no PE loss recapture in such case.	Article 36 ITL

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
10d.1 Deemed liquidation Cypriot tax legislation does not include the concept of deemed liquidation or deemed dividend distributions or deemed distribution of latent capital gains and retained earnings in case the registered office is transferred to another Member State.	N/A.

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
10d.2 Tax treatment of third country residents The country of residence of the shareholders of the SE or SCE is not relevant.	N/A.

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 *'Leur-Bloem'* and C321/05 *'Kofoed'*. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 *'Cadbury'*. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
11.1 Transposition of anti-abuse provisions The company reorganization relief rules do not include a specific anti-abuse provision.	N/A.

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' (*'Kofoed'*, paragraph 46)?	Reference
11.2 General anti-abuse provision Cypriot tax legislation contains two general anti-abuse provisions. The at arm's length principle has been codified in the ITL based on which the IRD can make profit adjustments. In addition, the ACT Law states that if the IRD is of the opinion that in respect of any year of assessment the object	Article 33 ITL Article 33 ACT Law

of tax of any person is reduced by any transaction which in his opinion was artificial or fictitious, he may disregard any such transaction and assess the person concerned on the proper object of tax.	

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' Case law of the ECJ has not had any impact on the Cypriot tax legislation or interpretation of wholly artificial arrangements so far.	N/A.

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions No.	N/A.

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' These concepts have not been interpreted in national legislation. As mentioned above, the Cypriot tax authorities apply the at arm's length principle and the principle of artificial or fictitious transactions. There are no specific rules or guidelines regarding the interpretation in practice of the terms 'artificial' transactions or 'fictitious' transactions.	N/A.

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof As mentioned above the concept of 'valid commercial reasons' has not been implemented in national legislation or practice. In principle the initial burden of proof that transactions are artificial or fictitious should be with the IRD but it is uncertain in which cases the burden of proof could shift from the IRD to the taxpayer.	N/A.

CZECH REPUBLIC

Abbreviations

English	Czech	English	Czech
AoR	ZoR	Act on Reserves	Zákon o rezervách
ATA	ZSDP	Administration of Taxes Act	Zákon o správě daní a poplatků
CoC	ObchZ	Commercial Code	Obchodní zákoník
MS		EU Member State	Jiný členský stát Evropské unie
ITA	ZDP	Income Taxes Act	Zákon o daních z příjmů
SE	SE	European Company	Evropská společnost
SCE	SCE	European Cooperative Society	Evropská družstevní společnost
JSC	AS	Joint-stock company	Akciová společnost
LLC	SRO	Limited liability company	Společnost s ručením omezeným
MFCR	MFČR	Ministry of Finance of the Czech Republic	Ministerstvo financí České republiky

Survey of the Implementation of Council Directive 90/434/EEC

(The Merger Directive, as amended)

CZECH REPUBLIC

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
<u>Overall state of implementation</u> In association with its accession to the European Union with the effectiveness as of 1 May 2004, the Czech Republic transposed the Merger Directive into Czech tax legislation by the Act No. 438/2003 Coll. ('2003 Act'), representing an amendment to the Income Taxes Act No. 586/1992 Coll. With the 2003 Act, the ITA was amended by sections 23a, 23b, 23c, and 23d, under which the tax treatment of transfer of assets, exchange of shares, mergers and divisions was incorporated into Czech legal environment with the effectiveness as of 1 January 2004. ITA was amended by the Act No. 545/2005 Coll. ('2005 Act'), which, included certain further anti-avoidance provisions relating to transfer of assets and set out the application of the sections 23a, 23b, 23c, and 23d also to the transfer of registered office of the SE/SCE. The 2005 Act became effective on 1 January 2006. ITA was further substantially amended by the Act No. 261/2007 Coll. ('2007 Act'), which, by reflecting the Council Directive 2005/19/EC, set out the tax treatment of a partial division and newly extended tax benefits to the European Cooperative Society (these benefits were formerly available to Czech joint-stock companies, limited liability companies and European companies only). The 2007 Act became effective on 1 January 2008. Recently, ITA was also amended by the Act No. 126/2008 ('2008 Act'), which governs the carry-over of provisions, reserves and tax losses created pursuant to foreign law. The 2008 Act became effective on 1 July 2008. The explanatory reports to the 2003, 2005 and 2007 Acts prepared by the Government of the Czech Republic may be possibly regarded as guidance to the wording of the respective said Acts. Without prejudice to the above, the Act No. 513/1991 Coll., the Commercial Code ('CoC'), provided only for mergers and divisions where the companies involved had a registered office in the Czech Republic, with the cross-border mergers and divisions thus having been not legally allowed. As a result, the Merger Directive was implemented only for the purposes of ITA. Availability of cross-border restructuring has been eventually achieved by the Act No. 125/2008 Coll., on Transformation of Companies and Cooperatives, which has become effective as of 1 July 2008. The SE Council Regulation No. 2157/2001 has been implemented into Czech law by the Act No. 627/2004 Coll., on the European Company ('EC Act'), with the effectiveness as of 14 December 2004, as amended by the Act No. 264/2006 Coll. The SCE-Regulation No. 1435/2003 has been implemented into Czech law by the Act No. 307/2006 Coll., on the European Cooperative Society ('SCE Act'), with the effectiveness as of 18 August 2006.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
1.1 Involved companies The definition of involved companies is inconsistent throughout ITA and therefore distinctions must be made between transfer of assets, exchanges of shares and mergers/divisions. 1.1.1 Transfer of assets The tax relief may be generally applied if: (a) both the transferring company and the receiving company are Czech tax residents and have the legal form of AS/SRO/SCE, or (b) the transferring company is a tax resident of another MS and the receiving company is a Czech company and a Czech tax resident and the transferred assets and liabilities are NOT effectively connected with a permanent establishment of the receiving company located outside the territory of the Czech Republic after the respective transfer, or (c) the transferring entity is a Czech tax resident or a tax resident of another MS and the receiving company is a tax resident of another MS and the transferred assets and liabilities are effectively connected with the permanent establishment of the receiving company located within the territory of the Czech Republic after the respective transfer. 1.1.2 Exchange of shares The tax relief may be generally applied if both the acquiring and acquired companies are Czech tax residents or are tax residents of another MS and the shareholder of the acquired company: (a) is a Czech tax resident; (b) is not a Czech tax resident but held a share in the acquired company and holds a share in the acquiring company through a permanent establishment located within the territory of the Czech Republic. 1.1.3 Mergers and divisions The tax relief may be generally applied if: (a) all the companies involved are Czech tax residents and have the legal form of AS/SRO/SCE.	Sec. 23a (6) ITA Sec. 23b (6) ITA Sec. 23c (9) ITA Sec. 23c (5) ITA

(b) dissolving/dividing company is a tax resident of MS and the successor existing company, successor newly established company, successor company being the sole shareholder or successor company in division (jointly referred to as 'successor company') is a Czech tax resident and have the legal form of AS/SRO/SCE, provided that the transferred assets and liabilities are NOT effectively connected with a permanent establishment of the successor company located outside the territory of the Czech Republic after the respective merger/division. (c) successor company is a tax resident of MS and the dissolving/dividing company is a Czech tax resident and have the legal form of AS/SRO/SCE, provided that the transferred assets and liabilities are effectively connected with the permanent establishment of the successor company located within the territory of the Czech Republic after the respective merger/division. The party involved in a merger/division are also considered companies which are tax residents of another MS and the shareholder of the dissolving/dividing company: (a) is a Czech tax resident; (b) is not a Czech tax resident but held a share in the dissolving/dividing company and holds a share in the successor company through a permanent establishment located within the territory of the Czech Republic. As follows from the above, ITA extends the tax relief in exchange of shares also to the shareholder of the acquired company and in merger/division also to the shareholder of the dissolving/dividing company provided the permanent establishment condition is met.	

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
<u>**1.2 Foreign Member State and third state merger**</u> Please see 1.1. The relief is applicable to intra-state restructuring, i.e. if both companies are from the Czech Republic. The benefits of the Merger Directive are not extended to companies from a third State.	Sec. 23a (6) ITA Sec. 23b (6) ITA Sec. 23c (9) ITA

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
<u>**2.1 The term 'securities'**</u> As the securities ('*podíly*') are not, per se, defined in the ITA, reference may be made to CoC. The securities are therein defined as participation of the shareholder in the company and rights and duties arising in association therewith.	Sec. 61(1) CoC

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
<u>**2.2 The term 'cash payments'**</u> The cash payment in the case of exchange of shares is defined as a payment made to former owners of the holding in the acquired company in exchange of the shares in the acquiring company, not exceeding 10% of the nominal value of all shares in the acquiring company or, in the case the nominal value in the acquiring company may not be ascertained, 10% of the book value of all shares in the acquiring company. ITA further also allows cash payments in case of a merger, division or partial division, however, does not provide any further definition. The respective guidance may be derived from CoC, which stipulates that the cash payment may not exceed 10% of the nominal value of the securities that shall be exchanged for the securities of the dissolving company in case of a merger. The same condition is given in case of a division and partial division, yet it is further stipulated that the cash payment may also not exceed 10% of the nominal value of the contributions made to the registered capital of the successor company. As follows from the above, it seems that the cash payment generally applies on an overall basis.	Sec. 23b (2) ITA Sec. 23b (4) ITA Sec. 23b (2) ITA Sec. 220a (5) CoC Sec. 220r (3) CoC

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
<u>2.3 Further types of merger</u> The ITA refers also to merger available under the CoC. However, it seems that at the moment, generally only the types of mergers as listed in the Directive are enabled by ITA.	Sec. 23c (1) ITA

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
<u>2.4 Qualifying exchange of shares</u> The exchange of shares is defined by ITA as an operation whereby the acquiring company obtains a holding in the acquired company representing a majority of the voting rights in the acquired company in exchange for the issue to the shareholders of the acquired company, in exchange of their securities, of securities representing the capital of the shareholders of the acquired company. As follows from the above, the definition of the exchange of shares is analogical with the wording of the Council Directive 90/434/EC, thereby not reflecting the amended version of the Council Directive 2005/19/EC. As a result, if, after obtaining majority holding, the acquiring company further increases its stake in the acquired company, no relief is granted in this respect and, therefore, possible infringement of the Merger Directive occurs.	Sec. 23b (1) ITA

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>2.5 Consolidation of qualifying holding</u> N/A.	

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 *'Andersen og Jensen'*. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
2.6 The term 'branch of activity' The ITA uses the term enterprise (*'podnik'*) for all branches of activity of the company and the term separate part of enterprise (*'samostatna cast podniku'*) for a branch of activity. The definition of 'enterprise' itself may not be found in ITA and, therefore, reference should be made to CoC where it is defined as a set of tangible, as well as personal and intangible components of a business, including objects, rights and other asset values which belong to the entrepreneur and serve for operating an enterprise or which can be possibly used for the purpose of operating an enterprise. Unlike the term enterprise, the branch of activity is already defined by ITA, being an independent organizational and functional unit performing one or more lines of business. Further guidance may be derived from CoC, which defines the term organizational unit of enterprise (*'organizační složka podniku '*), as encompassing: (a) branch office (*'odstepny zavod'*), which is registered as a branch in the Commercial Register. The branch office uses the commercial name of the enterprise, supplemented by an indication that it is a 'branch office' of the enterprise. (b) another organizational unit of the enterprise similar to a branch office provided the law requires that it shall be registered in the Commercial Register. The Case C-43/00 '*Andersen og Jensen*' did not have any substantial impact on Czech legislation or interpretation of the above.	Sec. 23a (1) ITA Sec. 6 CoC Sec. 23a (1) ITA Sec. 7 CoC

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
3.1 Types of entities Under its Czech implementation, the Merger Directive generally applies to all entities listed in the relevant EU legislation, as published in the Financial Gazette of MFCR. In this respect, in 2004, MFCR issued Announcement No. 54/63518/2004-541, published in the Financial Gazette No. 6/2004, ('2004 Announcement') containing all MS companies qualifying for the benefits of the Merger Directive. The 2004 Announcement was in 2005 amended by the Announcement No. 15/119 152/2005-151, published in the Financial Gazette No. 12/2/2005 ('2005 Announcement') and	Sec. 19 (3) a) 1 ITA MFCR Announcement, No. 15/112 988/2006-151, published in the Financial

afterwards substituted by the Announcement No. 15/112 988/2006-151, published in the Financial Gazette No. 3/2007, ('2007 Announcement') extending the tax benefits to qualified companies in Rumania and Bulgaria. The wording of the 2007 Announcement is identical with the Annex to the Directive and therefore all companies listed in the Annex are covered. Relevant provisions implementing the merger directive distinguish between Czech companies and companies established in other EU state. As regards the latter ones, Czech tax law refers to the decree issued by MF, which explicitly covers SE. Thus, SE established in other EU state is covered. On the other hand, SE is not explicitly mentioned in the case of Czech companies (although SCE is explicitly included). Nevertheless, the Czech tax law includes similar provision as included in the Article 10 of the SE regulation stating that SE should be subject to similar tax treatment as joint stock company. As the joint stock company is covered by respective provisions, we believe that SE should practically be covered by Czech tax law irrespective of the place of its establishment, though it is not explicitly covered by the wording of the law.	Gazette No. 3/2007

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>**3.2 Transparent entities**</u> The term 'transparent entity' is not explicitly defined in the Czech tax legislation. However, in 2005, the MFCR issued Guideline D-286 and related Guideline Information, both of which may serve as a yardstick for interpreting the concept of transparent entity and its tax implications in the Czech Republic. According to the Guideline Information, a foreign entity is considered transparent for Czech tax purposes (a) if – on the basis of the tax laws of the country where it is established, incorporated, or to which it has a 'close relation' – it is not regarded as a taxpayer in respect of its income; and (b) if – on the basis of the domestic tax laws of the other state – its income is at least partially attributable to other entities (i.e., to the beneficial owners of such income). Please note that the expression 'close relation' is not further defined or clarified in the MFCR Information on Guideline D-286, or in any other available source issued by the MFCR. As a result, the legal characteristics of a foreign entity in its country of establishment/incorporation are usually not relevant for Czech tax purposes. In practice, the Czech Tax Authorities tend to assess fiscal transparency on the basis of tax comparison. Therefore, provided the foreign legal entity is not subject to income tax or similar taxes and its income is (partially) allocated to other entities, it is likely to be considered fiscally transparent for Czech tax purposes. In this respect, the MFCR explicitly lists the following legal forms as tax transparent entities: partnerships (e.g., limited partnerships, general	Guideline D-286, on taxation of Czech-source income of Czech tax non-residents, Ref. 49/85 663/2005-493, published in the Financial Gazette No. 43/2005 MFCR Information on Guideline D-286, on taxation of Czech-source income of Czech tax non-residents

partnerships, ordinary partnerships), trusts, and the Slovak entity known as 'komanditna spolocnost'. Therefore, although these entities are listed in the Annex to the Merger Directive, they are principally regarded as transparent entities for Czech tax purposes. We have not performed a detailed analysis of all the companies listed in the Annex to the Merger Directive and implementing 2007 Announcement as that would be beyond the scope of our review. However, we cannot rule out that some entities listed therein may be of a transparent nature and, therefore, may be treated as transparent for tax purposes.	

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
<u>**3.3 Qualification of tax residency**</u> <u>3.3.1 Tax residency under domestic law</u> A legal entity is deemed to have unlimited tax liability towards the Czech Republic if its registered office or its place of management are located in the Czech Republic. ITA also stipulates that, in order to qualify for the benefits of the Directive, the company must be considered a tax resident on the basis of the tax law of the relevant MS and must not be considered a tax resident outside EU based on the provision of the Double Tax Convention with a third country. <u>3.3.2 Tax residency under double tax conventions</u> Czech double tax conventions generally provide for the following tiebreaker criterion to determine the tax residency of corporations: '*Where by reason of tax residency on grounds of place of management or any other criterion of a similar nature a person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident only of the State in which its place of effective management is situated.*'	Sec. 17 (3) ITA Sec. 19 (3) (a)(2) ITA

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>**3.4 Subject-to-tax clause**</u> The subject to tax clause has been implemented in the Czech Republic similarly as the concept of tax residents of another EU Member States, i.e., ITA provides that the respective tax must be principally listed in the relevant EU legislation, as published in the Financial Gazette of MFCR. As a result, the respective list of taxes was transposed into Czech legislation by the '2004 Announcement', amended by the '2005 Announcement' and substituted by the '2007 Announcement'. The wording of the 2007	Sec. 19 (3) a3) ITA MFCR Announcement, No. 15/112 988/2006-151, published in the Financial

Announcement is identical with Article 3(c) of the Merger Directive and therefore all taxes are covered (please see 3.1).	Gazette No. 3/2007

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
3.5 Shareholder requirements The ownership of a company by EU or EEA nationals or residents is not relevant for the purposes of ITA.	

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
4.1 The concepts of 'real values' and 'value for tax purposes' The concepts of 'real values' and 'value for tax purposes' have not been transposed to the Czech tax legislation. However, the income derived by the receiving company/acquiring company in connection with revaluation of assets/liabilities at transfer of assets, merger or division/partial division, and of acquired share at exchange of shares shall not give rise to any taxation. There are no specific rules for the transferring company. In any case, as these transactions are accounted through balance sheet (equity) under the Czech accounting legislation, there is no taxable profit/loss to be reported. Moreover, there are no specific provisions in the Czech tax law giving rise to the taxation of the potential capital gains. Taxable basis is derived from accounting profit/loss and transactions not reported in profit and loss generally do not have impact on the taxable basis.	Sec. 23a (3) ITA, Sec. 23c (4) ITA

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions No specific guidance was issued.	

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' 4.3.1. Effectively connected There is no specific definition of 'effectively connected' in Czech legislation. However, it might be reasonably assumed that assets are effectively connected with a permanent establishment if they are used by the permanent establishment to exercise its business activity and to generate taxable profits. No administrative guidance was issued. 4.3.2 Permanent establishment (a) Domestic law Under ITA, the permanent establishment is defined as a place through which a non-resident taxpayer exercises its activity in the Czech Republic, such as workshops, offices, selling centers, mines etc. In addition to the above, the installation site, place of execution of construction and building projects and further services and activities specifically listed by ITA as provided by the non-resident taxpayer, its employees or workers also create a permanent establishment if being present or rendered for more than six months throughout any twelve consecutive months. The services and activities specifically listed by ITA include *inter alia* commercial, technical or other advisory services, management or brokerage activities and similar activities rendered within the territory of the Czech Republic. Also, where a person is acting on behalf of a non-resident taxpayer and habitually exercises an authority to conclude contracts that are binding for such non-resident taxpayer, then such non-resident taxpayer shall be deemed to have a permanent establishment in the Czech Republic in respect of any activities which that person undertakes for the non-resident taxpayer in the Czech Republic. As follows from the above, ITA explicitly stipulates that rendering of selected services may create a permanent establishment and therefore, in its strictness, it goes beyond the OECD Model Tax Convention where no such wording is stated. (b) Double tax conventions Without prejudice to the above, the wording of majority of double tax conventions entered into by the Czech Republic is vastly congruent with that of the OECD Model Tax Conventions.	Sec. 22 (2) ITA Sec. 22 (2) ITA Sec. 22 (1) c ITA Sec. 22 (2) ITA

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief There are no restrictions imposed on relief in respect of prior periods in this respect. With regards to depreciation, ITA stipulates that the receiving/successor company or receiving/successor company by means of its permanent establishment in the Czech Republic carries on with the depreciation started by the transferring/dissolving/dividing company as far as transferred tangible and intangible assets are concerned.	Sec. 23a (4) ITA, Sec. 23c (7) ITA

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment Provided the assets and liabilities are not effectively connected with a permanent establishment of the receiving/successor company located within the territory of the Czech Republic, the transaction does not qualify for the tax relief under the implementing legislation. As a result, standard rules for transfer of assets under ITA would be subsequently applied.	

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company If the transaction qualifies for the tax relief under the implementing legislation, no further restrictions are posed in this respect and, therefore, no profit taxation occurs at the level of the receiving company.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral There have been no specific amendments in respect of the legislation implementing the Merger Directive as the result of Case Law. The tax is deferred until the disposal of the assets by the receiving/successor company if the conditions for the tax relief under ITA are generally met.	

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities Article 4(2) was not implemented in the Czech tax legislation. For general definition of a tax transparent entity as used by MFCR and additional information, please see 3.2.	

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief No specific conditions, apart from the anti-abuse rules.	

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
5.1 The term 'provisions and reserves' Both provisions and reserves are defined by the Act No. 593/1992 Coll., on Reserves, ('AoR'). The reserves are defined as bank reserves, insurance reserves, reserves for repair of tangible assets, reserves for cultural operations and other specific reserves defined by the AoR (e.g. reserve for recovery of land affected by mining).	Section 2 (1) AoR
The provisions are defined as provisions to the balance sheet value of non-time-barred receivables due after 31 December 1994 and accounted for in accordance with applicable Czech accounting legislation. The creation of reserves and provision may be rendered a tax-deductible expense only provided specific conditions laid down by the AoR are met.	Section 7 AoR
The reserve for repair of tangible assets, being the most commonly created reserve, may be rendered tax effective in particular upon fulfilment of the following conditions: (a) the legal entity has ownership title to the tangible assets in respect of which the reserve for repair is created; (b) the repair may not have the character of regular maintenance or technical improvement and may not be carried out as a result of damage or accident;	Section 8a AoR Section 23a (5)

(c) the reserve must be created in at least two taxable periods but, at the same time, its total creation is limited to a fixed number of taxable periods depending on the type of the tangible property; (d) the repair shall start no later than in the taxable period following the taxable period when it was supposed to start. The provisions to receivables may be rendered tax effective in particular upon fulfilment of the following conditions: (a) 20% of the unpaid balance sheet value of the given receivable may be rendered tax effective after six months since the maturity of the same; (b) higher provisions to receivables may be created only if the taxpayer claims these receivables in arbitration proceedings, judicial proceedings or administrative proceedings, subject to a time test since the date of its maturity. With the 2008 Act, the receiving/successor companies may carry over reserves and provisions from the non-resident transferring/dissolving/dividing companies created on the basis of the respective foreign law, provided the latter do not have a permanent establishment within the territory of the Czech Republic. However, such reserves and provisions may be carried over only up to the maximum amount enabled by AoR and the receiving/successor companies may continue creating such reserves and provisions in accordance with AoR solely.	ITA Section 23c (8) ITA

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments Provisions and reserves are carried over to the permanent establishment.	23a (5) ITA, 23c (8) ITA

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves No specific rules or guidance. Economic logic should be applied to each specific case. Generally, provisions (reserves) are allocated to the company that takes over the related assets (risks).	

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves No specific conditions, apart from the anti-abuse rules.	

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry over of losses	
The tax loss is defined for the purposes of ITA as a difference whereby the expenses (adjusted for tax purposes) of a company exceed its revenues (adjusted for tax purposes).	Section 38n (1) ITA
The tax treatment of carry over losses is inconsistent throughout ITA and therefore distinctions must be drawn between transfer of assets and mergers/divisions.	
6.1.1 Transfer of assets	
Under the Czech implementation, the receiving company or the receiving company by means of its permanent establishment located within the territory of the Czech Republic may carry over a tax loss or a part thereof incurred by the transferring company provided the tax loss is associated with the transferred enterprise/branch of activity and has not been yet claimed as an item decreasing the tax base of the transferring company.	Section 23a (5b) ITA
The tax loss may be claimed as an item decreasing the tax base in the five consecutive taxable periods following the taxable period in which the tax loss was incurred.	Section 38na (6) ITA
If the taxpayer is not able to prove which part of the tax loss is associated with the transferred enterprise/branch of activity, the respective part of the tax loss is pro-rated on the basis of the proportion between the book value of the transferred assets less book value of transferred liabilities as accounted for by the transferring company in its accounting books at the time of the transfer, and the total assets less total liabilities of the transferring company as accounted for by the transferring company in its accounting books at the time of the transfer.	
Notwithstanding the above, the tax loss or a part thereof incurred by the transferring company may be deducted from the tax base of the receiving company in the individual periods at most up to the proportionate tax base of the receiving company attributable to such activity exercised by the transferred enterprise/branch of activity that was exercised by the enterprise/branch of activity in the period when such tax loss was incurred. Such tax base of the receiving company shall be established on the basis of the proportion between the booked revenues derived from goods sold and services performed attributable to the same activities exercised by the transferring company in the period when such tax loss	Section 23c (8b) ITA Section 38na (6) ITA

was incurred, and the booked total revenues derived from the goods sold and services performed. This is applicable also in the case of a permanent establishment of the receiving company situated in the Czech Republic. <u>6.1.2. Mergers/divisions/partial divisions</u> The successor company or the successor company in case of a division by means of its permanent establishment located within the territory of the Czech Republic may carry over a tax loss incurred by the dissolving/dividing company provided the tax loss has not been yet claimed as an item decreasing the tax base of the dissolving/dividing company. The tax loss may be claimed as an item decreasing the tax base in the five consecutive taxable periods following the taxable period in which the tax loss was incurred. Without prejudice to the above, only such part of the tax loss may be taken over by the successor company from the dissolving/dividing company that may be justified by an economic criterion to be determined in the manner as follows. If a taxpayer which incurred a tax loss is dissolved during a reorganization and the tax loss is taken over by a successor company, the successor company may deduct the carried-over tax loss from its tax base at most up to such proportionate part of the tax base attributable to the same activities exercised by the dissolving entity in the period when such tax loss was incurred. In case of a division with the dividing company not being dissolved, the successor company may deduct the carried-over tax loss from its tax base at most up to such proportionate part of the tax base attributable to the same activities exercised by the dividing entity in the period when such tax loss was incurred. Such pro-rated tax base of the successor company shall be established on the basis of the proportion between the booked revenues derived from goods sold and services performed attributable to the same activities exercised by the dissolving/dividing company in the period when such tax loss was incurred, and the booked total revenues derived from the goods sold and services performed. This is applicable also in the case of a permanent establishment of the receiving company situated in the Czech Republic. With the 2008 Act, the receiving/successor companies may carry over unexpired tax losses from the non-resident transferring/dissolving/dividing companies created on the basis of the respective foreign law, provided the latter do not have a permanent establishment within the territory of the Czech Republic. However, such unexpired tax losses may be carried over only up to the maximum amount enabled by ITA in case of a resident taxpayer.	Section 23a (5) ITA Section 23c (8) ITA

What method is applied to allocate losses to the permanent establishment?	Reference
<u>6.2 Allocation of losses to the permanent establishment</u> No specific guidance is given by ITA in respect of allocation of losses to the permanent establishment. Economic logic needs to be followed.	

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
<u>6.3 Specific legislation for divisions/partial divisions/transfer of assets</u> Please see 6.1.	

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
<u>6.4 Further conditions for carry over of losses</u> No other specific conditions, apart from the anti-abuse rules.	

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
<u>7.1 Amended holding threshold</u> Article 7 has not been implemented in the Czech tax law. The capital gain is not taxed because the merger is a balance sheet transaction.	

Article 7(1) covers <u>gains</u> accruing on the cancellation of a holding. It does not cover <u>losses</u> that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
<u>7.2 Treatment of losses</u> Article 7 has not been implemented in the Czech tax law. The capital loss is not tax deductible because the merger is a balance sheet transaction.	

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder (a) Exchanges of shares Upon an exchange of shares, the shares received by the acquiring company in the acquired company are for tax purposes attributed their fair market value. (b) Mergers Upon a merger, the newly received shares are treated as having the same tax basis as the shares previously held. The allotment of securities to the shareholders is not treated as an income or profit of that shareholder (with regard to other tax and accounting law provisions). (c) Division or Partial Division Upon a division or partial division, the tax basis of the shares held is divided into the tax basis of the newly received shares on the basis of economically justifiable criterion.The allotment of securities to the shareholders is not treated as an income or profit of that shareholder (with regard to other tax and accounting law provisions). As no income or profit arises with the above transactions, the avoidance of economic double taxation at the level of the shareholder should be irrelevant for Czech tax purposes.	Sec. 23b (5) ITA Sec. 23c (6) ITA Sec. 23c (4) ITA Sec. 23c (6) ITA Sec. 23c (4) ITA

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
8.2 Computation of the capital gain The cash payment is not exempted from taxation under the provisions implementing the Directive and is subject to corporate income tax in case the recipient entity is a Czech tax resident. If the cash payment is paid to a non-Czech entity, standard methods for elimination of double taxation should apply. No specific guidance has been issues in respect of its taxation.	

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>8.3 Further conditions for tax relief</u> There are no further conditions stipulated in the relevant provision. Anti-avoidance provision applies (please see 11.1).	

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>9.1 Avoidance of economic double taxation at the level of the transferring company</u> Yes, the shares received by the transferring company are considered to be received at fair market value of the assets transferred.	Sec. 23a (2) ITA

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>9.2 Further conditions for tax relief</u> There are no further conditions stipulated in the relevant provision. Anti-avoidance provision applies (please see 11.1).	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>9.3 Tax deferral</u> There is no direct response to the judgment.	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Loss recapture for permanent establishments in third Member States</u> The loss recapture is not implemented in the Czech tax legislation.	

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> There are no specific rules in relation to the transfer of permanent establishment. However, under general rules the provisions implementing the Directive are to apply as long as the assets transferred (i) are not connected with a permanent establishment situated outside the Czech Republic after the transfer if the successor company is Czech tax resident or (ii) are connected with a permanent establishment situated in the Czech Republic after the transfer if the successor company is Czech tax non-resident. Therefore, strictly gramatically the situation described in final sentence of Article 10(1) is not covered by a specific provision of the Czech tax law.	

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> There are no specific rules in relation to the transfer of permanent establishment. Generally, the credit method is used in the majority of double tax treaties in order to eliminate double taxation on the conditions that the tax has been paid (unless the respective double tax treaty stipulates otherwise).	

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
10.4 Tax deferral There is no direct response to the judgment.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies Article 10a has not been implemented in the Czech tax law. Generally, the Merger Directive applies to entities listed in its Annex, i.e., even to Slovak limited partnership (for more information please see 3.2)	

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit Article 10a has not been implemented in the Czech tax law. General provisions should apply only for companies listed in the Annex to the Merger Directive.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit Article 10a has not been implemented in the Czech tax law. The notional credit should be applicable only for the companies listed in the Annex to the Merger Directive.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders Article 10a of the MD has not been implemented in the Czech tax law. General provisions should apply only for companies listed in the Annex to the Merger Directive.	

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company Article 10a of the MD has not been implemented in the Czech tax law. General provisions should apply only for companies listed in the Annex to the Merger Directive.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation There are no specific provisions giving rise to exit taxation.	

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' There is no definition of the term 'head office' in relation to implementation of Article 10b.	

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency As the tax law speaks about 'registered office' in connection with the implementation of Article 10b, it is not likely that the criteria used to determine tax residence would be applied. However, the place of 'effective management' should be observed in case of transfer of the registered office into/from the Czech Republic in order to avoid application of anti-avoidance rules.	Sec. 17 (3) ITA

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
10b.4 Assets and liabilities not effectively connected with a permanent establishment Transfer of registered office does not constitute taxation of assets effectively connected with the permanent establishment. In case of assets not effectively connected with permanent establishment, the relevant double tax treaty regarding the income arising from these assets should be used (please see 4.5, 4.7).	37b ITA

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
10b.5 Tax deferral There is no direct response to the judgment.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 The term 'comparable circumstances' There is no definition of the term available in the Czech tax law or administrative guidelines.	

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
<u>10c.2 Loss recapture for permanent establishments</u> There are no specific rules in the Czech tax law.	

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>10d.1 Deemed liquidation</u> There are no specific rules in the Czech tax law. Standard rules apply to taxation of income or gains of non-resident taxpayers. As a result, the non-resident shareholder would not be subject to Czech tax if the income is not Czech-sourced or is protected by a double tax treaty.	

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>10d.2 Tax treatment of third country residents</u> This is not clear from the implementation of the Directive. However, it seems that shareholders from the third countries might be covered by the respective provisions if the general conditions are fulfilled. Standard rules apply to taxation of income or gains of non-resident taxpayers. As a result, the non-resident shareholder would not be subject to Czech tax if the income is not Czech-sourced or is protected by a double tax treaty.	

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 *'Leur-Bloem'* and C321/05 *'Kofoed'*. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 *'Cadbury'*. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> The Article has been transposed into the Czech tax law as Section 23d of the ITA. When the main reason or one of the main reasons for the transfer of assets, exchange of shares or merger or division is tax avoidance or tax evasion, in particular when it is obvious that there are no proper economic reasons such as restructuring or rationalization of the activities of the companies involved, the following benefits can be denied: (a) step-up in the basis of the acquired share upon the transfer of assets; (b) step-up in the basis of the acquired share upon the exchange of shares; (c) possibility to take over tax losses or tax allowances upon the transfer of assets, merger or division. If the receiving company in the transfer of assets or one of the companies involved in the merger or division does not carry out any activity for more than 12 months preceding the decisive day of the merger or division or the day when assets are transferred, it is deemed that no proper economic reasons exist, unless one of the concerned taxpayers proves otherwise. Furthermore, should the transferring /acquiring company sell its share in the receiving/acquired company, which was acquired upon the transfer of assets/exchange of shares, within one year from the transfer of assets/exchange of shares, any step-up in the basis of the acquired share is denied retroactively. The above provisions apply equally to Czech resident taxpayers, as well as to Czech non-resident taxpayers.	Sec. 23d (2-6) ITA

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' (*'Kofoed'*, paragraph 46)?	Reference
<u>11.2 General anti-abuse provision</u> This is not applicable since the Article has been transposed into the Czech tax law.	

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
<u>11.3 The concept of 'wholly artificial arrangement'</u> There is no direct response to the '*Cadbury*' judgment.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
<u>11.4 Specific anti-abuse provisions</u> The restrictions mentioned in answer 11.1 above were imposed. There are no other relating specific requirements.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
<u>11.5 The concept of 'valid commercial reasons'</u> There is no specific guidance in relation to the interpretation of these terms (please see 11.1). The term 'valid economic reasons' should be interpreted similarly to 'proper economic reasons'.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
<u>11.6 Burden of proof</u> Under the Czech tax law, the burden of proof generally lies with the taxpayer.	Sec. 31 (9) ATA

DENMARK

Abbreviations

English	Danish	English	Danish
FUL	FUL	The Merger Tax Act.	Fusionsskatteloven
SEL	SEL	The (Danish) Corporation Tax Act.	Selskabsskatteloven
ABL	ABL	the Capital Gains Tax Act	Aktieavancebeskatningsloven
LL	LL	Danish Tax Assessment Act	Ligningsloven
LV	LV	The Tax Authorities Guidelines	Ligningsvejledningen

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.

Overall state of implementation

The Danish Merger Tax Act dates back to 1975 were the Danish parliament passed the bill regarding a tax regime on mergers between Danish companies.

In 1981 a regime for tax exempt share exchange was inserted in the Danish Capital Gains Tax Act Section 13.

The Danish Merger Tax Act contains the rules on tax exempt merger, division and transfer of assets. The Danish Capital Gains Tax Act contains the rules tax exempt on share exchange. Both the Merger Tax Act and the Capital Gains Tax Act has been amended multiple times. One of the main reasons for the amendments in the recent years has been the impact of the EU legislation.

Below we present the main amendments to the Danish Merger Tax Act and Capital Gains Tax Act:

(a) In 1992 (by Act No 219 of 3 April 1992) the Merger Directive (90/434/EC) was implemented in Danish tax legislation. The implementation was made by way of incorporating the Merger Directive in the original Merger Tax Act from 1975 and the Capital Gains Tax Act. The Merger Tax Act was extended to contain provisions on cross border merger, domestic and cross border full divisions and domestic and cross border transfer of assets. Also, the Capital Gains Tax Act was furthermore, as a consequence of the implementation of the Merger Directive the terminology in the Merger Tax Act was amended.

(b) In 1996 (by act No 487 of 12 June 1996) the definition of division was extended to cover domestic and cross border partial division.

(c) In 2002 (by act No 313 of 21 May 2002) the restriction on cash payments to 10% of the nominal value was abolished for merger, full and partial division and share exchange.

(d) In 2005 (by act No 1182 of 12 December 2005) the Merger Directive (2005/19/EC) was implemented in Danish tax legislation. The EU Directive resulted in more entities that could benefit from the rules.

(e) In 2007 (by act No 576 of 6 June 2007) the EU Directive 2005/56/EC was implemented in Danish tax legislation.

As to the definition of the restructure options (mergers/division/partial divisions/transfer of assets/exchange of shares), Danish tax law follows the legal terms, which means that in order to qualify under the directive the transaction must be carried out as a (merger/division/partial divisions/transfer of assets) under corporate law.

Alternative rules for domestic restructurings

In 2007 (by way of act no 343 of 18 April 2007) new alternative rules on mergers/full division/partial divisions/transfer of assets/exchange of shares were introduced. Treatment under these rules does not require permission from the tax authorities. However, the new

alternative rules are not an alternative implementation of the Merger Directive as the rules comprise restrictions on cross-border transactions, restrictions to the principle of succession and distributions of dividends. The new alternative rules cannot be seen as an implementation of the Directive, and we have not addressed the new rules unless specifically mentioned. The new alternative rules did not amend the existing implementation of the EU Merger Directive.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
1.1 Involved companies The expression 'in which companies from two or more Member States are involved' has been interpreted as comprising only the merging companies and not the parent companies.	FUL § 15

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
1.2 Foreign Member State and third state merger The benefits of the Merger Directive apply to a merger between companies from one or more EU Member States only. If a company from a third country is involved as either the transferring or receiving company, all benefits from the merger directive does not apply. However, according to Danish tax legislation the shareholder will succeed in the acquisition cost and time of the shares in the receiving company.	FUL § 15, stk. 3 and 6

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term 'securities' In relation to a merger, transfer of assets and divisions, the term 'securities' refers to shares in the respective companies i.e. as comprising shares in the registered equity.	FUL §§ 2, 15, 15a and 15c

2.1.1 Merger/transfer of assets/divisions In the case of a merger or a division, the FUL refers to shares of the receiving company which can be either new shares or existing shares of the receiving company. According to FUL, no shares need to be issued in the case of a 100% merger between a parent company and its subsidiary when the parent company is the receiving company. According to tax practice, no shares need to be issued in the case of a 100% merger between a parent company and its subsidiary when the subsidiary is the receiving company. 2.1.2 Exchange of shares In the case of a share exchange, the term 'securities' seems to be wider. The legislation only states that shares can be exchanged for shares. However, it is defined in this specific legislation that – unless otherwise decided – the legislation also applies to other securities, e.g. convertible bonds. However, in the administrative guidelines it is mentioned that convertible bonds may not be exchanged for other convertible bonds. This issue has been debated in published literature. No court rulings exist.	ABL §§ 1 and 36

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' As from 2002 there are no limits as to the maximum cash payment in the case of a merger, division/partial division and exchange of shares. The only requirement is that at least one share must be issued to/received by at least one shareholder. Also it is not a requirement that the cash payment is distributed on a per-shareholder basis, and shareholders may therefore be bought out. The value of the share and cash payment must correspond to the fair market value of the shares held in the transferring company. Of course no cash payments are allowed under the rules on transfer of asset. However, under Danish tax practice subsequent dividend distributions from the receiving company to the contributing company have been deemed a prohibited 'cash payments' in terms of the transfer of assets. The effect of the Danish tax practice is that the tax payer could not benefit from the Merger Directive as this has been considered a violation of the conditions for carrying out the transfer of assets. Despite the *'Kofoed'-case* it is still uncertain to what extent Danish tax authorities can/will qualify subsequent dividend distributions as prohibited 'cash payments' under the rules on transfer of assets.	FUL § 2, § 15a and 15c ABL § 36

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger For mergers between the Danish and foreign companies which are listed in the Annex to the EU Merger Directive, no other types of merger are possible. According to Danish tax practice, only mergers that are recognized from a legal perspective are recognized from tax practice. According to Danish legislation, a merger between other business entities not covered by the Merger Directive is also possible: cooperatives, savings banks, foundations, mutual insurance associations, cooperative savings banks, investment funds and electricity companies. The merger transaction of these latter entities is generally the same as the ones applying to the companies covered by the Annex to the EU Merger Directive.	FUL § 1, stk. 3 FUL §§12-14k

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares The Danish legislation implemented which grants relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target. However, to the extent that permission to carry out an exchange of shares is required, such permission should also be obtained for the successive exchange of shares. According to Danish tax law, it is required that all shares in connection with each exchange of shares are exchanged within a period of 6 months after the first share was exchanged (dispensation for the deadline is possible). Furthermore, according to firm tax practice it is a requirement that the exchange be carried out within 6 months after the permission (if required/desired) has been obtained. The two 6-month requirements are specific tax law requirements which do not follow from the Merger Directive. In our opinion these requirements may be considered a violation of to the Merger Directive.	ABL § 36, stk. 2 ABL § 36, stk. 4 LV S.G.18.5.3

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>2.5 Consolidation of qualifying holding</u> No. Neither any time nor ownership percentage conditions apply. However, according to Danish tax practice it is normally a requirement that any ownership changes in respect of the receiving company is reported to the tax authorities within a period of 3 years. In the guidelines issued by the tax authorities the following transactions are mentioned as transactions that should be reported to the tax authorities: (a) agreements on sale of shares in the subsidiary including call or put-options ; (b) changes in the ownership or capital of the subsidiary including issuance of shares to employees; (c) changes in share classes (establishment of share classes or dissolve share classes) in the subsidiary; (d) other tax exempt restructurings as mentioned in the Merger Directive (merger, division and transfer of assets); (e) sale of the received shares in the holding company to the holding company (sale back arrangement); (f) entering into or abolishment shareholder agreements; (g) dividend distributions exceeding the annual result; (h) sale of specific or all assets from the subsidiary. It is specifically mentioned that the list of transaction that are to be reported to the tax authorities are not exhaustive. The reason for the reporting requirement is that the tax authorities may re-examine the approval for tax exempt exchange of shares e.g. whether the factual information that the approval for tax exempt exchange of shares was based upon was indeed correct. On the basis of the new information the tax authorities may withdraw the approval for tax exempt exchange of shares if the new information leads to the conclusion that one of the main objects of the *original* approval was tax evasion.	ABL § 36

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 *'Andersen og Jensen'*. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
2.6 The term 'branch of activity' The definition of a 'branch of activity' in the Danish legislation implementing Article 2(i) is worded exactly as the definition in EU Directive. The tax authorities will - on the basis of the information provided by the tax payer - evaluate whether the contributed activity constitutes a branch of activity. 2.6.1 Guidelines The Danish tax authorities' guidelines interpret a 'branch of activity' as follows: 'A specific evaluation must determine whether a business may be considered having several 'branches' of activity or not. If a business may be considered having several 'branches' of activity, a specific evaluation must also determine whether the specified assets and liabilities may be considered belonging to one or the other 'branch' of activity. A specific evaluation must also determine whether what is being transferred meets the requirements of being a business or 'branch' of activity. According to the circumstances, a branch of a business or a cross-company department of a business will be able to meet the requirements of constituting a 'branch' of activity. A transfer of assets must include all assets and liabilities of the enterprise or all assets and liabilities of the 'branch' of activity being transferred. As a main rule, the rules on transfer of assets are therefore not applicable when transferring individual assets and/or liabilities. However, the rules on transfer of assets are applicable when transferring rental property and related mortgage debt, if the property as such meets the requirements of constituting a 'branch' of activity. So as a main rule, the rules on transfer of assets cannot be applied either if some of the assets and/or liabilities of the business or 'branch' of activity are kept in the contributing company after a transfer of a business or 'branch' of activity. Nor are the rules on transfer of assets applicable if loans subject to particular risk form part of the transferred assets of the business or 'branch' of activity have been kept in the contributing company while the other assets and liabilities have been transferred to another company. Besides its main activities, a contributing company may sometimes carry on sideline activities, which do not have anything (directly) to do with the main activities. A company may — e.g. besides the assets and liabilities linked to the business that it carries on — have real property, a sailboat, etc. used by the principal shareholder/managing director. In such a case the company will be able to segregate the assets and liabilities linked to its business and keep the real property, sailboat, etc. in the contributing company. A company may also have funds invested in financial assets and liquid assets, which are not required in order for the company to operate on own means. If so the company would be able to segregate the assets and liabilities linked to its business and keep the	FUL § 15c, stk. 2

financial assets in the contributing company. On the other hand though, the financial assets may only – as an exception – be considered constituting an independent 'branch' of activity. As mentioned, a transfer of assets must include all assets and liabilities of the business or 'branch' of activity being transferred. Transfer of a (branch of) activity to which goodwill or other intangible assets are linked must therefore also include the intangible assets linked to the (branch of) activity.' <u>2.6.2 Real property</u> Special rules apply to real property. A real property may thus be considered a branch of activity in itself. This applies to both rental property, but also to property that has been used in the company's business. Also, when deciding which assets to allocate to branch of activity, the company is free to decide whether real property connected to the branch of activity should be transferred or whether the real property may be kept in the transferring company (This is different compared to other assets which are to be transferred if they are connected to the branch of activity). <u>2.6.3 Shares</u> According to Danish tax practice shares held by the transferring company cannot in itself be considered a branch of activity. However, the shares should be transferred if they are connected to an activity which meets the requirements for being a branch of activity. In this case the shares are not seen as a branch of activity but are merely connected the said branch of activity. In a case published in SKM 2000.238LR the tax assessment council ruled that the shares in three subsidiaries should be transferred to the receiving company as the subsidiaries performed activities which were connected to the transferred activity. However, in the same case the assessment council also ruled that other shares in several holding companies neither should nor could be transferred as the holding companies were not connected to the branch of activity. <u>2.6.4 Partnership interests</u> According to the tax authorities guidelines the same tax practice as for shares applies to partnership interests. However, practice seems stricter for partnership interests and stricter than justified under the Directive. <u>2.6.5 'capable of functioning by its own means'</u> As all assets and liabilities connected to the branch of activity should be transferred, this means that also loan proceeds and debt must be transferred if it is connected to the branch activity. However, according to tax practice the crucial point is whether the transferred assets and liabilities constitute a business being capable of functioning by it own means.	

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> <u>3.1.1 Merger/transfer of assets/division/partial division</u> In relation to cross-border mergers, transfer of assets and divisions, the Merger Directive is decisive and only the entities listed in the Annex can therefore carry out such cross-border restructurings. A direct reference to the Annex in the Merger Directive is inserted in the relevant Danish law. Furthermore, Danish tax law also allows other Danish entities to merge according to the same rules as the ones implemented from the Merger Directive (please see 2.3 above). Further, the succession principle also applies to mergers in third countries, i.e. the Danish shareholders are seen as having acquired the shares in the foreign receiving company at the original acquisition cost and time(please see 1.2 above). <u>3.1.2 Exchange of shares</u> The definition of entities, which may be the receiving company in an exchange of shares, is wider as – besides the companies which are mentioned in the Annex to the Merger Directive – also foreign companies 'similar' to Danish public limited companies ('*aktieselskaber*') and private limited companies ('*anpartsselskaber*') may be the receiving company. Other companies cannot benefit from the rules, cf. Danish tax practice. In SKM 2005.463 reference is made to a case where exchange of holdings in a cooperative was denied, as the cooperative was not a company in the sense of Article 3 of the Merger Directive.	FUL §§ 15, 15a and 15c ABL § 36, stk. 1 and ABL § 36A, stk. 1

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>3.2 Transparent entities</u> According to Danish tax practice, none of the entities in the Annex are considered transparent, as in general the entities are comprised by the EU corporate law directives 68/151/EEC etc. However, not all entities listed in the Annex have been tested in Danish tax practice, especially with respect to new Member States. Denmark has introduced anti-avoidance rules regarding tax legislation in foreign countries (US in particular) that deems some Danish companies as being transparent for tax purposes. The Danish tax legislation imply that the Danish company is also - from a Danish tax perspective - considered a transparent entity which may not benefit from the EU Merger	SEL § 2A

Directive. See also our comments regarding Article 10a (please see10a.1).	

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
<u>3.3 Qualification of tax residency</u> Generally, Denmark applies the registration principle. Furthermore, foreign companies having their daily management in Denmark are deemed as having their tax residency in Denmark. The definition in most of the DTC' concluded by Denmark includes a reference to the effective place of management in case of dual residency. From a Danish tax perspective the concepts of 'effective place of management' under the treaties and 'daily management' under domestic law will probably often coincide, however, at least from a theoretically point of view there may be situations where the two concepts differ. No Danish tax practice exists where the two concepts does not coincide. See also 10b.3.	SEL § 1

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>3.4 Subject-to-tax clause</u> The subject-to-tax clause is only indirectly implemented in Danish tax legislation. In the case of a cross-border merger, division, etc. it follows from the Danish legislation that the conditions in Article 3 of the Merger Directive should be fulfilled. Consequently, this reference includes a reference to the subject-to-tax clause. No administrative guidelines have been issued, and the issue does not seem to have been dealt with in published tax practice. According to Danish tax practice, tonnage tax based on the Net Tonnage (NT) of vessels will qualify as this is indeed taxed with the corporate income tax rate (but the taxable income is assessed according to special rules) whereas cooperatives paying tax on the net wealth and not on an assessment of the income will not qualify. The disqualification of cooperatives may be argued as not being in line with the EU Merger Directive.	FUL § 15, stk. 2-4, § 15a, stk. 1 and § 15c, stk. 1

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>3.5 Shareholder requirements</u> No. The Merger Directive is applicable for companies in the EU (if listed in the Annex to the Merger Directive and not being transparent) regardless of the residence of the shareholders.	FUL §§ 15, 15a and 15c

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>4.1 The concepts of 'real values' and 'value for tax purposes'</u> The concepts of 'real values' and 'value for tax purposes' have not been transposed into Danish tax legislation. A Danish merger, division and partial division applies the succession principle meaning that no capital gains taxes are triggered due to the real value being higher than the value for tax purposes. Instead the receiving company takes over the tax value of the received assets/liabilities (i.e. the acquisition cost at time that the transferring company paid for the assets). Due to the succession principle the real value is relevant only in the case of transfer of assets, as the tax basis of the shares received is calculated on the basis of the real value. However, to the extent that two companies are merged and there is a debt between the companies, the debt is considered realized. A gain on the debt may be subject to taxation under certain circumstances, cf. Danish tax practice (TfS 1990.274 LSR). This is an exception to the general rule that no capital gains taxes are triggered due to the merger. The same exception applies to division and partial division. According to the Merger Directive Article 4 a merger, transfer of assets and division shall not give rise to any taxation of capital gains calculated by reference to the difference between the real values of the assets and liabilities transferred and their values for tax purposes. It is therefore doubtful whether the taxation of debt is in accordance with the Merger Directive.	FUL § 15d

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions The valuation of assets in case of a division and partial division follows the same rules as for a merger (please see 4.1). It is required that the transferred assets in a partial division forms a branch of activity. It is not required that any of the assets transferred in a full division should form a branch of activity.	

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' Both the term 'effectively connected' and 'permanent establishment' are referred to in the Danish law on merger, division and partial division. To the extent that a Danish company is merged with a foreign company (receiving company) and some of the Danish company's assets are allocated ('knyttet') to a Danish permanent establishment of the foreign company, no taxes are triggered on gains of those assets. The Danish permanent establishment succeeds in the tax values. The same applies to a division and partial division where assets transferred are allocated ('knyttet') to a Danish permanent establishment. According to Danish tax practice, a permanent establishment is interpreted in the same way as the OECD Double Taxation Treaty Article 5, and the OECD commentaries to this Article. No guidelines have been issued on the interpretation of 'effectively connected'. In the preparatory documents the following was mentioned: '*The provisions of section 8 on succession of the contributing company's acquisition sums and depreciation/amortization made, etc. cannot apply to all the assets and liabilities of a foreign contributing company. The provisions cannot apply to assets and liabilities becoming non-taxable according to Danish tax law as a result of a merger. Furthermore, the provisions can only apply to assets and liabilities where there is a Danish tax value in which a succession can be made. Consequently, the provisions can apply if the foreign contributing company has assets and liabilities, etc. linked to the permanent establishment in Denmark. The provisions may also apply if the foreign contributing company is a subsidiary of the receiving Danish company and the foreign contributing company was jointly taxed with the receiving Danish company when the most recent ordinary tax assessment prior to the merger was made. As far as the assets and liabilities of the foreign contributing company abroad are concerned, e.g. in the head office or in a permanent establishment in another state, succession may take place according to the tax rules of these countries if*	FUL § 15, stk. 4 (merger) FUL § 15b, stk. 2 (division and partial division)

tax is levied in the state where the head office or the permanent establishment is domiciled. However, in the Merger Directive as such, no position has been taken as to the basis of depreciation/amortization, capital gains or losses when imposing tax in the Member State of the receiving company. '	

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
<u>4.4 Limitation of the scope of relief</u> No limitation on the scope of relief applies. However, in case of a division and transfer of assets to an existing company and to the exchange of shares, all restructures, etc. must be notified to the tax authorities beforehand. The authorities will decide whether the restructure, etc. can be justified by commercial reasons. If this is not the case the original exchange of shares etc. may become taxable. This issue has been dealt with in an extensive tax practice. Please note that to the extent that the Danish company has deducted tax losses from a foreign permanent establishment or jointly taxed company, a restructuring (i.e. merger, division and other) may trigger taxation of the recapture balance (i.e. the previously deducted tax losses). It has been argued in literature that the recapture rules are in themselves contrary to EU Treaty, cf. the Marks and Spencer case. However, Danish administrative tax practice has denied this view without submission of the question to ECJ.	LV S.D.2 LV S.D.3 S.G.18

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
<u>**4.5 Assets and liabilities not effectively connected with a permanent establishment**</u> If a Danish company merges with a foreign company where the foreign company is the receiving company the assets which are effectively connected to a Danish permanent establishment are considered acquired by the permanent establishment at the original cost and time (succession principle). Assets which are not effectively connected to a Danish permanent establishment are considered sold at the market value at the time of the transaction, and any taxable gains on the assets will trigger Danish taxes.	FUL § 15

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company Generally, the succession principles apply to all shareholders. However, to the extent that the receiving company owns shares in the transferring company, no shares need to be issued and hence the succession principle does not apply. A gain/loss on the shares is not taxable.	FUL § 2, stk. 2 and § 10, stk. 1

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral As a consequence of 'Lasteyrie de Saillant' Danish tax law was amended and does not - in relation to exit taxation for individuals - require the tax payer to provide the tax authorities with security (bank guarantee etc.) for the deferred taxes. No specific measures in respect of the Merger Directive has been taken.	

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities It is defined in the tax legislation that relief is not granted to transparent entities, cf. Article 10a (1), but a notional credit is granted according to Article 10a (2) of the Merger Directive. The term transparent entity has not been defined in law. In the preparatory documents regarding the Merger Tax Act it is mentioned that a Danish limited partnership ('*kommanditselskaber*') and a Danish limited partnership ('*interessentskab*') are considered transparent entities. However, no general definition is presented. It is possible that a foreign entity will be compared to the aforementioned Danish partnerships when determining whether the foreign entity is transparent or not. It is mentioned that one of the characteristics of Danish partnerships are that the partners are seen as owners of a proportionate part of the assets and liabilities of the transparent entity. And that the partners resume liability. Furthermore, if the partnerships is transparent under local law it is more likely to be transparent under Danish tax law. No administrative guidelines regarding the concept of transparent entities in the merger tax act have been issued. From published tax practice we can refer to a ruling from 2006 where the 'shareholders' of a Danish partnership ('*kommanditselskab*') wanted to	FUL §§ 15, 15a and 15c LL § 33, stk. 4

exchange their 'shares' in the partnership with shares in a limited liability company by way of a tax-exempt exchange of shares. The tax authorities denied permission to the exchange with reference to the partnership being considered a transparent entity from a Danish tax perspective. The tax authorities did not stipulate on what basis the partnership was considered a transparent entity.	

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
<u>4.9 Further conditions for tax relief</u> No further conditions apply.	

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>5.1 The term 'provisions and reserves'</u> Provisions and reserves are not defined in the tax legislation re. mergers, but Danish tax law allows for carry-over (deferral) of provision and reserves.	FUL § 8, stk. 1, § 15b, stk. 2 and § 15d

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
<u>5.2 Exclusion of 'provisions and reserves' from permanent establishments</u> Danish tax law comprises no exceptions as to provisions and reserves to permanent establishments abroad in respect of mergers between two Danish companies. However, if a transferring Danish company merges with a foreign receiving company the carry-over of provisions and reserves requires that the provisions and reserves can be allocated to a Danish permanent establishment of the receiving. Similar rules apply to divisions and transfer of assets.	FUL § 8, stk. 1, FUL § 15b, stk. 2 and § 15d

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves The provision and reserves should relate to the assets transferred. If the provisions and reserves do not relate to specific assets, no guidelines exist. In these cases we would recommend that the allocation is clarified with the tax authorities beforehand. Clarification may be obtained through either a request for binding ruling or through the approval procedure.	FUL § 8, stk. 1, FUL § 15b, stk. 2 and § 15d

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves No further conditions exist, but as no guidelines are available, the treatment of provisions and reserves is unclear. Please note that Danish tax law generally does not allow for tax deduction of provisions and reserves.	

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry-over of losses Generally, losses in the transferring company cannot be carried over by the receiving company in a domestic merger, and therefore no carry-over loss rule must be extended to cross-border mergers under the Merger Directive. Further, a merger will also lead to the forfeiture of existing tax losses by the receiving company. Therefore - with the exceptions mentioned below - tax losses in both the transferring and receiving company are lost due to the merger. However, to the extent that the merging companies are jointly taxed, tax losses may be carried over to the receiving company provided that the losses were incurred at a time when the companies were jointly taxed. In principal this rule is also applicable for a cross-border merger, however, it is unclear how it would be interpreted in practice, and there is a risk that the result will be discriminatory towards foreign companies, as they are generally not jointly taxed with Danish companies (at least following the recent changes of Danish joint taxation rules after which international joint taxation is generally not elected by Danish companies). The rules may therefore be contrary to EU Treaty and potentially the Merger Directive depending on the administration of the rule. The rules described above also apply to divisions and transfer of assets. It is mentioned though that in a domestic partial division the tax losses are	FUL § 8, stk. 6-7 and FUL § 7 FUL § 15b and FUL § 15d

not lost, cf. the tax authorities' guidelines. This should also apply to a cross-border partial division. Tax losses may also be restricted under the exchange of control rules which are applicable to exchange of shares also. However, in general exchange of controls rules does not prohibit companies carrying forward losses to be offset against active income, but restricts only losses to be offset against passive income.	

What method is applied to allocate losses to the permanent establishment?	Reference
<u>6.2 Allocation of losses to the permanent establishment</u> To the extent that tax losses may be carried over to a Danish permanent establishment it is unclear what allocation principles that would be applied.	

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
<u>6.3 Specific legislation for divisions/partial divisions/transfer of assets</u> No specific legislation has been enacted regarding the carry-forward of tax loss divisions/partial divisions and transfer of assets which means that the principles applies to mergers, cf. 6.1 will also apply in this case. This means that - with the exception mentioned below - tax losses in both the receiving and transferring company will be lost as a consequence of the tax exempt restructuring (division/partial division/transfer of assets). However, in the tax authorities' guidelines it is mentioned that tax losses of the transferring company in a partial division and in transferring company in a transfer of assets are not lost. In this case the tax losses of the receiving company will still be lost (please see 6.1). It is mentioned in the preparatory documents regarding the legislation that this rule on loss of tax losses in the receiving company (and by way of the merger also the transferring company) is due to the risk that the transferring and receiving company only merge in order to utilize tax losses in the receiving (or transferring) company. If the rule did not apply to both the receiving and the transferring company the parties could easily bypass the rule as the company having the tax losses could be the receiving company (or vice versa). The rule on loss of tax losses in the receiving company was inserted in the Danish Merger Tax Act in 1975 and has remained in the Merger Tax Act since (the wording has been updated and other changes have been made e.g. when the companies have been jointly taxed (please see 6.1).	LV S.D.2 and LV S.D.3

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses In general the conditions should be the same, cf. the legislation. However, no guidelines or tax practice exist on the application of the rules in a cross-border situation (please see 6.1).	

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Amended holding threshold N/A. A capital gain on the holding is not taxable. Denmark has not implemented Article 7(2).	FUL § 10, stk. 1

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses Yes. According to Danish tax law losses have no tax implications (i.e. losses are not tax deductible).	FUL § 10, stk. 1

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder From a Danish tax perspective, divisions and share exchange can in each case be made according to two sets of rules: One requiring permission from the tax authorities and having a valid business reason for the restructuring whereas the other does not require permission and also no valid business reason. The taxpayer may decide which sets of rules he wants to use. Only the one that requires permission is an implementation of the EU Merger Directive. Only the regime that is an implementation of the Merger Directive is described below.	FUL § 11

(a) Merger The succession principle applies on shareholder level and prevents economic double taxation.	ABL § 36
(b) Exchange of shares The shareholder is seen as having acquired the shares in the receiving company at the original cost and time (succession principle). The receiving company is seen as having received the shares in the transferred company at the fair market value at the time of the exchange and at the time of the exchange.	§ 15b
(c) Division The shares in the receiving company are considered being acquired at the original cost and time (succession principle).	
(d) Transfer of assets Reference is made to Section 9.1 describing avoidance of economic double taxation regarding transfer of assets.	

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
8.2 Computation of the capital gain Any cash payments received when making a merger, division or share exchange is taxable at the level of the Danish shareholder. Generally, the cash payment is taxed as a sale of shares. However, a cash payment in a partial division is taxed as a dividend distribution (please see. 2.2). It is not possible to receive a cash payment in a transfer of assets, cf. also the Merger Directive Article 2 (d).	FUL § 9, stk. 1 (merger) FUL § 15b, stk. 4 (division) ABL § 36, stk. 2 and 3

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
8.3 Further conditions for tax relief No.	

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
9.1 Avoidance of economic double taxation at the level of the transferring company As outlined above Danish tax law follows the succession principle (please see 4.1). However, as to the transfer of assets Danish tax law creates genuine double taxation when applying the Directive. In the event of a transfer of assets the receiving company takes over the tax basis and realizes no step-up. At the same time the transferring company receives shares in the receiving company as consideration. The shares received are considered acquired at fair market value less the deferred tax on the transferred assets. This means that if the receiving company subsequently sells the assets, and the transferring company sells the shares in the receiving company (within three years) the deferred tax is taxed twice (i.e. double taxation can occur). This is a major disadvantage when applying the rules on a transfer of assets. The tax practice is not in line with the objectives of the EU Merger Directive. No measures have been taken to eliminate this economic double taxation.	FUL § 15d

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
9.2 Further conditions for tax relief If the receiving company is an active company, the shares that the transferring company receives in the receiving company must be subscribed at the fair market value, and no premium in excess is allowed. In specific cases the Danish tax authorities have made the approval conditioned upon subsequent transactions within the next three years must be notified to the tax authorities. This condition has been used in cases where the taxation within three years after the transfer of assets is tax exempt. For a Danish transferring company a gain on the shares in the receiving company will thus be taxable, whereas this is not the case if the transferring company is not a Danish company. This tax practice will often only trigger special conditions on foreign companies and may therefore not be in line with the objectives of the Merger Directive.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
9.3 Tax deferral N/A.	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
10.1 Loss recapture for permanent establishments in third Member States According to Danish tax legislation recapture of tax losses from a foreign permanent establishment may under certain circumstances occur.	
(a) Recapture of tax losses incurred before 2005	LL § 33D
Until income year 2005 income (including losses) from a foreign permanent establishment were included in the taxable income of the Danish company having the permanent establishment.	
The tax losses were under certain circumstances recaptured according to special and complicated legislation e.g. if the permanent establishment was transferred from one affiliated company to another affiliated company. Different transactions could trigger taxation of the recapture balance i.e. merger, transfer of assets and division.	SEL § 8, stk. 2
However, an exception applies to this recapture rule as no recapture of tax losses is triggered if the receiving company succeeds in the tax losses from a foreign tax perspective, and if the receiving foreign company's profits are taxed in Denmark. This exemption does not apply to other restructurings than mergers.	SEL § 31A, stk. 10 and 11
(b) Recapture of tax losses incurred after 2005 As from 2005 income (including losses) from a foreign permanent establishment s no longer included in the taxable income of the Danish company having the permanent establishment. However, if the Danish company has elected international joint taxation (which hardly any Danish companies/groups has done) the income from a foreign company will still be included in the taxable income of the Danish company having the permanent establishment.	

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
10.2 Permanent establishment in the Member State of the receiving company No special rules apply to this situation.	

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
10.3 Concept of worldwide taxation/tax credit system Please note that as from 2005 Denmark has abolished the concept of worldwide taxation and does not tax Danish resident companies on income deriving from permanent establishments abroad unless the company specifically has elected international joint taxation. Only an insignificant minority of Danish companies has made this election. Special rules apply to shipping companies.	

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
10.4 Tax deferral N/A.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies Denmark has opted not to apply the rules for tax-exempt restructuring into transparent entities, cf. Article 10a (1), and the taxpayer should therefore be granted a tax credit in accordance with Article 10a (2). According to Danish tax law, the taxpayer is granted a notional tax credit for taxes which would have been taxed if the transaction was carried out as a taxable transfer. Denmark has introduced anti-avoidance legislation regarding foreign tax	Act implementing Directive 2005/19 (Law No 1182 of 12 December 2005) LL § 33, stk. 4 SEL § 2A

legislation (especially US Check-The-Box legislation) which may re-qualify some Danish companies to transparent entities. If a Danish entity is re-qualified according to foreign tax legislation the Danish entity will also be re-qualified as a transparent entity for Danish tax purposes. If a Danish company is re-qualified according to this rule this implies that the company cannot benefit from the EU Merger Directive.	

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit The profit is computed as if all assets and liabilities including non-booked assets had been sold at the fair market value.	LL § 33, stk. 3

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit The tax base of the notional tax credit is the foreign taxes that would have been levied if the business was sold at the fair market value. The Danish authorities have adopted the wording of the Merger Directive. However, no guidelines or tax practice are available.	LL § 33, stk. 3

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders Denmark has decided not to apply the benefits from the Merger Directive to transparent entities. On that basis the taxation of such restructurings undertaken by such transparent entities will trigger Danish taxes regardless of whether the restructuring is carried out as a domestic or cross-border restructuring. There is no difference between the taxation of a domestic or a foreign entity or a domestic or foreign shareholder if a transparent entity carries out a restructure which triggers Danish taxation due to the Merger Directive not covering such restructurings. It is specifically mentioned in the preparatory documents to the law implementing Directive 2005/19 (Act No 1182 of 12 December 2005) that taxation of foreign transparent entities will be taxed on the basis of the same tax rules as Danish transparent entities. Finally, Danish tax legislation does not clearly distinguish between Article 11a(3) and 11a(4) as it is just mentioned in the preparatory documents	Act implementing Directive 2005/19 (Law No 1182 of 12 December 2005)

that Denmark will tax transparent entities and the shareholders according to existing rules.	

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company In the preparatory documents to the law implementing Directive 2005/19 (Act No 1182 of 12 December 2005) it is mentioned that taxation of foreign transparent entities will be taxed on the basis of the same tax rules as Danish transparent entities. In our opinion there should be no doubt that by this statement the tax authorities mean that foreign transparent entities carrying out (participating in) restructurings in Denmark should rely on the same treatment for tax purposes in Denmark as Danish transparent entities. However, no guidelines exist and no published tax practice has been published regarding this issue.	Act implementing Directive 2005/19 (Law No 1182 of 12 December 2005)

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation A transfer of the registered office gives rise to exit taxation. However, to the extent that assets remain subject to Danish taxation such assets are not taxable. Assets which are allocated to a Danish permanent establishment of the foreign company will be considered 'subject to Danish taxation'. Also real property located in Denmark would remain under Danish taxation. Furthermore, it should be examined whether the SE company remains a Danish tax resident company. This is the case if the daily management of the company is carried out from Denmark. The daily management (tax law) is not necessarily equal to the head office (company law). In this case all assets will remain under Danish taxation. It is mentioned in the preparatory documents regarding the legislation that a permanent establishment will be able to utilize tax losses that have not been utilized by the SE company.	SEL § 5, stk. 7

It is yet to be decided by the ECJ to what extent exit taxation is in accordance with the EU Treaty.	

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' The term head office has not been defined in tax law and is not mentioned in the preparatory documents regarding the implementation of the tax legislation. No administrative guidance has been issued and no tax practice exists regarding the term. Furthermore, the term has not been defined in Danish company law when implementing Article 7 of Regulation 2157/2001 in Danish company law.	

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency As mentioned under 10b.2 the term 'head office' has not been interpreted in Danish tax law and it is therefore not possible to say whether the concept of tax residency due to the 'daily management' being in Denmark and the company law concept of 'head office' coincide. The term 'head office' is not referred to as a tax residence criterion in Danish tax legislation. From a Danish tax perspective the concept of 'daily management' is defined as the place where the decisions regarding the daily management of the company are taken. In administrative guidelines it is mentioned that the daily management will often be the place where the Board of Management ('*direktion*') is placed. If the Board of Directors ('*Bestyrelse*') carries out the actual daily management of the company, the place of the daily management will be the place where the Board of Directors makes decisions regarding the company instead. In any event, the place of daily management is based on a specific evaluation of the relevant facts. The definition in many of the DTCs that have been concluded by Denmark includes a reference to the effective place of management in the case of dual residency. The content of the concept 'effective place of management' has not been defined in Danish tax law. Further, as most Danish DTCs are interpreted in line with the OECD Model Taxation Treaty Article 4. However, the commentaries to the OECD Model Double Taxation Treaty do also not contain a definition of the concept. From a Danish tax perspective the concepts of 'effective place of management' and 'daily management' will probably often coincide, however, there may be specific situations where the concepts differ.	LV S.A.1

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
10b.4 Assets and liabilities not effectively connected with a permanent establishment Please see 10b.1.	SEL § 5, stk. 7

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
10b.5 Tax deferral Under Danish tax law Denmark impose exit taxation on companies moving daily management/effective place of management from Denmark. The company is taxed as if all assets - not allocated to permanent establishments in Denmark - are sold at the fair market value. Denmark has taken no action as to tighten up the exit taxation legislation regarding companies. It is uncertain whether the unconditioned Danish exit taxation is in accordance with EU law.	SEL § 5, stk. 7

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 The term 'comparable circumstances' The term 'comparable circumstances' has not been defined in Danish tax legislation. It is mentioned in the law implementing the Article 10b when describing the rules in the Directive regarding transfer of the registered office. No published tax practice exists.	Law No 1182 of 12 December 2005

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Loss recapture for permanent establishments No special tax legislation has been enacted regarding recapture of tax losses in a foreign permanent establishment due to a transfer of the registered office from Denmark to a foreign country. Therefore - in our opinion - the normal rules on recapture of tax losses should apply. See Section 10(1).	SEL § 5, stk. 7 and

Normally, the recapture balance is triggered if a Danish company ceases to be fully taxable in Denmark (cf. SEL § 5, stk. 7), cf. LL § 33D, stk. 5. However, the cease of full taxation to Denmark for a SE-company which transfer its registered office to another EU country is not comprised by SEL § 5, stk. 7 as it is instead comprised by SEL § 5, stk. 8. Therefore, the recapture rule regarding cease of taxation to Denmark does not seem to apply and - based on the wording of the legislation - no recapture of tax losses seam to be triggered as a consequence of the transfer of the registered office. It is not possible to tell whether this is intended or whether it is a lapse in the Danish recapture of tax loss legislation. The preparatory documents regarding the tax legislation does not contain any reasons. Currently, the Danish tax legislation on recapture of tax losses consequently seem to comply with the Merger Directive which does not contain any rules which allows for recapture of tax losses in a foreign permanent establishment.	8 LL § 33D, stk. 5

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>**10d.1 Deemed liquidation**</u> According to the Danish tax authorities' guidelines a company is generally regarded as dissolved if it changes its legal identity. No guidelines are available as to whether SE/SEC but in our opinion the transfer of the registered office of an SE/SEC company should not be seen as a deemed liquidation which trigger taxation on the shareholder level as the concept of the SE/SEC company must imply that the legal identity remains even though a transfer of the registered office. As opposed to another company vehicles. However, neither tax practice nor guidelines are available.	LV S.B.3

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>**10d.2 Tax treatment of third country residents**</u> No legislation has been enacted regarding this situation; however, as foreign shareholders are generally not taxable to Denmark of a gain on the shares in the SE-company even if the SE-Company is tax resident in Denmark, it is our opinion that such shareholders should also not be taxable to Denmark due to the transfer of the registered office.	

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 *'Leur-Bloem'* and C321/05 *'Kofoed'*. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 *'Cadbury'*. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> The Article 11 have not been transposed into Danish tax law but as the divisions/transfer of assets/exchange of shares requires permission from the Danish tax authorities the authorities includes equal provisions on anti-abuse when determining whether permission can be granted. The Merger Directive does not as such prohibit that taxation under the Directive is subject to permission. However, in our opinion the permission procedure must not be an obstacle and permission cannot be based on conditions that go further than stated in Article 11. In order to obtain permission a sound business reason must be proved. In our opinion the Danish tax authorities set very strict conditions that sometimes seem to go beyond Article 11.	FUL § 15, § 15a and FUL § 15c ABL § 36

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' (*'Kofoed'*, paragraph 46)?	Reference
<u>11.2 General anti-abuse provision</u> Please see 11.1.	FUL § 15, § 15a and FUL § 15c ABL § 36

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
<u>11.3 The concept of 'wholly artificial arrangement'</u> As a consequence of the 'Cadbury' judgment the Danish tax law on CFC has been changed. As for companies CFC taxation is today applicable for Danish and foreign subsidiaries regardless whether the establishment of the subsidiary can be regarded as wholly artificial. It is highly questionable whether this approach complies with EU Treaty. This means that Denmark has taken no steps as to include the principles in question under Danish tax law and the 'Cadbury' judgment has therefore not resulted in new national provisions or interpretations of Article 11.	FUL § 15, § 15a and FUL § 15c ABL § 36

However, individuals can be exempt from CFC taxation if it can be demonstrated that it is not an artificial arrangement. However, Danish tax law refers to the 'Cadbury' judgment only without any additional guidelines.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
<u>11.4 Specific anti-abuse provisions</u> Denmark has adopted specific anti-abuse provisions by means of a requirement that the company should obtain permission from the tax authorities on beforehand. Under this permission procedure the tax authorities will examine whether the restructuring is based on sound business reasons. Also under Danish tax practice the Danish tax administration can impose a three year notification period of all restructurings and also demand continuity of ownership for three years after the specific restructuring (exchange of shares, transfer of assets etc.). The original permission can be upheld only if a restructure or a discontinuity of ownership is based on valid commercial reasons. This can leave the tax payer in an uncertain situation that does not always seem in line of the objectives of the Merger Directive. If the tax payer does not comply with the notification procedure (i.e. does not notify the tax authorities on beforehand of the subsequent restructure) the permission is as a general rule - and as stated in the rulings without further discussions - withdrawn with retroactive effect. The permission is withdrawn regardless of the subsequent restructure undertaken and regardless of whether it is based on sound business reasons. In our opinion this part of the Danish tax practice is not in line with the EU Merger Directive. The problem is that a restructure that is carried out on the basis of the Merger Directive may become taxable even when if it is based on sound business reasons.	FUL § 15, § 15a and FUL § 15c ABL § 36

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' The term has not been interpreted / transposed in national legislation. But according to tax practice tax payers must provide a business case to demonstrate the valid commercial reasons and convince the tax authorities that the objective of the restructure is not to sell the business or shares without taxation or in order to reduce taxation. The basic condition is that the restructure must be for the benefit of the business (company) and not to favor the shareholders and of course the restructure must not be driven by tax objectives.	FUL § 15, § 15a and FUL § 15c ABL § 36

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof No rules are available but according to practice the tax administration has definitely given the initial burden of proof to the tax payer.	FUL § 15, § 15a and FUL § 15c ABL § 36

ESTONIA

Abbreviations

English	Estonian	English	Estonian
CC	ÄS	Commercial Code	Äriseadustik
AA	RPS	Accounting Act	Raamatupidamise seadus
ITA	TuMS	Income Tax Act	Tulumaksuseadus
TA	MKS	Taxation Act	Maksukorralduse seadus

Survey of the Implementation of Council Directive 90/434/EEC

(The Merger Directive, as amended)

ESTONIA

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
Overall state of implementation The Merger Directive has been implemented into the Estonian tax law through the general provisions to be found in the Income Tax Act (ITA). It is a general principle that mergers, divisions, and reorganizations are tax-neutral and the movement of fiscal reserves among the transferred assets is not taxable in line with the general principles of the Estonian tax system. No individual income tax will be levied on the capital gain realized on the substituted shares or on the allotment of shares, nor on the unrealized capital gain on the shares in a SE or SCE transferring its registered office, as long as the substituting shares in the acquiring/receiving, split off or migrating company are not sold by the shareholder. For legal entities, this requirement is fulfilled by the general concept that accrued but undistributed profits are not taxed. Another requirement of the Merger Directive that is met due to the Estonian unique tax system is the carry over of tax-free provisions and reserves – as companies in Estonia are obliged to pay corporate income tax only on distributed profits, such provisions and reserves do not exist, i.e. there is nothing to carry over. Although not all of the situations covered by the Merger Directive are explicitly regulated by the ITA, tax neutrality should be achieved through the interpretation of general clauses. Our analysis is substantiated by the following Estonian legal acts: Income Tax Act, Taxation Act, Commercial Code and Accounting Act. In conclusion, we find that the Merger Directive has been fully and correctly implemented into the Estonian tax law.

Article 1 – Scope

Please describe how the expression ‘in which companies from two or more Member States are involved’ has been interpreted and implemented. Has the term ‘companies involved’ been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
1.1 Involved companies Companies involved according to the Tax Law Merger Directive are ‘*täisühing*’, ‘*usaldusühing*’, ‘*osaühing*’, ‘*aktsiaselts*’, ‘*tulundusühistu*’. From the Company Law Merger Directive implementation perspective, however, cross-border mergers are not allowed for ‘*tulundusühistu*’, i.e. cooperative society (as laid down in Article 3(2) of the Company Law Merger Directive, Member States may decide not to apply this directive to cross-border mergers involving a cooperative society). It has further been stipulated that ‘*aktsiaselts*’ and ‘*osaühing*’ can only merge with a limited liability company of an EEA Member State meeting the requirements of	CC Sec. 433^1 (1) Article 2(1) 2005/56/EC

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Article 2 section 1 of Directive 2005/56/EC, if the registered office, place of management or main location of activity is located in another EEA Member State. The expression 'in which companies from two or more Member States are involved' has been interpreted considering the directly involved companies not the parent entities.	

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
1.2 Foreign Member State and third state merger Benefits of the Merger Directive do not apply if the merging companies are from a single (foreign) Member State or from a third State or States.	CC Sec. 433^1 (1)

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term 'securities' In the Estonian legislation covering mergers, divisions (partial divisions) and asset transfers, the term 'securities' is defined as a share in a company's share capital. In case of a corporation 'security' is considered to be a share in the registered share capital and in case of other legal entities it is representing the membership in a legal entity.	

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' Cash payments exceeding 10% are permitted if the share exchange rate is fixed too low or the legislation applicable in the Member State of the acquiring company allows it. According to our understanding of the CC, the cash payment applies on an overall basis.	CC Sec. 392 (2) CC Sec. 398 (3) 2005/36/EC art 3 Sec. 1

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger No further types of merger applicable.	N/A.

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares The Estonian legislation does not prescribe the term 'gradual increase in the stake of target company'. Exchange of shares in the course of increase of share capital with non-monetary contribution and thus consolidation of the majority is also tax-neutral if the majority is consolidated via share capital increase. Transfer of shares without any increase/decrease in the share capital, i.e. not in the course of a merger, division or transformation of companies, may not be tax-neutral (e.g. shareholder X of company A contributes shares in company A to company B and receives shares of company B in exchange, whereas company B would grant already existing shares in company B (own shares) to X – this transaction could constitute a taxable gain if share values are not equal).	N/A.

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
2.5 Consolidation of qualifying holding Exchange of shares is tax neutral only if executed in the course of merger, division or transformation of companies. Absence of a specific provision for situations where own shares are transferred in exchange, could lead to taxation of private individuals and non-residents (for Estonian legal entities such gain would not be taxable until the distribution of profit).	ITA Sec. 15 (4) clause 10 ITA Sec. 31 (1) clause 9

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 *'Andersen og Jensen'*. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
2.6 The term 'branch of activity' The legislation in Estonia defines the term 'branch of activity' as enterprise - an economic unit through which an undertaking operates. Enterprise is comprised of things, rights and obligations which are or should, by their nature, be designated for the activities of the enterprise. The remaining branch requirement has been implemented through the remaining 'enterprise' definition. The legislation defines also the place through which the permanent economic activity of a non-resident is fully or partially carried out in Estonia as a 'branch'.	CC Sec. 5 (1) CC Sec. 384

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
3.1 Types of entities All Estonian legal entity types are listed in the annex.	CC Sec. 433^1 (1)

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
3.2 Transparent entities According to the legislation applicable in Estonia, the entities not having the status of a legal person are considered to be transparent. None of the legal persons established according to the Estonian Commercial Code are considered transparent for tax purposes.	

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency The ITA prescribes the criterion of the tax residency of persons other than individuals, as following - a legal person is a resident if it is established pursuant to Estonian law. European Company (SE) and European Cooperative Society (SCE) whose seat is registered in Estonia are also	ITA Sec. 6 (2 – 5)

residents. A legal person not specified above, is treated as a non-resident. Tax residency is not determined based on the 'place of effective management' test. Double tax conventions concluded by Estonia refer to the mutual agreement procedure for the determination of the country of residence in the case of dual resident person other than an individual and, in the absence of such an arrangement, deny benefits under the convention to this person. Estonian tax treaties do not use 'place of effective management' test.	

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>**3.4 Subject-to-tax clause**</u> All Estonian legal persons are subject to regular corporate income tax ('*tulumaks*') it is not possible to apply for tax exemption. Neither could companies apply for special incentives. Also, according to the ITA, it is not necessary for the non-Estonian company in the transaction to be subject to tax.	ITA Sec. 1 (3)

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>**3.5 Shareholder requirements**</u> No requirements.	N/A.

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>**4.1 The concepts of 'real values' and 'value for tax purposes'**</u> Real value can be defined as fair market value. Value for tax purposes (applicable only to non-residents and resident natural persons, since resident legal entities are subject to tax only on distributed profits) is the acquisition cost as defined in ITA as all certified expenses which a taxpayer makes in order to obtain, improve or supplement property, including any commissions and fees paid. The acquisition cost in terms of mergers, divisions or transformation of companies is deemed to be the acquisition cost of a holding in a company being acquired, acquiring, or being divided or transformed or contributions	AA Sec. 17 (1) ITA Sec. 38 (5) (5^1) (5^2)

made to acquire such holding, to which additional contributions made during the merger, division or transformation have been added, and from which payments received have been deducted.	

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions No specific guidance has been issued in respect of divisions and partial divisions.	

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' Permanent establishment is defined by ITA as the place through which the economic activity of a non-resident is fully or partially carried out in Estonia. Permanent establishment inter alia is: (a) a branch; (b) a centre of management, or an office, factory or workshop; (c) a building site, a place of construction, or an installation or assembly project; (d) a place where the examination or extraction of natural resources is carried out, as well as any supervisory activities related thereto; (e) a place for the provision of services (including management and consultation services). If upon merger a resident company is deleted from the commercial register without liquidation and the economic activities of the company are continued in Estonia through the company's permanent establishment, then the part of the value of the property taken out of the permanent establishment in excess of the amount specified in the clauses below is subject to taxation: (a) the own capital of the resident company as at 31 December 1999; (b) monetary and non-monetary contributions paid into the own capital as of 1 January 2000; (c) the value of property brought to Estonia for the permanent establishment after the deletion of the company from the	ITA Sec. 7 (1) ITA Sec. 53 (4^3)

commercial register. The assets and liabilities 'effectively connected' with a permanent establishment of the receiving company in the Member State of the transferring company can therefore be defined as the aggregated sum of the amounts above. Taxation arises only if the value of property taken out exceeds the aggregated sum of the amounts above. 'Taking out' encompasses transactions both with head office and third parties that decrease the aggregated amounts above. Property to be taken out is subject to tax in the part for which no other property or service is provided in return. If the branch is entitled to claim back the property taken out or a claim of equal value arises in return of the property taken out, no tax consequences will follow, i.e. the claim recognized in the accounting of the branch must at least be equal to the value of property taken out. Permanent establishment must keep detailed record of expenses made, revenue earned, assets and obligations. Some administrative guidance has been issued by the Estonian Tax and Customs Board in relation to hidden profit distributions made by the permanent establishment.	

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
<u>**4.4 Limitation of the scope of relief**</u> According to the Taxation Act, if the transfer of rights and obligations from one person to another pursuant to legal succession is prescribed by law, all claims and obligations (tax liability, tax withholding liability, claim for refund, tax liability of third party, accessory obligation, except the obligation to pay a penalty payment) also transfer to the legal successor without any immediate tax consequences. The permanent establishment of the transferring company is treated as an independent taxpayer from tax perspective (with its own accounting and tax calculation obligation). Furthermore, recapturing depreciation of assets could not result in any tax obligation, as the branch is liable to corporate income tax only if it transfers profits out of Estonia. In other words, the scope of relief is not limited.	TA Sec. 35

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
<u>**4.5 Assets and liabilities not effectively connected with a permanent establishment**</u> Corporate income tax is levied on distributed profits only. Generally, any asset, once it has become part of the branch's assets for tax purposes, can be taxed upon disappearing from the branch's balance sheet (considered as taxable profit from the Estonian Income Tax Law perspective) or upon closing down of the branch (considered as liquidation proceeds from the	

Estonian Income Tax Law perspective). As mentioned above, if no claim of equal value arises in return of the property taken out and the aggregated amount stated in 4.3 of this questionnaire is exceeded, tax consequences arise for the branch. Assets not effectively connected with the PE (general OECD Model Convention guidelines are followed in this respect), are left out of the income tax calculation., i.e. assets that remain effectively connected to the remaining legal entity will not be subject to income tax as long as these are not distributed.	

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company The cancellation of a holding in the transferring company should not result in any gains accruing to the receiving company. For consolidation purposes any profits allotted to the shares should already have been recorded in the financial statements of the acquiring company.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral According to the best of our knowledge there has been no account taken of the case law of the ECJ as there has been no discrimination in Estonia similar to those in the judgment in Case C-470/04 'N'.	

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities Tax transparent entities are defined as foreign associations of persons or pools of assets without the status of a legal person. The income of such entities is subject to taxation as the income of the shareholders or members of such association or pool in proportion to the sizes of their holdings. If the members or shareholders of an association or pools of assets are unknown or their residency is not proved, the income is attributed to the person who administers the assets of the association or the pool of assets or who concludes transactions in the name thereof. The criterion by which an entity is defined as transparent is therefore the absence of a legal person status. None of the legal entities in Estonia could therefore be defined as transparent.	ITA Sec. 6 (3^1)

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
<u>4.9 Further conditions for tax relief</u> Relief under Article 4 has not been made subject to any further conditions.	

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>5.1 The term 'provisions and reserves'</u> The term 'provisions and reserves' has not been defined in the Estonian tax legislation since 1 January 2000, as corporate income tax is no longer calculated on the basis of earned, but on the basis of distributed profits.	

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
<u>5.2 Exclusion of 'provisions and reserves' from permanent establishments</u> The Article has not been implemented at all.	

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
<u>5.3 Allocation method for provisions and reserves</u> The need for allocation does not arise as there are no provisions or reserves to carry over.	

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
<u>5.4 Further conditions for carry-over of provisions and reserves</u> No further conditions.	

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry-over of losses The concept of loss is irrelevant from the Estonian tax law perspective as there is no taxation of annual profits, In other words there is no equivalent domestic situation, irrespective of the accounting situation (profit or loss), a company distributing profits is subject to income tax.	

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment There is no method for the allocation of losses (please see 6.1).	

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets No specific legislation has been enacted, for divisions, partial divisions, and transfers of assets.	

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses No further conditions.	

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Amended holding threshold There is no need for such implementation as gains accruing to the receiving company on the cancellation of its holding shall not be subject to any taxation following the general principle of the Estonian income tax law.	

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses There is no national legislation or administrative guidelines in this respect.	

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder According to the ITA, acquisition cost means all certified expenses which a taxpayer makes in order to obtain, improve or supplement property, including any commissions and fees paid. The acquisition cost of a holding (shares, contributions) acquired as a result of a merger, division or transformation of companies or non-profit co-operatives is deemed to be the acquisition cost of a holding in the company or non-profit co-operative being acquired, acquiring or being divided or transformed or contributions made to acquire such holding, to which additional contributions made during the merger, division or transformation have been added, and from which payments received have been deducted. The acquisition cost of a holding (shares, contributions) acquired by way of a non-monetary contribution shall be equivalent to the acquisition cost of the assets which constituted the non-monetary contribution. If the acquisition cost of the thing or proprietary right which constituted a non-monetary contribution has previously been deducted from the business income of the natural person and income tax has not been charged on it as assets taken into personal use, the acquisition cost of the holding shall be deemed to be zero. Additional contributions made shall be added to the acquisition cost determined pursuant to subsection (5^1) and payments received shall be deducted. In the calculation of acquisition cost, supply of labor or other services shall not be considered to be a non-monetary contribution. Therefore, taxation of capital gains is deferred until the latter alienation of shares received in return. The gain is recomputed on a subsequent taxable disposal of the asset based on the original cost of asset.	ITA Sec. 38 (1) ITA Sec. 38 (5) ITA Sec. 38 (5^1) ITA Sec. 38 (5^2)

Deferral is conditional upon the shareholder assigning to his new shares the same value for tax purposes as the old shares had for tax purposes (rolled-over tax base). Thus, the capital gain will be taxed later when the shareholder disposes of the shares in the acquiring/ receiving company.	

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
8.2 Computation of the capital gain No guidance has been issued by the tax authority on the computation of the capital gain in the situation covered by Article 8(9), however from the wording of the ITA section 38(5) it may be concluded that additional cash payments made to the shareholders (natural persons) are deducted from the initial acquisition cost for tax purposes and shall be subject to capital gain taxation on the latter disposal of shares of the acquiring company. Additional contributions made by the shareholder (natural persons) increase the acquisition cost. For legal entities earned capital gain is subject to tax only upon distribution of profits.	

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
8.3 Further conditions for tax relief There are no further conditions for the tax relief.	

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
9.1 Avoidance of economic double taxation at the level of the transferring company The shares received by the transferring company should be considered to have been received at fair market value of the assets transferred.	

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
9.2 Further conditions for tax relief No.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
9.3 Tax deferral According to the best of our knowledge there has been no account taken on the case law of the ECJ as there has been no discrimination similar to the cases discussed in the judgment in Case C-470/04*'N'*.	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
10.1 Loss recapture for permanent establishments in third Member States No	

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
10.2 Permanent establishment in the Member State of the receiving company N/A.	

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> Unrealized capital gains are not taxed; cash-basis principle is applied. Profit that has been subject to tax on the level of the PE is tax exempt on the level of the Estonian company; profits derived from the PE may be distributed tax exempt.	

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
<u>10.4 Tax deferral</u> According to the best of our knowledge there has been no account taken on the case law of the ECJ as there has been no discrimination similar to the cases discussed in the rulings of the ECJ.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
<u>10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies</u> The option right has not been implemented into the ITA. Transactions covered by the Merger Directive are tax-neutral also for Stransparent entities.	

How have the 'profits' of an <u>acquired</u> company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
<u>10a.2 Tax base for notional tax credit</u> N/A.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit N/A.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders The option right has not been implemented into the ITA. Transactions covered by the Merger Directive are tax-neutral also for transparent entities.	

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company N/A.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation There are no exit taxes or comparable fiscal liabilities in relation to the relocation of the SE if the economic activities are continued. If a resident company is deleted from the commercial register without liquidation and the company terminates its economic activity in Estonia, the market price of the holdings (shares or contributions) of the non-resident in the company minus the acquisition value of the holdings is subject to taxation as gains of the non-resident. We concur that the non-taxation of resident	ITA Sec. 29 (5) 5'1

legal entities in the same circumstances could result in violation with the EC Primary Law, however it does not contradict with the Merger Directive as such.	

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' The term head office has not been defined for the purposes of the Merger Directive. The term 'head office' has been defined in Estonian legislation as one of the criterions to determine non-resident's permanent establishment in Estonia. Head office has the meaning of 'place of management' as defined in the OECD Model Tax Convention guidelines.	ITA Sec. 7(1)(2)

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency The only criterion used to determine tax residency is the place of incorporation. DTCs concluded by Estonia do not include any tiebreaker rules in this respect – where a company is resident of both Contracting States, the competent authorities shall endeavor to settle the question by mutual agreement and determine the mode of application of the DTC to such company.	

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
10b.4 Assets and liabilities not effectively connected with a permanent establishment Generally, any asset, once it has become part of the branch's assets for tax purposes, can be taxed upon disposal from the branch's balance sheet or upon closing down of the branch. As mentioned above, if no claim of equal value arises in return of the property taken out and the aggregated amount stated in 4.3 of this questionnaire is exceeded, tax consequences arise for the branch. As described above, there are no exit taxes in Estonia – provided that the assets remain connected to the remaining permanent establishment or remaining legal entity.	

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
<u>10b.5 Tax deferral</u> According to the best of our knowledge there has been no account taken on the case law of the ECJ as there is no discrimination similar to the cases discussed in the judgment in the *'N'* case.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
<u>10c.1 The term 'comparable circumstances'</u> N/A in the context of the Estonian tax legislation.	

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
<u>10c.2 Loss recapture for permanent establishments</u> N/A in the context of the Estonian tax legislation.	

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>10d.1 Deemed liquidation</u> If a resident company is deleted from the commercial register without liquidation and the company terminates its economic activity in Estonia, the market price of the holdings (shares or contributions) of the non-resident in the company minus the acquisition value of the holdings is subject to taxation as gains of the non-resident. Taxation is deferred if the economic activities of the company are continued in Estonia through the company's permanent establishment (please see 4.3). We concur that the non-taxation of resident legal entities in the same circumstances could result in violation with the EC Primary Law, however it does not contradict with the Merger Directive as such.	ITA Sec. 29 (5^1)

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>10d.2 Tax treatment of third country residents</u> See 10d.1.	

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 *'Leur-Bloem'* and C321/05 *'Kofoed'*. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 *'Cadbury'*. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> No specific anti-abuse provisions enacted to the ITA, general anti-abuse clauses of the Taxation Act followed by tax authorities.	

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' (*'Kofoed'*, paragraph 46)?	Reference
<u>11.2 General anti-abuse provision</u> According to the Taxation Act, if it is evident from the content of a transaction or act is performed for the purposes of tax evasion, conditions which correspond to the actual economic content of the transaction or act apply upon taxation. There is, however limited court practice as of date, and the interpretation of this concept will most likely be illustrated further in the future.	TA Sec. 84

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
<u>11.3 The concept of 'wholly artificial arrangement'</u> The concept 'wholly artificial arrangement' has been interpreted by several rulings of the Supreme Court, most commonly the case 3-3-1-31-99 is quoted: 'sections of the ITA must be interpreted in accordance with other	

sections, the meaning an purpose of the ITA and general clauses of tax law. Tax law sets the content of tax liability. Legal aspects constituting the tax liability must be in compliance with the actual economic substance of the transaction. Otherwise, the contracting parties would be entitled to determine the tax liability, its essence and size. This situation would contradict with the essence of tax as public law element and cause unequal taxation.'	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions According to the best of our knowledge there have been no such cases.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' The absence of valid commercial reasons can lead to the conclusion that the transaction is artificial. Although not specifically mentioned in the TA, economic rationale behind the transaction is a crucial element in determining whether a transaction is artificial or not. There is, however limited court practice as of date, and the interpretation of this concept will most likely be illustrated further in the future.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof TA section 82 states that 'upon verification of the performance of the tax liabilities of a taxable person and upon making an assessment of tax, a tax authority shall proceed primarily from tax returns submitted by the taxable person, the accounts kept by the taxable person and other records kept by the taxable person concerning the activities of the taxable person. If a tax authority has doubts concerning the accuracy of information submitted by a taxable person, the tax authority shall collect supplementary evidence'. Therefore, initial burden of proof lies on the tax authority. In order to make an assessment of tax, a tax authority shall prepare a notice of assessment. The notice of assessment shall clarify the method by which assessment of the tax payable is to be made. If none of the evidence submitted by a taxable person is taken into consideration upon making an assessment of tax or if only some of the evidence is taken into	TA Sec. 82 TA Sec. 95 (1,2) TA Sec. 150 (1) TA Sec. 150 (2)

consideration, the reasons therefore must be set out in the notice of assessment. If an amount of tax assessed in a tax notice or notice of assessment is challenged, the burden of proof that the tax was assessed incorrectly lies with the taxable person. Nevertheless, the burden of proof regarding evidence possessed only by a tax authority lies with the tax authority.	

FINLAND

Abbreviations

English	Finnish	English	Finnish
-	EVL	Business Income Tax Act	Laki elinkeinotulon verottamista
-	TVL	Income Tax Act	Tuloverolaki
-	VML	Act on Taxing Procedures	Laki verotusmenettelystä
-	KHO	Supreme Administrative Court	Korkein hallinto-oikeus
-	HE	Government Bill	Hallituksen esitys
-	KVL	Advance Ruling by the Central Board of Taxation	Keskusverolautakunnan ennakkoratkaisu

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
<u>Overall state of implementation</u> The original relevant Acts 29.12.1995/1733, which contained the implementation legislation into the EVL, entered into force on 1 January 1996. The rules applied retroactively to cross-border transactions entered into on or after 1 January 1995 if the taxpayer so requested. Notice 1/1997 by the National Board of Taxes on company reorganizations. Directive 2005/19/EC amending the Merger Directive (Amendment Directive) has been implemented into the EVL (22.12.2005/1137) as of 1.1.2006 by a government bill (HE 193/2005) with respect to amendments related to the SE and SCE, and as of 1 January 2007 (29.12.2006/1424) by a government bill (HE 247/2006) with respect to other amendments. The same Finnish domestic law provisions apply to both purely domestic arrangements and to arrangements involving a company of another EU Member State.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> The implementing tax law expressly refers to corporations as defined in Article 3a of the Merger Directive. The expression 'in which companies from two or more Member States are involved' appears in the reference to the Merger Directive's official title in EVL 52.2 §. In this respect, the residence of a parent company is insignificant.	EVL 52.2 § KHO 2004:112

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
<u>1.2 Foreign Member State and third state merger</u> According to case KHO 2004:112 of the Supreme Administrative Court, the principles of the Merger Directive as implemented into Finnish tax law were applied in the Finnish shareholder's taxation when two SICAVs established under Luxembourg law merged into each other. Therefore, at the level of the Finnish shareholder's taxation also single Member State transactions are covered. Pursuant to the freedom of establishment under the EC and EEA treaty the benefits of the Merger Directive are also granted to reorganizations which involve comparable companies established in EEA states. (Central Tax Board's advance ruling 2007/38). According to case KHO 1997/2531 of the Supreme Administrative Court, the principles of the Merger Directive as implemented into Finnish tax law were applied in the Finnish shareholder's taxation where two Canadian companies merged.	KHO 2004:112 Central Tax Board's advance ruling 2007/38 KHO 1997/2531

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
<u>2.1 The term 'securities'</u> The term 'securities' has been transcribed into Finnish tax law as '*osake*' which means 'share'. A specific definition for 'share' has not been implemented in Finnish tax laws. The definition for 'share' can be found mainly in the Companies Act. Whereas Article 2(a) of the Merger Directive refers to the receiving company issuing 'share', EVL 52a §, EVL 52c §, EVL 52d § and EVL 52f § refer to 'new shares' being issued to the shareholders of the transferring company. EVL clearly differs from the Directive in this respect and may be incompliant. However, it is our understanding that a draft Government Bill is pending which would amend the EVL so that the requirement of the securities being new is abolished.	EVL 52a § EVL 52c § EVL 52d § EVL 52f §

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' Finland has implemented a 10% cap on cash payments in compliance with the Merger Directive. Not more than 10% of the combined nominal value of the shares received as compensation may consists of a cash payment. The 10% cap on cash payments has been interpreted (although it is neither stated clearly in the directive nor in the Finnish legislation) to apply on an overall basis so a cash buy-out of minority shareholders is allowed. However, the practical significance of cash payments has been minor since the assessment basis for the cap is the nominal value of shares.	EVL 52a § EVL 52c § EVL 52f §

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger The Finnish national implementing legislation covers all types of mergers mentioned in the Merger Directive and does not cover any other or further types of merger.	N/A.

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares According to EVL 52f § capital gains taxation is deferred if the acquiring company acquires more than 50% of the other company's voting rights, or if the acquiring company already holds more than 50% of the other company's voting rights, acquires more shares in the target company. Therefore the tax deferral is applicable to the exchange of shares that leads to a stake of more than 50% of the other company's voting rights and any subsequent gradual increase.	EVL 52f

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
2.5 Consolidation of qualifying holding If the acquiring company already owns a majority holding any further exchanges of shares would be treated as a qualifying exchange of shares.	EVL 52f

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 *'Andersen og Jensen'*. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
2.6 The term 'branch of activity' According to EVL 52c § a 'branch of activity' means all the assets and liabilities of a division of a company which -from an organizational point of view - constitute an independent business, meaning an entity capable of functioning by its own. The definition of branch of activity has been clarified in extensive case law: A transfer of a single asset or only a few assets will not generally constitute a transfer of a branch of activity. For example, a single real property used by the transferring company in its business was not considered to qualify as a branch of activity (KVL 1996/101). However, the whole real property including any real estates and shares in real estate companies used by a group of companies in its business may constitute a branch of activity (KVL 2000/100). However transfers of e.g. information technology, public relations, marketing and equivalent business units should qualify for a branch of activity (KVL 1996/311). Also company's considerable investment activity (e.g. securities trading) has been considered to constitute a branch of activity.	EVL 52c § KVL 1996/101 KVL 2000/100 KVL 1996/311 KVL 2007/37

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
3.1 Types of entities According to EVL 52.2 § the application of Finnish rules governing mergers, divisions, transfers of assets and exchanges of shares with respect to cross-border transactions are limited to cases involving companies which are resident in two or more different EU Member States referred to in Article 3(a) of the Merger Directive and subject to corporation tax. Pursuant to the freedom of establishment under the EC and EEA Treaty the benefits of the Merger Directive are also granted to reorganizations which involve comparable companies established in EEA states. (Central	EVL 52.2 § KVL 2007/38 KHO 2004:112

Tax Board's advance ruling 2007/38). According to case KHO 2004:112 of the Supreme Administrative Court, the principles of the Merger Directive as implemented into Finnish tax law was applied in the Finnish shareholder's taxation when two SICAVs established under Luxembourg law merged into each other.	

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
3.2 Transparent entities There is no express provision on classification of entities for the Finnish tax purposes. In practice, the classification of entities as non-transparent and transparent is made by comparing the company and civil law characteristics of a foreign entity with those of Finnish entities. The classification for the tax purposes in the state of residence of a foreign entity may also be taken into account. It is likely that none of the entities listed in the Annex be treated as being transparent for Finnish tax purposes, though this may be a matter of argument with the tax authorities.	N/A.

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency There are no specific rules in Finnish legislation governing the residence of companies. In practice, companies are considered to be residents of Finland if they are established in accordance with Finnish law and registered in the Trade Register in Finland (criterion of incorporation). Foreign companies are not deemed to be residents of Finland even if they are effectively managed from Finland. Under most DTCs concluded by Finland a company is considered to be a resident of the state where the place of its effective management is located. Therefore a Finnish company may become resident in another state due to the application of the DTC (KHO 2003:33 and KHO 2003:34). However, under its domestic law Finland does not deem foreign companies to be residents of Finland even if they are effectively managed from Finland.	N/A.

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>3.4 Subject-to-tax clause</u> The implementing law mentions that only companies subject to tax are covered by the implementing legislation. No administrative guidance has been issued.	EVL 52.2 §

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>3.5 Shareholder requirements</u> The Finish legislation does not limit the benefits of the Directive to such companies.	N/A.

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>4.1 The concepts of 'real values' and 'value for tax purposes'</u> Concepts of 'real values' and 'value for tax purposes' have not been specifically defined in the Finnish implementing legislation. Based on the general tax principles, the real value is regarded as the probable transfer value of the property between arm's length parties. The value for tax purposes corresponds to the depreciated acquisition value of the asset for tax purposes.	N/A.

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
<u>4.2 Specific guidance for divisions/partial divisions</u> No specific guidance has been issued.	N/A.

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>4.3 The concepts of 'effectively connected' and 'permanent establishment'</u> In cross-border transactions when the receiving company is resident in another Member State, EVL 52e § requires that the assets are effectively connected to its permanent establishment situated in Finland. If the receiving company does not have a permanent establishment in Finland, or if the assets thus transferred cease to be effectively connected to the permanent establishment, the difference between the fair market value and the tax book value of the items will be treated as taxable income in Finland. The term 'effectively connected' has not been further defined in Finnish tax law. Generally speaking, assets would be considered to be effectively connected as long as they are used in the business carried on in Finland and therefore generate income which is subject to Finnish tax laws. The definition of 'permanent establishment' is not specifically defined in the implementing legislation but a general definition is included in TVL 13a § and in the DTCs of Finland. The definitions in the DTC of Finland are mainly imported from the OECD Model Convention. The definitions of different tax treaties differ in detail from each other. The definition of the Income Tax Act differs in some respects from the DTC definition but is very similar to the definition of the DTCs . According to the Income Tax Act, a permanent establishment is a place in which a specific business is permanently conducted or there are special arrangements for carrying on business, such as: (a) where the management is located; (b) where there is a branch, office, industrial plant, production plant, workshop or shop; (c) where there is another kind of place for buying or selling purposes; (d) where there is a mine, quarry, fuel peat swamp, or gravel pit; or (e) in construction business, where such a business is largely carried on. The definition of the permanent establishment in Income Tax Act is not as detailed as that in the DTCs of Finland. For example, it does not contain specific rules regarding dependent agents, construction and installation projects or a negative list of activities that do not create a permanent establishment. However, despite the differences the definition in the Income Tax Act has in practice been interpreted in the way that it corresponds to the definition in the DTCs of Finland.	EVL 52e § TVL 13a §

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
<u>4.4 Limitation of the scope of relief</u> The national law does not establish any limitation on the scope of relief.	N/A.

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
<u>4.5 Assets and liabilities not effectively connected with a permanent establishment</u> EVL 52e § stipulates that if the receiving company does not have a permanent establishment in Finland, or if the assets thus transferred cease to be effectively connected to the permanent establishment, the difference between the fair market value and the tax book value of the items will be treated as taxable income. In case the assets later cease to be effectively connected to the permanent establishment, according to a general exit tax provision in EVL 51e § fair market value is included in income when any asset which is allocable to a permanent establishment in Finland ceases to belong to that establishment.	EVL 52e § EVL 51e §

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
<u>4.6 Tax treatment of shares of the receiving company</u> According to the EVL 52.1 § merger profit is not taxable income in Finland and respectively merger loss is not deductible expenditure for tax purposes even if the profit/loss could be allotted to shares of the receiving company.	EVL 52.1 §

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>4.7 Tax deferral</u> No account has been taken of the ECJ case law. Tax deferral is not possible.	N/A.

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities Please see 3.2.	N/A.

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief No further conditions. However see 11.1 concerning anti-abuse.	N/A.

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
5.1 The term 'provisions and reserves' There is no specific definition for 'provisions and reserves' in the implementing legislation. Generally speaking there are only a few provisions and reserves that can be made under Finnish tax laws and hence possibilities for companies to create new explicit untaxed reserves are limited. Below is a list of the most common reserves. In addition there are also a few specific reserves that can only be made by e.g. depository banks, credit and pension institutions and housing companies. (a) Replacement reserve Replacement reserve can be formed on the basis of a received insurance compensation or other consideration based on a damaging event to fixed assets or capital gain deriving of the sales of premises. The idea of the reserve is that the damaged fixed assets or transferred premises are replaced later with a similar one. (b) Guarantee reserve This reserve is allowed to taxpayers engaged in a qualifying construction, shipbuilding or metal industry for the anticipated costs arising from product guarantees. (c) Price fluctuation reserve If at the date of the balance sheet the replacement cost of inventory ordered but not yet received is at least 10% lower than the price agreed upon with the supplier, the excess of the agreed price over the	N/A. EVL 43 § EVL 47 § EVL 49 §

replacement cost may be charged against the current year's taxable income.	

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
<u>5.2 Exclusion of 'provisions and reserves' from permanent establishments</u> The distinction between provisions and reserves derived from a foreign permanent establishment and provisions and reserves of other permanent establishments or business divisions, or of the company as a whole has not been explicitly dealt with in the Finnish tax laws implementing the Directive and no further guidance has been issued. See also 10.3 for the recapture of reserves in the case where the transferred assets and liabilities include a permanent establishment of a Finnish company situated in another Member State.	N/A.

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
<u>5.3 Allocation method for provisions and reserves</u> According to EVL 52c.4 §, in a division and partial division, the transferring company's reserves, which are allocable to certain operations, are transferred to the entity which receives the operations. In a division other reserves are allocated to the receiving companies in the proportion the receiving companies receive the original company's net assets. In a partial division other reserves are allocated to the original company and receiving company in the same proportion that the original company's net assets are distributed. According to EVL 52d.1 and .3 §, a transfer of assets is a transaction where a company transfers all assets, liabilities and reserves relating to one or more branches of activity to a receiving company which continues the activity, in exchange for new shares in that company. Any reserves transferred in connection with a transfer of assets are entered as income in the books of the receiving company in the same way as they would have been entered as income in the books of the transferring company.	EVL 52c.4 § EVL 52d.1 and .3 §

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves No further conditions have to be met.	N/A.

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry-over of losses The concept of 'loss' has not been specifically defined for the purposes of implementing Article 6 of the Merger Directive. Generally speaking, if the business operations of a company yield a net loss, this tax loss may be carried forward for tax purposes and set off against future business profits. The loss can be carried forward for up to 10 tax years. There are some restrictions regarding the use of losses e.g. in the case of ownership change.	N/A.

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment Permanent establishments are treated in the same way as companies for the purposes of allocating losses. In cross-border mergers the losses of the merged company may be used by the permanent establishment remaining in Finland under the same conditions as if the acquiring company was a Finnish company. The acquiring company is entitled to deduct losses carried forward by the transferring company from its taxable income provided that the combined holdings of the acquiring company and its shareholders have exceeded 50% of the shares in the merged company since the beginning of the loss year.	TVL 123.2 §

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets According to TVL 123.1 § in a division or partial division the original company's sustained losses are attributed to the receiving company to the extent that it is evident that the losses are related to the activity transferred to the receiving company. Other losses are attributed to the receiving companies in the same proportion as the value of the net assets	TVL 123.1 § TVL 123a §

transferred to the latter. If the original company has several sources of income, any losses relating to the relevant source of income are allocated to the corresponding source of income for the receiving company. A transfer of assets is not a general succession and therefore the right to utilize sustained losses is not assigned to the receiving company. However, there is one exception to this rule relating to a conversion of a Finnish PE of an EU resident company into a Finnish corporation. Under TVL 123a §, if the entire permanent establishment of a company which is a resident of EU Member State is converted into a Finnish corporation, the latter may utilize the permanent establishment's sustained losses, subject, however, to the general rules governing the utilization of losses.	

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses No, the same limitation as in the wholly domestic context applies.	N/A.

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Amended holding threshold Under EVL 52b.1 § a merger gain is tax free, and a merger loss is not deductible in the hands of the receiving company. In this respect there is no minimum ownership requirement.	EVL 52b.1 §

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses Please see 7.1.	EVL 52b.1 §

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
<u>8.1 Avoidance of economic double taxation at the level of the shareholder</u> According to case law, in exchange of shares the shares received by the acquiring company are regarded to have been received at market value.	KHO 2002:81

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>8.2 Computation of the capital gain</u> No guidance but general capital gain tax principles are applied i.e. acquisition prices of the shares are deductible and sales prices are taxable.	N/A.

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>8.3 Further conditions for tax relief</u> Pursuant to EVL 52f.2 §, if a natural person who receives new shares in exchange of shares becomes resident abroad either according to Finnish domestic tax law or to an applicable DTC, within 3 years from the end of the year in which the exchange took place, the amount which escapes taxation through the application of EVL 52f, is treated as income in the year in which the person becomes resident abroad. This is likely to be incompliant with ECJ case law because the taxation is not realized at the moment of the actual disposal of shares, which is also the event which would trigger the capital gains taxation in a domestic context.	EVL 52f.3 §

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
9.1 Avoidance of economic double taxation at the level of the transferring company No avoidance of economic double taxation is provided. Pursuant to EVL 52d.4 § the acquisition costs for received shares is the difference between the cost base for tax purposes of the transferred assets less the amount of transferred debts and reserves. However, under the general participation exemption rules, the subsequent disposal of shares may be exempted from tax in which case no double economic taxation arises. The conditions for a tax exempt sale of shares are: the seller is not a venture capital company, shares belong to the seller's fixed assets, the seller owned at least 10% of the share capital in the company directly and continuously for at least 1 year. The shares in real estate companies do not qualify for the tax exemption.	EVL 52d.4 §

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
9.2 Further conditions for tax relief No such specific requirements exist. However, the benefits of the Merger Directive are subject to the anti-avoidance provision (please see 11.4).	N/A.

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
9.3 Tax deferral No account has been taken.	N/A.

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Loss recapture for permanent establishments in third Member States</u> Yes, the loss recapture rule was implemented and was effective from 1 January2007. Under TVL 123b § losses that have been deducted in the Finnish company's taxation are added back to the taxable income of the company to the extent that such losses have not been covered by subsequent profits of the permanent establishment. The add-back only covers the losses of the previous 10 tax years. The loss recapture rule does not apply in the case where the income of the permanent establishment is subject to the exemption method under an applicable DTC.	TVL 123b §

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> Finnish tax law implementing the Merger Directive does not distinguish between situations where the permanent establishment is or is not located in the same Member State as the receiving company so that both the situations should be equally covered by the Merger Directive.	N/A.

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> EVL 52e.3 § expressly states that if the transferred assets and liabilities are effectively connected with a permanent establishment of a Finnish company situated in another Member State, the difference between the fair market value and the book value of the assets, as well as reserves deducted from the permanent establishment's income, are treated as income in the hands of the transferring company. With respect to the Finnish tax due on this income, relief is granted for the amount of tax that, but for the provisions of the Merger Directive, would have been charged on	EVL 52e.3 §

the relevant income in the state in which the permanent establishment is located.	

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
10.4 Tax deferral No account has been taken of the ECJ case law. Tax deferral is not possible.	N/A.

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies EVL 52(2) § refers to Article 3a of the Merger Directive. The Finnish restructuring rules are applicable to all companies mentioned in the Annex of the Directive. The companies must be liable to corporation tax and have their fiscal residence in an EU Member State. The 'option right' has not been implemented in Finnish tax law. Based on the entity classification, it is unlikely that any of the entities covered by the Merger Directive would be treated as transparent for Finnish tax purposes (please see 3.2).	N/A.

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit Please see 10a.1.	N/A.

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit Please see 10a.1.	N/A.

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
<u>**10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders**</u> Please see 10a.1.	N/A.

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
<u>**10a.5 Comparison with a resident fiscally transparent company**</u> Please see 10a.1.	N/A.

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
<u>**10b.1 Exit taxation**</u> Prior to the implementation of the SE Statute, it was not possible for a Finnish limited liability company to transfer its registered office to another country. In terms of tax residence, Finnish tax laws employ the place of incorporation as the sole criterion for establishing tax residency in Finland. EVL 52g § states that a transfer of registered office of an SE or an SCE does not give rise to capital gains taxation to the extent that the assets remain effectively connected to a permanent establishment in Finland. Under EVL 52g.2 § in conjunction with EVL 52e.2 §, to the extent the SE does not have a permanent establishment in Finland, or if the transferred assets cease to be effectively connected to the permanent establishment, the difference between the fair market value and the book value of the items will be treated as taxable income. No account has been taken of the ECJ case law regarding the exit taxation. Tax deferral is not possible.	EVL 52g §, EVL 52g.2 §, EVL 52e.2 §

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
<u>**10b.2 The term 'head office'**</u> The term 'head office' has been translated into Finnish tax law as '*sääntömääräinen kotipaikka*' ('registered office'). The term is not further defined in tax laws. However, in company law the registered office means the place of residence as mentioned in the Articles of association of a Finnish company.	EVL 52g §

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
<u>**10b.3 Head office and tax residency**</u> Yes, under Finnish tax laws only companies incorporated under Finnish law are treated as having their tax residence in Finland. Finnish DTCs with the other Member States generally follow Article 4 (3) OECD Model Convention stating that a person principally resident in both Contracting States shall be deemed to be a resident only of the State in which its place of effective management is situated. This may result that for DTC purposes a company incorporated in Finland may have its residency in the other contracting States but not vice versa.	TVL 9.1 §

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>**10b.4 Assets and liabilities not effectively connected with a permanent establishment**</u> Under EVL 52g.2 § in conjunction with EVL 52e.2 §, to the extent the SE does not have a permanent establishment in Finland, or if the transferred assets cease to be effectively connected to the permanent establishment, the difference between the fair market value and the book value of the items will be treated as taxable income.	EVL 52g.2, EVL 52e.2 §

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the '*N*' case?	Reference
10b.5 Tax deferral No account has been taken of the ECJ case law. Tax deferral is not possible.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 The term 'comparable circumstances' EVL 52g.2 § lays down the principle of continuity in that the transfer of a registered office of an SE/SCE does not have an impact on depreciations, reserves, losses etc. It expressly states that such deductions may be made as if the registered office were not transferred out of Finland's jurisdiction.	EVL 52g.2 §

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Loss recapture for permanent establishments TVL 123b § providing for the recapture of losses applies also to the transfer of a registered office of an SE/SCE (please see 10.1).	TVL 123b §

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
10d.1 Deemed liquidation The transfer of registered office of an SE/SCE should not of itself give rise to a deemed liquidation.	N/A.

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
10d.2 Tax treatment of third country residents Also Finland would not generally have the taxing right to capital gains on shares disposed by non-resident shareholders.	N/A.

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how'?	Reference
11.1 Transposition of anti-abuse provisions EVL § 52h incorporates Article 11(1)(a) of the Merger Directive. It states that EVL 52-52f § do not apply if it is evident that the sole or one of the principal objectives of the transaction is tax avoidance or tax evasion.	EVL 52h §

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
11.2 General anti-abuse provision In addition to anti-abuse provision referred to in 11.1, Finnish tax law includes a general anti-avoidance clause (VML 28 §) which is based on the substance-over-form principle. However, the prevailing view is that the specific anti-avoidance provision takes precedent over the general one.	VML 28 §

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the '*Cadbury*' judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' No express steps have been taken, though the interpretation of EVL 52h § generally comes close to the concept of wholly artificial arrangements and might be affected by the ECJ case law. The 'Cadbury' judgment also resulted in changes of applicable Finnish CFC-rules. The proposal for legislative amendments to CFC-rules has been	N/A.

issued by the government and amendments are scheduled to take effect as from 1.January 2009. Under the amendments CFCs in EU and EEA countries (with the exception of Liechtenstein due to lack of effective information exchange) will always be exempted from the scope of the rules provided that they are actually established in their residence state and carry on there genuine business activities. The same principles are also applied to non-EU or non-EEA countries provided that a country is not listed in a so-called black list due to low general level of taxation and that there is sufficient information exchange between Finland and the country in question.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions No such further restrictions and conditions have been imposed. However, continuity of ownership and business requirements may be taken into account when establishing whether the transaction has valid commercial reasons or constitute tax avoidance or tax evasion. There is no unambiguous definition for 'business requirements' but this depends on the specific facts and circumstances. For example preparation of a company acquisition, risk management and synergy benefits have been considered as acceptable business requirements for different transactions.	KHO 1999:63, KHO 1999:3080

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' The concepts 'restructuring' and 'rationalization' have not been addressed in this context. The principle is that a company reorganization should have valid commercial reasons, in addition to the possible tax reasons, in order for the beneficial tax treatment as provided for by the Merger Directive to apply. See also answer to 11.4.	N/A.

Which party has the initial burden of proof to establish the existence or absence of ‘valid commercial reasons’?	Reference
<u>11.6 Burden of proof</u> The initial burden of proof to establish that the tax benefits provided for by the Merger Directive may be denied under the anti-avoidance provision is on the tax authorities. However, once challenged the taxpayer must demonstrate that there are valid commercial reasons for the transaction. The taxpayer may also apply for a binding advance ruling as whether the tax benefits provided for by the Merger Directive are applied to a contemplated transaction.	N/A.

FRANCE

Abbreviations

English	French	English	French
FTC	CGI	French Tax Code	Code Général des Impôts
BOI	BOI	Administrative Guidelines	Bulletin Officiel des Impôts
DB	DB	General Administrative Guidelines	Documentation de Base
RM	RM	Reply by the Minister	Réponse Ministérielle
CRC	CRC	French Accounting Regulations Committee	Comité de la Réglementation Comptable
SIF	FCP	specialised investment funds	Fonds commun de placement
ICVC	SICAV	Investment Company with Variable Capital	Société d'Investissement à Capital Variable
UCITS	OPCVM	Undertakings for Collective Investments in Transferable Securities	Organismes de Placement Collectif en Valeurs Mobilières

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
Overall state of implementation The Merger Directive 90/434/CEE, dated 23 July 1990, has been implemented into French legislation by Article 25 of the Amended Finance Bill for 1991 (Law n°91-1323, 30 December 1991), which has adapted the existing regulations enacted by Articles 15 to 17 of the Law n°65-566, 12 July 1965. Those new rules have been commented in the administrative guidelines 4 I-1-93, dated 11 August 1993. The Finance Bill for 1995 (Law n°94-1162, 19 December 1994, Article 28) has modified Section 210 B of the FTC in order to extend the favourable tax merger regime to divisions realized on 1 January 1995 and after. The Finance Bill for 2000 (Law n°99-1172, 30 December 1999, Article 22) has modified the conditions set out in Section 210 B of the FTC under which a transfer of assets and a division may benefit from the favourable tax merger regime. The new rules introduced in 1995 and 2000 have been commented in the administrative guidelines 4 I-2-00, dated 3 August 2000. The Finance Bill for 2002 (Law n°2001-1275, 28 December 2001, Article 85) has introduced in the French tax code the Section 210-0 A which defines the operations that may benefit from the favourable tax merger regime on the basis of the definitions set out in the Merger Directive, thus allowing operations defined in Section 1844-5 of the French Civil Code whereby, in case of dissolution of a company which shares are detained by a sole shareholder, all its assets and liabilities are transferred to its shareholder without liquidation, to benefit from the favourable tax merger regime. Furthermore, the existing rules have been modified in respect of the neutralization of the operations at the level of the shareholders, the transfer of carried-back and carried-forward losses of the transferring company to the receiving company, the assimilation of certain transfer of shares to transfer of assets to transfer of shares. Those new rules applied to operations realized on 1 January 2002 and after. The new rules introduced in 2002 have been commented in the administrative guidelines 4 I-2-02, dated 25 October 2002, administrative guidelines 13 D-2-02, dated 21 August 2002, in respect of the transfer of losses, and, administrative guidelines 13 D-1-03, dated 2 June 2003, in respect of the ruling required in case a transferring company transfers the shares received in exchange for the transfer of assets and liabilities to its shareholders, which have been completed by administrative guidelines 13 D-1-06 dated 10 February 2006. The Amended Finance Bill for 2004 (Law n°2004-1485, 30 December 2004, Article 42) have modified the existing favourable tax merger regime. Those new provisions have been commented in administrative guidelines 4 I-1-05, dated 30 December 2005. Finally, the Finance Bill for 2005 (Law n°2004-1484, 30 December 2004, Article 34) has implemented the provisions of the Directive 2005/19/EC of 17 February 2005 relating to the transfer of the registered office of Societas Europea (SE) or European Cooperative Societies (SCE). The new provisions set out in Section 221-2 of the French Tax Code have been commented in draft administrative guidelines which have never been published.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>**1.1 Involved companies**</u> The term 'companies involved' has been interpreted as encompassing only the 'merging' companies. Indeed, pursuant to Section 210-0 A, paragraph 2, of the FTC, the favorable tax merger regime may not apply to mergers, divisions or transfers of assets realized by a company, acting either as the transferring company or as the receiving company, whose head office is located in a non-EU country with which France has not concluded a double tax treaty including an administrative assistance clause. Commenting these provisions, administrative guidelines 4 I-2-02 precise that such geographical restriction only applies to the merging companies, and not to the shareholders which would reside in the excluded countries.	FTC, Section 210-0 A BOI 4 I-2-02, n°19-25

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
<u>**1.2 Foreign Member State and third state merger**</u> According to administrative guidelines 4 I-2-02 which comments Section 210-0 A of the FTC, the mergers or divisions which may benefit from the favorable tax merger regime are the operations, realized in France or abroad, whereby: (a) the transferring company is dissolved without liquidation, (b) all its assets and liabilities are transferred, (c) shares of the receiving company / companies are issued in exchange for shares of the transferring company, and (d) there is no cash payment exceeding 10% of the nominal value of the shares of the receiving company / companies. Pursuant to Section 210-0 A, para. 2, of the FTC, the favorable tax merger regime may not apply to mergers, divisions or transfers of assets realized by a company, acting either as the transferring company or as the receiving company, whose head office is located in a country with which France has not concluded a double tax treaty including an administrative	FTC, Section 210-0 A FTC, Section 210 A BOI 4 I-2-02, n°19-25

assistance clause. However, this restriction does not apply to operations that are within the scope of the Merger Directive. Hence, as stated in administrative guidelines 4 I-2-02, the favorable tax merger regime may apply to: (a) operations realized by French companies; (b) operations realized by companies from one or several Member States; (c) operations realized by companies whose head office is located in a country with which France has concluded a double tax treaty including an administrative assistance clause. Please note that from a practical point of view, due to the territoriality principle applied by French legislation, French tax merger rules would apply to operations involving two foreign companies if the transferring company has a permanent establishment located in France which is part of the transaction, or in respect of French tax resident shareholders of the transferring company.	

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
<u>**2.1 The term 'securities'**</u> According to administrative guidelines 4 I-2-02, the securities, which may result from a capital increase or a distribution of shares of treasury stock, must represent the capital of the receiving company. Hence, the following securities are excluded: securities representing debts, convertible bonds, bonds redeemable in shares, equity warrants, etc… In case non qualifying securities are exchanged, they are deemed to constitute a part of the cash payment for the determination of the threshold of 10% of the nominal value of the shares.	BOI 4 I-2-02, n°16-18

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
<u>**2.2 The term 'cash payments'**</u> As a preliminary remark, we draw your attention that the French favourable tax merger regime may apply to both reorganizations at book value and reorganizations at real value (please refer to our comments under 4.1 for more details).	FTC, Section 210-0 A BOI 4 I-2-00, n°64 BOI 5 G-10-92, n°25

With regards to mergers, divisions and exchange of shares, French domestic legislation and administrative guidelines provide for the possibility to allow a cash payment not exceeding 10% of the nominal value of the shares received in exchange for the shares of the transferring company. As stated in administrative guidelines 5 G-10-92, this requirement must be appreciated on a per shareholder basis. It should be noted that administrative guidelines 5 G-10-92 and 5 B-12-92 state that in the absence of a nominal value for the securities issued in exchange, the cash payment threshold would be determined by reference to the accounting par value of those securities, defined as the amount of paid capital divided by the number of securities issued. With regards to transfer of assets, the administrative guidelines provides for the possibility to allow a cash payment not exceeding the value of one share of the receiving company (BOI 4 I-2-00, n°64).	BOI 5 B-12-92, n°12

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
<u>**2.3 Further types of merger**</u> As listed in Article 2(a) of the Directive, the favourable tax merger regime applies to the following operations: As a consequence, as confirmed in administrative guidelines 4 I-2-02 and 4 I-1-03, operations defined in Section 1844-5 of the French Civil Code whereby, in case of dissolution of a company which shares are detained by a sole shareholder, all its assets and liabilities are transferred to its shareholder without liquidation may benefit from the favourable tax merger regime. Furthermore, it should be noted that administrative guidelines 5 G-10-92 and 5 B-12-92 state that in the absence of a nominal value for the securities issued in exchange, the cash payment threshold would be determined by reference to the accounting par value of those securities, defined as the amount of paid capital divided by the number of securities issued. Finally, the favourable tax merger regime may also apply, if agreed by the French tax authorities, to operations realized by companies resident in other Member States which differ from the operations as defined in the Merger Directive and French legislation but are subject in the relevant Member State to an equivalent favourable tax merger regime (e.g. merger operations realized in the United Kingdom by way of an arrangement under Section 110 of the Insolvency Act 1986, whereby the transferring company goes into voluntary liquidation and the liquidator transfers its assets to the receiving company in exchange for shares).	FTC, Section 210-0 A BOI 4 I-2-02 BOI 4 I-1-03 BOI 5 G-10-92, n°27 BOI 5 B-12-92

<table>
<tr><td>The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority.

In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?</td><td>Reference</td></tr>
<tr><td><u>2.4 Qualifying exchange of shares</u>

<u>2.4.1. Domestic legislation</u>

Article 2(d), as amended by Directive 2005/19/EC has not been per se implemented into French domestic legislation which was considered as already compliant. However ‘exchange of shares’ are not defined as such in French legislation but are considered as transfers of assets.

Indeed, pursuant to Section 210 B of the FTC, under certain conditions, the following operations may benefit from the favourable tax merger regime since they are deemed to constitute a transfer of a complete branch of activity:

(a) the transfer of securities representing more than 50% of the capital of a company;

(b) the transfer of securities providing the acquiring company with the direct holding of more than 30% of the voting rights when no other shareholder detains, directly or indirectly, more voting rights;

(c) the transfer of securities providing the acquiring company, which already detains more than 30% of the voting rights, with the most important share of voting rights in the company.

Hence, the national legislation only grants relief in respect of concomitant transfers of securities that finally lead to the holding of a voting rights share which is both superior than 30% and the most important voting rights share in the company.

In case the acquiring company already holds more than 50% of the capital of the company, the transfers of securities aiming at increasing its holding may only benefit from the favourable tax merger regime if authorized by the French tax authorities.

<u>2.4.2 Conclusion</u>

With regards to exchange of shares, the French legislation may be regarded as not complying with the Merger Directive insofar as the consolidation of an existing majority may not benefit from the favourable tax merger regime without a prior ruling of the French tax authorities.</td><td>FTC, Section 210 B

BOI 4 I-2-02</td></tr>
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With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>**2.5 Consolidation of qualifying holding**</u> Since the transfer of securities that aims at consolidating an existing majority of voting rights does not constitute a transfer of a complete branch of activity under French legislation, such transfer may only benefit from the favorable tax merger regime if authorized by the French tax authorities. Pursuant to Section 210 B of the FTC, such prior ruling would be granted if: (a) the operation is justified by economical reasons; (b) the operation is not motivated by fraud or tax evasion; (c) the operational modalities ensure the future taxation of the latent capital gains. Furthermore, as for other transfers of a complete branch of activity, the transferring company must commit itself to (i) hold the shares received in exchange for a three years period and (ii) calculate the capital gains deriving from the disposal of those shares on the basis of their value for tax purposes as recorded in own accounts at the time of the transfer. As previously mentioned, the French legislation may be regarded as not complying with the Merger Directive insofar as the consolidation of an existing majority may not benefit from the favourable tax merger regime without a prior ruling of the French tax authorities. Furthermore, the additional requirement that the transferring company commits itself to hold the shares for three years may be regarded as not complying with the Merger Directive. Indeed, such requirement may be considered as disproportionate to the objectives set out in Article 11(1)(a) since it also applies to operations which do not have as principal objective tax evasion or tax avoidance and less restrictive measures might be implemented to ensure the future taxation of the latent capital gains (e.g. declarative obligations).	FTC, Section 210 B

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 *'Andersen og Jensen'*. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>**2.6 The term "branch of activity"**</u> The French Tax Code does not define the term "branch of activity" which has been defined by administrative guidelines and French courts.	BOI 4 I-1-93, n°40-41 BOI 4 I-2-00, n°47-75 BOI 4 I-1-01, n°5-7

2.6.1 Characterization of a "branch of activity"

Administrative guidelines 4 I-1-93, which refers to Article 2(i), and administrative guidelines 4 I-2-00 define the term "branch of activity" as "all the assets and liabilities of a division of a company which from an organizational point of view constitute an independent business, that is to say an entity capable of functioning by its own means".

This definition has been further detailed by administrative guidelines 4 I-2-00. In order to be characterized as a branch of activity, the transferred activity must constitute (i) an organization independent from the others company divisions in respect of clientele, facilities and equipment, staff, administration (internal independency criterion) and (ii) an organization capable of functioning by its own means in normal conditions (external independency criterion).

The French tax authorities and the French courts require that these conditions are fulfilled at both the level of the receiving company and the level of the transferring company at the date of realization of the operation and also at its date of effectiveness (e.g. retroactive date). For instance, the French Supreme Administrative Court has decided that the ability to function by its own means which characterized a branch of activity must be appreciated at both the level of the receiving company and the level of the transferring company (CE, 27 July 2005, n°259052, Sté BL; CAA Bordeaux, 20 March 2003, n°98-1690).

Such requirement may not be consistent with the ECJ interpretation of the Directive. Indeed, in the *Andersen og Jensen* decision, the ECJ seems to not require that the transferred assets constitute an independent business at the transferring company level but only at the receiving company level.

It should be noted that, in case the transferred assets and liabilities do not fulfil the conditions to be characterized as a branch of activity, the favourable tax merger regime may nonetheless be granted by way of a prior ruling by the French tax authorities. However, in such a case, the French rules, as interpreted by the French tax authorities and the French tax courts, may be regarded as not compliant with the Merger Directive as interpreted in the *Andersen og Jensen* decision since the prior ruling requirement constitutes a disproportionate administrative burden.

2.6.2 Determination of the assets and liabilities attached to the "branch of activity"

The French tax authorities have also provided some guidance on the assets and liabilities to be transferred, softening the rule according to which all the assets and liabilities directly or indirectly attached to the branch of activity must be transferred.

With regards to the transfer of liabilities, the guidelines precise that:

(a) the transfer of liabilities non attached to the branch of activity is considered as a cash payment;

(b) the favourable tax merger regime may nonetheless apply in such case when the cash payment does not exceed the value of one

share representing the capital of the receiving company; (c) all the liabilities attached to the branch of activity should normally be transferred (however, the French tax authorities accept that some liabilities may not be transferred with the branch of activity if (i) these liabilities are not directly and exclusively attached to the branch of activity and (ii) there is no economical or legal reason for the transfer). With regards to the transfer of assets, the guidelines precise that : (a) the transferring company may retain the ownership of the buildings (business premises, administrative premises) attached to the branch of activity if a right to use the buildings is granted to the receiving company, allowing it to exploit independently and for a long period the transferred branch of activity (from a practical point of view, based on previous experiences, the French tax authorities are very reluctant to grant a ruling when industrial buildings are not transferred within the branch of activity); (b) in case the brands used for the commercialization of the products of the transferred branch of activity are also used for other branches of activity or subsidiaries of the transferring company, this company may retain the ownership of those brands but should grant the receiving company the right to use those brands for a minimum period of 10 years; (c) if the common administrative services must be affected between the several branches of activity, assets and liabilities attached to these common administrative services may not be split between the several branches of activity and may not be transferred.	

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
3.1 Types of entities Pursuant to Section 210 C of the FTC, the favourable tax merger regime applies to operations realized by legal entities subject to the French corporate income tax. Furthermore, as stated in administrative guidelines 4 I-2-02 which comments Section 210-0-A of the FTC, the favourable tax merger regime may apply to operations realized by French companies, operations realized by companies from one or several Member States and operations realized by companies whose head office is located in a country with which France has concluded a double tax treaty including an administrative assistance clause. Hence, French legislation does not refer to any limitative list of types of entities. With regards to French entities, the favourable tax merger regime may apply, if certain conditions are fulfilled, to operations realized between	FTC, Section 210 C BOI 4 I-2-02

FCPs and SICAVs and operations involving real estate UCITS, which are not listed in the Annex.	

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
3.2 Transparent entities Please note that French legislation does not recognize the concept of tax transparency but recognizes a semi-transparency concept (or translucency concept) in which the amount of taxable income is determined at the level of the entity but the tax is calculated at the level of its partners on the amount of taxable income attributed in proportion of their rights. Furthermore, such semi-transparent entities which have opted for the corporate income tax may benefit from the favourable tax merger regime (please refer to our comments under 3.4). In order to determine the tax treatment of income derived through a transparent entity, French tax authorities usually rely on a legal analysis of the transparent entity and its comparability to similar French entities, especially in regards of the partners' responsibilities. For instance, for treaty purposes, French tax authorities determine whether or not the foreign partnership qualifies as a resident for treaty purposes by reference to French domestic law by comparing the foreign partnership to French entities by reference to company law criteria (e.g. (un)limited liability of the partners). The foreign entity is then treated for tax purposes similarly to the comparable French entity. It should be noted that this position of the French tax authorities has been recently modified. Administrative guidelines 4 H-5-07, introduces, under certain conditions, the recognition of the transparency approach for French-source passive income (dividends, interest and royalties) derived by foreign and French-resident partners of a foreign partnership. Accordingly, France waives in certain situations the comparison method under which the foreign partnership is classified by reference to French entities: for the purposes of these guidelines, foreign partnerships are defined as foreign entities treated as transparent for tax purposes in the country where they are established. However, this new approach only applies in respect of tax treaty provisions and not in respect of domestic regulations and thus does not affect the domestic regulations implementing the Merger Directive. Hence, for the purposes of provisions implementing the Merger Directive, the French tax authorities still rely on the comparison method. However, to the best of our knowledge, the French tax authorities do not regard any of the entities listed in the Annex as transparent.	FTC, Section 8 BOI 4 H-5-07

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
<u>3.3 Qualification of tax residency</u> <u>3.3.1 Domestic law</u> With regards to the taxation of legal entities, Section 205 of the FTC provides that the French corporate income tax applies to the benefits and income realized by legal entities mentioned in Section 206 of the FTC, such as 'sociétés anonymes', 'sociétés en commandite par actions', 'sociétés à responsabilité limitée' which have not opted for the partnership tax regime, and legal entities with for-profit activities. Hence, from a practical point of view, such legal entities which are registered in France are liable to tax in France. Furthermore, pursuant to Section 209 of the FTC, French corporate income tax apply to benefits realized by an organization exploited in France ('territoriality principle') and to benefits attributed to France by application of a tax treaty provisions. The concept of 'organization exploited in France', which is not defined by the law, has been defined by French case law as: (a) establishments located in France, defined as a permanent and independent facilities (e.g., plant, branch, etc.); (b) agent; (c) operations representing a complete commercial process. <u>3.3.2 Double tax treaties</u> With regards to legal entities, due to the territoriality principle applied into French legislation, the most common residence tiebreaker criterion used in double tax treaties concluded by France is the 'permanent establishment' criterion.	FTC, Section 205 FTC, Section 206 FTC, Section 209

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>3.4 Subject-to-tax clause</u> The 'subject-to-tax' clause has been implemented in the provisions of Section 210 C of the FTC. However, whereas Article 3(c) of the Merger Directive excludes companies which are subject to tax by way of an option or tax liable companies which benefit from a tax-exemption, Section 210 C of the FTC provides that the favourable tax merger regime applies to operations realized by legal entities <u>liable</u> to corporate income tax. Hence, the favourable tax merger regime also applies to operations involving legal	FTC, Section 210 C DB 4 I-1242

entities benefiting from a corporate income tax exemption or legal entities subject to corporate income tax by way of an option. Furthermore, the favourable tax merger regime may apply to operations realized by entities which are not subject to corporate income tax on all their income. For instance, the favourable tax merger regime may apply to 'sociétés coopératives agricoles' or 'sociétés en commandite par actions' (limited liability partnership with shares) whatever the portion of their results subject to corporate income tax is.	

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>**3.5 Shareholder requirements**</u> French legislation does not limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents.	FTC, Section 210 C

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>**4.1 The concepts of 'real values' and 'value for tax purposes'**</u> <u>4.1.1. Overview of the accounting treatment of the transfer of assets and liabilities</u> For operations realized on January 1, 2005 and after, the assets and liabilities must be booked in the receiving company accounts in accordance with accounting regulations (CRC Regulation 2004-04): (a) the assets and liabilities must be booked at accounting value where the operation is realized (i) between companies controlled by the same company, (ii) between a company and its controlling company, or (iii) operations realized between companies under distinct control by which the principal shareholder of the transferring company takes control of the receiving company (reverse merger); (b) the assets and liabilities must be booked at real value where the operation is realized between companies under distinct control by which the principal shareholder of the receiving company keeps its control. These rules aimed at reinforcing the credibility of companies' accounts by suppressing the possibility for companies realizing a merger to opt for either the booking of the assets and liabilities at the accounting value or the booking at the real value.	FTC, Section 210 A

As mentioned in the notice 2005-C enacted by the Urgent Committee of the French accounting regulator (CNC), those rules only apply for operations whereby the receiving company is a French entity. As a consequence, since a permanent establishment is not considered as a legal entity distinct from the foreign company, those accounting rules do not apply to the transfer of assets and liabilities by way of a merger, a division or a transfer of assets, by a French company to the permanent establishment in France of a foreign company. In such cases, with regards to the French regulations, the operation may be booked at either the accounting value or the real value. However, in practice, the operation would be booked accordingly to the rules applicable in the country of establishment of the foreign company.

4.1.2. Overview of the tax treatment of the transfer of assets and liabilities

Pursuant to Section 210 A of the FTC, the net capital gains relating to the transfer of the assets of the transferring company are not taxed at the time of the merger.

Hence, from a practical point of view, the taxation of those capital gains, constituted by the difference between the real value of the transferred assets at the time of the merger and their value for tax purposes as recorded in the transferring company accounts, is postponed until the disposal of those assets by the receiving company.

This favourable tax treatment may apply to both operations realized at accounting value and operations realized at real value. Hence, as a result of the disconnection between accounting rules and tax rules in respect of mergers and acquisitions (CE, 8 June 2005, n°270967, SAS Sofinad), the tax deferral is not subordinated to a specific accounting treatment. However specific rules apply in case the operation is realized at real value.

4.1.2.1 Operations realized at accounting value

In case the operation is realized at accounting value, the receiving company must register in its accounts (i) the transferred assets and liabilities at their book value as recorded in the transferring company accounts and (ii) the amortizations and depreciations as recorded in the transferring company accounts.

Further capital gains to be realized by the receiving company on the disposal of transferred assets must be calculated as the difference between their sale price and their value for tax purposes as registered in the accounts of the transferring company at the time of the merger.

Most often, the value for tax purposes equals to the net accounting value. It may however be lower in cases where the assets have been previously transferred by way of a merger realized at real values which benefited from the favourable tax merger regime.

4.1.2.2 Operations realized at real value

(a) Non-amortizable fixed assets

Further capital gains to be realized by the receiving company on the sale of non-amortizable assets should be calculated as the difference between the sale price and the value for tax purposes, as previously defined (DB 4 I-1242, n°62-63). (b) Amortizable fixed assets Since the assets and liabilities transferred to the receiving company are booked at real value, the amortization of amortizable fixed assets would be calculated on the basis of their real value at the time of the transfer. Pursuant to Section 210 A, para. 3-d, of the FTC, the receiving company must reintegrate in its taxable income the capital gains resulting from the transfer of amortizable fixed assets of the transferring company which have not been taxed at the level of the transferring company. The reintegration of those net capital gains must be realized over a 5 years period (or 15 years for buildings, fixtures, installations, land improvements, plantations, or the average duration of amortizations if 90% of more of the capital gains relates to buildings). Furthermore, in case of a sale of such asset before the completion of the reintegration, the part of the capital gain which has not been reintegrated yet is taxable (DB 4 I-1242, n°52). Those rules tend to compensate for the amortization provided by French accounting rules of assets received on the basis of their real value at the time of the transfer, so that operations realized at real value may comply with the provisions of Articles 4(3) and 4(4) of the Merger Directive and may benefit from the favourable tax merger regime. (c) Current assets Pursuant to Section 210 A, para. 3-e, of the FTC, the capital gains resulting from the transfer of current assets of the transferring company are neutralized if the receiving company registers in its accounts those assets at their value for tax purposes as recorded in the accounts of the transferring company. Since this condition cannot be fulfilled from an accounting point of view in case of an operation realized at real value, those capital gains must be included in the taxable income of the receiving company (BOI 4 I-1-05, n°17-18). Hence, French legislation may be regarded as non compliant with the Merger Directive insofar as the capital gains resulting from the transfer of current assets in case of an operation realized at real value are immediately taxed and do not benefit from the favourable tax merger regime. <u>4.1.3. Concept of ‘real value’</u> The concept of ‘real value’ of an asset is defined into French regulations as the value estimated for the purpose of the contemplated operation on the basis of both its ‘market value’ and its ‘usefulness value’ for the receiving company (CRC Regulation 2004-01, para. 4-4; BOI 4 I-1-05 n°35). For tax purposes, the ‘market value’ may be defined as the price at which the asset may be sold at the time of the contemplated operation under normal market conditions. The ‘usefulness value’ of an asset may be	

defined as the value of the economical benefits awaited from its use or its disposal (PCG, Article 322-1, para. 11). 4.1.4. Concept of 'value for tax purposes' The concept of 'value for tax purposes' of an asset is defined into French legislation as the gross accounting value, less tax deductible depreciations and amortizations. For acquired assets, the gross accounting value equals to the acquisition costs, defined as the acquisition price plus ancillary costs. For self-product assets, the gross accounting value equals to the acquisition costs of the materials and supplies consumed for production, plus related direct, plus a share of related indirect costs.	

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions With regards to divisions and transfer of assets, the main issue is the determination of the branch of activity. Indeed, pursuant to Section 210 B of the FTC, the favourable tax merger regime should apply if the division or transfer of assets relate to a complete branch of activity. However, from a practical point of view, in order to secure the tax treatment of the operation and avoid any calling into question by the French tax authorities of the applicability of the favourable tax merger, it is usual and necessary to require a prior validation from the French tax authorities. Indeed, since the transfer should relate to all the assets and liabilities relating to the branch of activity but only such assets and liabilities, the existence of accounts common to several activities require such validation. It should be noted that the French tax authorities do not consider that an activity consisting solely in holding shares or real estate may constitute a branch of activity.	FTC, Section 210 B

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' Pursuant to Section 210 C of the FTC, the favourable tax merger regime may apply to the transfer of assets by way of a merger, a division or a transfer of assets realized by French legal entities to foreign legal entities only if a prior ruling is granted by the French tax authorities. As set out in Section 210 B, such ruling would be granted if (i) the operation is justified	FTC, Section 209

by economical reasons, (ii) the operation is not motivated by fraud or tax evasion and, (iii) the operational modalities ensure the future taxation of the latent capital gains (please refer to our comments under 11.1.1 for more details on the issue of the compliance of these requirements with the Merger Directive). In order to comply with this last requirement, the transfer of assets to a foreign company by way of a merger, a division or a transfer of assets must be allocated to a French permanent establishment of the foreign company. With regards to the concept of permanent establishment, since the allocation of the transferred assets and liabilities aims at ensuring the future taxation of the latent capital gains, such concept must be interpreted by reference to both the territoriality principle as defined in Section 209 of the FTC and the permanent establishment concept defined in the relevant tax treaties. Indeed, according to Section 209 of the FTC, French corporate income tax apply to benefits realized by an organization exploited in France ('territoriality principle') and to benefits attributed to France by application of a tax treaty provision. The concept of 'organization exploited in France', which is not defined by the law, has been defined by French case law as establishments located in France, defined as permanent and independent facilities (e.g., plant, branch, etc…), agents and operations representing a complete commercial process. With regards to the concept of 'effectively connected', such concept has not been defined and the application of the favourable tax merger regime relates, from a practical point of view, on the recording of the transferred assets and liabilities in the balance sheet of the French permanent establishment of the foreign receiving company. Hence, transferred assets and liabilities by way of an operation for which a prior ruling has been granted would benefit from the favourable tax merger regime insofar as those assets and liabilities remain registered in the balance sheet of the French permanent establishment of the foreign receiving company, even if they are not effectively connected (e.g. shares of subsidiaries) so that further taxation in France remains possible.	

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
<u>4.4 Limitation of the scope of relief</u> In cases where the operation is realized at book value, there is no limitation of the scope of relief. In cases where the operation is realized at real value, as previously mentioned under Question 4.1, the receiving company is required to reintegrate in its taxable income the capital gains resulting from the transfer of amortizable fixed assets of the transferring company which have not been taxed at the level of the transferring company (Section 210	FTC, Section 210 A

A, para. 3-d, of the FTC). The reintegration of those net capital gains must be realized over a 5 years period (or 15 years for buildings, fixtures, installations, land improvements, plantations, or the average duration of amortizations if 90% of more of the capital gains relates to buildings). Furthermore, in case of a sale of such asset before the completion of the reintegration, the part of the capital gain which has not been reintegrated yet is taxable (DB 4 I-1242, n°52). Those rules tend to compensate for the amortization provided by French accounting rules of assets received on the basis of their real value at the time of the transfer, so that operations realized at real value may comply with the provisions of Articles 4(3) and Article 4(4) of the Merger Directive and may benefit from the favourable tax merger regime.	

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
<u>**4.5 Assets and liabilities not effectively connected with a permanent establishment**</u> Pursuant to Section 210 C of the FTC, the favourable tax merger regime may apply to the transfer of assets by way of a merger, a division or a transfer of assets realized by French legal entities to foreign legal entities only if a prior ruling is granted by the French tax authorities. As set out in Section 210 B, such ruling would be granted if the operation is justified by economical reasons, the operation is not motivated by fraud or tax evasion and, the operational modalities ensure the future taxation of the latent capital gains (please refer to our comments under 11.1.1 for more details on the issue of the compliance of these requirements with the Merger Directive). In order to comply with this last requirement, the transfer of assets to a foreign company by way of a merger, a division or a transfer of assets must be allocated to a French permanent establishment of the foreign company. From a practical point of view, transferred assets and liabilities by way of an operation for which a prior ruling has been granted would benefit from the favourable tax merger regime insofar as those assets and liabilities remain registered in the balance sheet of the French permanent establishment of the foreign receiving company. Transferred assets and liabilities which are not registered in the balance sheet of the French permanent establishment would be subject to immediate taxation of the relating capital gains.	FTC, Section 210 A FTC, Section 210 B FTC, Section 210 C

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company Pursuant to Section 210 A of the FTC, the capital gain relating to the cancellation of the shares of the transferring company detained by the receiving company is not taxed.	FTC, Section 210 A

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral To the best of our knowledge, the case law of the ECJ relating to the deferral of taxation, in particular the judgment in Case C-470/04 *'N'* has not been taken into account into French legislation (please refer to our comments under 10b.5 for more details).	

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities Article 4(2) of the Merger Directive has not been *per se* implemented into French legislation. Indeed, as previously mentioned, French legislation does not recognize the concept of tax transparency but recognize a semi-transparency concept (or translucency concept) in which the amount of taxable income is determined at the level of the entity but the tax is calculated at the level of its partners on the amount of taxable income attributed in proportion of their rights. Hence, French legislation does not provide as such any legal basis for the implementation of Article 4(2) of the Merger Directive. Furthermore, French tax authorities usually rely on a legal analysis of the transparent entity and its comparability to similar French entities, especially in regards of the partners' responsibilities. For instance, for treaty purposes, French tax authorities determines whether or not the foreign partnership qualifies as a resident for treaty purposes by reference to French domestic law by comparing the foreign partnership to French entities by reference to company law criteria (e.g. (un)limited liability of the partners). The foreign entity is then treated for tax purposes similarly to the comparable French entity. It should be noted that this position of the French tax authorities has been recently modified. Administrative guidelines 4 H-5-07, introduces, under certain conditions, the recognition of the transparency approach for	FTC, Section 8 BOI 4 H-5-07

French-source passive income (dividends, interest and royalties) derived by foreign and French-resident partners of a foreign partnership. Accordingly, France waives in certain situations the comparison method under which the foreign partnership is classified by reference to French entities: for the purposes of these guidelines, foreign partnerships are defined as foreign entities treated as transparent for tax purposes in the country where they are established. However, this new approach only applies in respect of tax treaty provisions and not in respect of domestic regulations and thus does not affect domestic regulations implementing the Merger Directive. Hence, for the purposes of provisions implementing the Merger Directive, the French tax authorities still rely on the comparison method. As a consequence, to the best of our knowledge, the French tax authorities should not regard any non-resident transferring company as 'fiscally transparent on the basis of that State's assessment of the legal characteristics of that company arising from the law under which it is constituted'.	

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
<u>4.9 Further conditions for tax relief</u> With regards to mergers, divisions and transfer of assets, the receiving company must commit itself to: (a) record in its accounts the provisions whose taxation has been deferred (Section 210 A, para. 3-a); (b) substitute itself to the transferring company in respect of the reintegration of results whose taxation has been deferred at the level of the transferring company (Section 210 A, para. 3-b); (c) calculate the capital gains deriving from the disposal of transferred non amortizable assets on the basis of their value for tax purposes as recorded in the transferring company accounts (Section 210 A, para. 3-c); (d) in cases where the operations are realized at real value, reintegrate over a fixed period of time in its taxable income the capital gains deriving from the transfer of amortizable fixed assets of the transferring company which have not been taxed at the level of the transferring company (Section 210 A, para. 3-d) (please refer to our comments under 4.1 for more details); (e) record in its accounts the transferred current assets at their value for tax purposes as recorded in the accounts of the transferring company (Section 210 A, para. 3-e) (please refer to our comments under 4.1 for more details on this issue in case of a operation realized at real value). Furthermore, with regards to transfer of assets and divisions, the	FTC, Section 210 A FTC, Section 210 B

transferring company or the shareholders of the transferring company must commit itself to: (a) hold for three years the shares received in exchange of the transfer of assets (Section 210 B, para. 1-a) (please refer to our comments under 11.4 for more details on the issue of the compliance of this requirement with the Merger Directive); (b) calculate the capital gains deriving from the disposal of those shares on the basis of their value for tax purposes as recorded in own accounts at the time of the transfer (Section 210 B, para. 1-b). Finally, please note that in case of a transfer of shares, deemed to constitute a transfer of a branch of activity (please refer to our comments under 2.4), to a foreign company, the French tax authorities require that: (a) the transferring company must commit itself to hold the shares received in exchange for three years; (b) the receiving company must commit itself to hold the received shares as long as being detained by the transferring company (please refer to our comments under 11.4 for more details on the issue of the compliance of such requirements with the Merger Directive).	

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>5.1 The term 'provisions and reserves'</u> The French tax merger regime is driven by a neutrality principle: the receiving company is substituted in the rights and obligations of the transferring company. Hence, with regards to operations realized at accounting value, the receiving company registers in its own accounts all the assets and liabilities, including provisions, depreciations and reserves, as they were registered in the transferring company accounts. As a consequence, the term 'provisions and reserves' have not been transposed into French legislation which simply referred to the accounting and tax concepts as defined by domestic regulations.	

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments With regards to the taxation of legal entities, France relies on the territoriality principle as defined in Section 209 of the FTC. As a consequence, provisions and reserves derived from foreign permanent establishments are not accounted for tax purposes by French legal entities.	

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves As for other types of assets and liabilities, provisions and reserves which only relate to the branch of activity to be transferred should be allocated to it. With regards to provisions and reserves which do not only relate to the branch of activity to be transferred but are items relating to both transferred and non-transferred activities, several allocation methods exist depending on the type of provisions and reserves, as for other assets or liabilities. Indeed, the allocation method is a global issue since such methods are needed accounting items which relate to both transferred activities and non-transferred activities. Hence, the method used will be determined by the nature of the account: (a) provisions for bad debts will be allocated to the different activities on the basis of statistical elements or in proportion of gross sales; (b) accrued vacation expenses, or other provisions relating to employees, will be allocated to the different activities on the basis of information relating to the employees transferred (number, salaries,…), (c) cash will be allocated on the basis of estimates of the working capital requirements for the transferred activities. As a consequence, from a practical point of view, the realization and the securing of the tax treatment of divisions or transfers of assets necessitate to request a validation from the French tax authorities on the various methods used for determining the assets and liabilities to be transferred in order to secure the characterization of a complete branch of activity.	

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
<u>5.4 Further conditions for carry-over of provisions and reserves</u> As for the transfer of assets and liabilities, the receiving company must commit itself, with regards to mergers, divisions and transfer of assets, to: (a) record in its accounts the provisions whose taxation has been deferred (Section 210 A, para. 3-a); (a) substitute itself to the transferring company in respect of the reintegration of results whose taxation has been deferred at the level of the transferring company (Section 210 A, para. 3-b); (b) calculate the capital gains deriving from the disposal of transferred non amortizable assets on the basis of their value for tax purposes as recorded in the transferring company accounts (Section 210 A, para. 3-c); (c) in cases where the operations are realized at real value, reintegrate over a fixed period of time in its taxable income the capital gains deriving from the transfer of amortizable fixed assets of the transferring company which have not been taxed at the level of the transferring company (Section 210 A, para. 3-d) (please refer to our comments under 4.1 for more details); (d) record in its accounts the transferred current assets at their value for tax purposes as recorded in the accounts of the transferring company (Section 210 A, para. 3-e) (please refer to our comments under 4.1 for more details on this issue in case of a operation realized at real value). Furthermore, with regards to transfer of assets and divisions, the transferring company or the shareholders of the transferring company must commit itself to: (a) hold for three years the shares received in exchange of the transfer of assets (Section 210 B, para. 1-a) (please refer to our comments under 11.4 for more details on the issue of the compliance of such requirement with the Merger Directive); (b) calculate the capital gains deriving from the disposal of those shares on the basis of their value for tax purposes as recorded in own accounts at the time of the transfer (Section 210 B, para. 1-b). Finally, as mentioned under 5.3, it is necessary from a practical standpoint to obtain an agreement from the French tax authorities on the elements to be transferred before realizing the contemplated division or transfer of assets.	FTC, Section 210 A FTC, Section 210 B

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
<u>**6.1 Definition of 'loss'**</u> <u>**6.1.1. Overview of the carry-over of losses in case of a merger, division or transfer of assets**</u> French tax rules provide companies liable to corporate income tax which have realised tax losses during a fiscal year with the possibility to: (a) carry-forward these losses so that they may be offset against future tax profits (FTC, Section 209-I); (b) carry-back these losses so that they may be offset against tax profits of the three previous fiscal years, thus creating a receivable against the Treasury equals to the excess of taxes paid in respect of these fiscal years (FTC, Section 220 quinquies). With regards to carry-back losses, the receivable detained by the company which corresponds to the excess of taxes previously paid, or the part of this receivable which is allocated to the transferred branch of activity in case of divisions or transfers of assets, is transferred to the receiving company. Please note that in case of a transfer of assets, the transferring company may decide to retain such receivable. With regards to carry-forward losses, the dissolution with liquidation of the transferring company in case of a merger or a division or the major change of activity that may result from a transfer of assets should trigger the impossibility to use previous losses that have been carried-forward. However, Section 209-II of the FTC provides that the previous losses of the transferring company, or the previous losses relating to the transferred branch of activity in case of divisions or transfers of assets, may be transferred to the receiving company which would be able to offset these losses against its future profits. Such transfer of losses is subject to a prior ruling from the French tax authorities which should be granted if the following conditions are fulfilled: (a) the operation benefits from the favourable tax merger regime, (b) the operation is justified by economical reasons and is not mainly driven by tax reasons, (c) the activity, which has generated the losses to be transferred, is maintained by the receiving company for a minimum period of three years (please note that the French tax authorities have expressed that this requirement should not be fulfilled in case of a transfer of a pure holding, since such company is deemed to have no activity; such position may also be applicable in case of a transfer of a company whose activity is limited to the holding of real estate properties). For operations realized before 1 January 2005, the losses transferred were limited to the gross value of the non-financial fixed assets allocated	FTC, Section 209 FTC, Section 220 quinquies RM Richemont, Sénat, 30 march 2006, p. 923, n°17801

to the business or if superior, the value of those assets at which they are transferred. **6.1.2. Definition of 'losses'** Hence, the French rules implementing Article 6 of the Merger Directive refer to the tax losses which are calculated by application of the existing French corporate income tax regulations.	

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment With regards to mergers, the issue of the allocation of losses to a permanent establishment should only arise where some assets (such as shares) of either the transferring company or the French permanent establishment of a foreign transferring company are not allocated to the French permanent establishment of the foreign receiving company but transferred to this company. In such case, as for divisions and transfer of assets, the losses to be transferred to the permanent establishment would be determined on the basis of allocation keys agreed by the French tax authorities. Indeed, pursuant to Section 209 of the FTC, the transfer of losses incurred and carried-forward by the transferring company to the receiving company (i.e., in the case at hand, the French permanent establishment of the foreign company) must be agreed by the French tax authorities. In such case, the French tax authorities have stated in administrative guidelines 13 D-2-02 that the company which requests such ruling must demonstrate by all means the allocation of the losses between the transferred activities and the non-transferred activities. Hence, from a practical point of view, the issue of the allocation of losses to a permanent establishment is similar to the one relating to the allocation of assets and liabilities described under 5.3. As a consequence, the losses should be allocated on the basis of the management accounts of the transferring company.	FTC, Section 209 BOI 13 D-2-02

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets With regards to carry-back losses, Section 220 quinquies of the FTC provide the transferring company with the possibility to retain the receivable which corresponds to the excess of taxes previously paid. Furthermore, in case of transfer of assets, the losses could remain at the level of the transferring company which will be able to offset such losses against its future tax profits insofar as the transfer of assets does not entail a major change of activity (please note that such option may raise	FTC, Section 220 quinquies

legal issues in presence of minority shareholders). Finally, in case losses are transferred, it should be demonstrated that they are connected with the transferred activities. From a practical point of view, the amount of losses transferred in case of a division or a transfer of assets is determined under the conditions detailed under 5.3.	

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
<u>**6.4 Further conditions for carry over of losses**</u> As previously mentioned, Section 209-II of the FTC, which provides that the previous losses of the transferring company may be transferred to the receiving company which would be able to offset these losses against its future profits, requires a prior ruling from the French tax authorities. Such ruling should be granted if the following conditions are fulfilled: (a) the operation benefits from the favourable tax merger regime, (b) the operation is justified by economical reasons and is not mainly motivated by tax reasons, (c) the activity, which has generated the losses to be transferred, is maintained by the receiving company for a minimum period of three years (please note that the French tax authorities have expressed that this requirement should not be fulfilled in case of a transfer of a pure holding, since such company is deemed to have no activity; such position may also be applicable in case of a transfer of a company whose activity is limited to the holding of real estate properties). This last condition is strictly appreciated by the French tax authorities. Indeed, even if there is no major change of the business conducted by the receiving company, an important decrease of activity - which may be demonstrated for instance by a reduction of the number of employees for instance, or the number of establishments, etc… - may impede the grant of the ruling. Even if those conditions do not differ from those requested in a domestic context, the French tax authorities tend, when asked to grant a prior ruling, to interpret and apply those conditions differently (e.g., requirement to maintain the activity transferred) so that, for instance, it may bar the merger of pure holdings or real estate companies Furthermore, for operations realized before 1 January 2005, the losses transferred were limited to the gross value of the non-financial fixed assets allocated to the business or if superior, the value of those assets at which they are transferred.	FTC, Section 209

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Amended holding threshold The ‘holding threshold’ limitation set out in Article 7(2) of the Merger Directive has not been implemented into French legislation. The tax exemption of the capital gains deriving from the cancellation of a holding in the capital of the transferring company, which is provided by Section 210 A of the FTC, applies if the operation benefit from the favorable tax merger regime and is not subject to any holding threshold requirement.	FTC, Section 210 A FTC, Section 210 B DB 4 I-1244, n°1-3

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses Specific guidance is provided by French legislation, along with administrative guidelines, in respect of the losses that may be realized on the cancellation of a holding. Since the implementation of the new accounting rules for mergers (please refer to our comments under 4.1), a loss is recognized only to the extent that it corresponds to an effective depreciation of the holding, which should have been previously depreciated. Hence, the difference between the book value of the holding in the receiving company accounts and the transfer value of the net assets received, insofar as it corresponds to latent capital gains which have not been recognized, is accounted as an intangible asset whose value for tax purposes equals to 0 (it is a so-called technical loss or ‘mali technique’). The real loss, which corresponds to the remaining part and is accounted as a loss, is tax deductible provided that the company demonstrates the reality and effectiveness of the decrease value. Please note that, depending on the qualification of the cancelled holding, such loss may either be offset against profits taxable at the normal corporate income tax rate, or be only offset against long term capital gains of the same nature.	FTC, Section 210 A FTC, Section 210 B CRC Reg. 2004-01 DB 4 I-1-05, n° 40 f.

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
<u>8.1 Avoidance of economic double taxation at the level of the shareholder</u> French legislation does not provide for the avoidance of economic double taxation at the level of the shareholders. For instance, shareholders of the transferring company which receive shares of the acquiring company may only benefit from a tax deferral on the capital gains resulting from the exchange of shares if certain requirements are fulfilled (please refer to our comments under 8.3 for more details on these requirements). <u>8.1.1. Mergers, divisions and exchange of shares</u> Pursuant to Section 115-1 of the FTC, in case of mergers and divisions, the attribution of shares or cash to the shareholder of the transferring company in exchange of the cancellation of their shares in this company is not deemed to be a distribution of income from securities and does not trigger any taxation on that grounds. Furthermore, the French tax legislation provides for the deferred taxation of the gain or loss resulting from the exchange of shares (i.e., the shareholders exchange their shares in the capital of the transferring company against the shares in the capital of the acquiring company), whether the shareholder is a company (Sections 38-7 and 38-7 bis of the FTC) or an individual (Sections 150-0 B and 150 UB of the FTC). Such tax deferral is compulsory for individuals and for corporate shareholders in case of exchange of shares and optional for corporate shareholders in case of an exchange of shares resulting from a merger or division. With regards to corporate shareholders, Sections 38-7 and 38-7 bis require that the capital gains deriving from the future disposal of the shares received are calculated on the basis of the value for tax purposes of those shares. Hence, the taxation of the capital gains deriving from the exchange of shares is only deferred until the shares received are disposed of. <u>8.1.2. Partial divisions</u> Partial divisions, as defined in Article 2(b)(a) of the Merger Directive, cannot be realized as such under existing French corporate law. However, from a practical point of view, a partial division may be realized as a two-steps operation: (1) a transfer of assets from the transferring company to the receiving company whereby the transferring company receives shares of the receiving company, followed by (2) a distribution by the transferring company to its shareholders of the shares received	FTC, Section 38-7 FTC, Section 38-7 bis FTC, Section 115-1, FTC, Section 115-2, FTC, Section 150-0 B FTC, Section 150-0 D FTC, Section 150 UB BOI 4 I-2-00 BOI 4 I-2-02

from the receiving company. Pursuant to Section 115-2 of the FTC, such distribution of shares of the receiving company to shareholders of the transferring company does not trigger any taxation if a prior ruling from the French tax authorities is granted. Such ruling should be granted if the following requirements are fulfilled: (a) the distribution of shares must be realized, within a one year period starting from the date of realization of the transfer of assets, in proportion of the rights of the shareholders in the transferring company; (b) the transfer of assets benefits from the favourable tax merger regime; (c) the transfer of assets and the distribution of shares are justified by economical reason and are not mainly motivated by tax fraud or tax evasion. As for the prior ruling set out in Section 210 C of the FTC (see our comments under 11.1), the prior ruling requirement set out in Section 115-2 of the FTC may be regarded as implicitly authorized by Article 11(1)(a) of the Merger Directive since it aims at ensuring that the contemplated operation is justified by economical reason and is not mainly motivated by tax fraud or tax evasion (see our comments under 8.3 for more details on the compliance issue). **8.1.3. Rules applicable to foreign shareholders** According to domestic regulations, which may be modified by tax treaty provisions, in case the shareholder that receives the shares of the receiving company is not a French resident, the capital gain deriving from the exchange of shares would be taxable in France only if either the shareholder holds, or has held at any time during the five years prior to the operation, a holding of 25 % or more in the capital of the transferring company, or the transferring company qualifies as 'real estate' company for French tax purposes. However, in both cases, the foreign shareholder should benefit from the deferred taxation if requirements are fulfilled but, as for French resident shareholders, there is no avoidance of economic double taxation at its level. Except those cases, the foreign shareholder is not taxed in France on the capital gain deriving from the exchange of shares. Hence, in respect of the taxation of foreign shareholders, French legislation may be regarded as complying with the Merger Directive.	

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>8.2 Computation of the capital gain</u> In case of an operation whereby the shareholders of the transferring company receive shares of the receiving company and a cash payment, such cash payment may not benefit from a tax deferral and is thus immediately taxable. French tax authorities have only issued guidance on the computation of the capital gain in case of a cash payment only in respect of divisions. According to administrative guidelines 4 I-2-00, (a) the capital gain deriving from the exchange of shares is taxable to the extent of the amount of cash payment, and (b) the part of the capital gain exceeding the cash payment may benefit from the deferred taxation if (i) the cash payment represents less than 10% of the nominal value of the shares, and (ii) the cash payment does not exceed the amount of the capital gain. Furthermore, in case of a disposal of the shares received in exchange, the capital gains will be calculated on the basis of the value for tax purposes of those shares determined as the value for tax purposes of the shares of the transferring company multiplied by the following ratio: the real value of the receiving company shares over the real value of transferring company shares. Hence, the value for tax purposes is proportionally split between the several receiving companies. Please note that similar rules applies to transfer of assets whereby the shares received by the transferring company in exchange for the transfer are distributed to its shareholders under the conditions set out in Section 115-2 of the FTC (please refer to our comments relating to partial divisions under Question 8.1 for more details on such operation).	BOI 4 I-2-00, n°148-161

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>8.3 Further conditions for tax relief</u> <u>8.3.1. Mergers, divisions and exchange of shares</u> In case of mergers, divisions or exchange of shares, Sections 38-7 and 38-7 bis of the FTC provide for a tax deferral of the capital gains deriving from the exchange of shares if the following requirements are fulfilled: (a) the operation realized may qualify as a merger, division or exchange of shares as defined by Section 210-0 A of the FTC;	FTC, Section 38-7 FTC, Section 38-7 bis FTC, Section 54 septies FTC, Section 115-2, FTC, Section 150-0 B FTC, Section 150y-

(b) the cash payment received does not exceed 10% of the nominal value of the shares received in exchange for the transfer; (c) the shareholder must fill-in with its annual tax return a special statement in order to follow-up the capital gains whose taxation has been deferred for every years until the year during which the shares have been disposed of; and (d) the shareholders must maintain a register of the capital gains whose taxation has been deferred which specifies the date of the operation, the book value of the shares received, their value for tax purposes and their exchange value. Hence, the application of the tax deferral of the capital gains deriving from the exchange of shares does not depend to the application or not of the favourable tax merger regime to the operation. Those requirements, except the last one, also apply in respect of individual shareholders. Furthermore, in case of exchange of shares, the tax deferral does not apply if one of the party transfers shares which have been issued less than three years before by way of a capital increase realized by either a company which holds directly or indirectly more than 5% of the capital of the company receiving those shares, or a company in which 5% or more of the capital is held directly or indirectly by the company receiving those shares (FTC, Section 38-7). This exception aims at avoiding abusive operations that may be realized between related entities. However, such requirement may be regarded as disproportionate to the objective set out in Article 11(1)(a) of the Merger Directive since it also applies to operations which do not have as principal objective tax evasion or tax avoidance. **8.3.2. Partial divisions** With regards to transfer of assets followed by a distribution of the shares received by the transferring company to its shareholders, Section 115-2 of the FTC provides for a tax deferral of the capital gains deriving from such distribution of shares if a prior ruling is granted by the French tax authorities. Such ruling is granted if the following requirements are fulfilled: (a) the distribution of shares is realized, within a one year period starting from the date of realization of the transfer of assets, in proportion of the rights of the shareholders in the transferring company; (b) the transfer of assets benefits from the favourable tax merger regime; (c) the transfer of assets and the distribution of shares are justified by economical reason and are not mainly motivated by tax fraud or tax evasion. Hence, according to administrative guidelines, the shareholders may be	0 D BOI 4 I-2-00, n°145 BOI 13 D-1-03 BOI 13 D-1-06

required by the French tax authorities to commit themselves to hold the distributed shares for three years. Those requirements also apply in respect of individual shareholders. In case the transferring company is a French entity, two rulings have to be granted: one in order to avoid the commitment of the transferring company to hold the shares received in exchange for three years (please refer to our comments under 4.9), and one in order to distribute the shares received under the tax deferral regime provided by Section 115-2 of the FTC. In practice, a global ruling covering both operations is required. In case the transferring company is a foreign entity, only the ruling required under Section 115-2 has to be granted. As for the prior ruling set out in Section 210 C of the FTC (see our comments under 11.1), the prior ruling requirement set out in Section 115-2 of the FTC may be regarded as implicitly authorized by Article 11(1)(a) of the Merger Directive since it aims at ensuring that the contemplated operation is justified by economical reason and is not mainly motivated by tax fraud or tax evasion. However, the additional requirement set out in the administrative guidelines that the shareholders commit themselves to hold the distributed shares for three years may be regarded as contrary to the Merger Directive. Indeed, such requirement may be considered as disproportionate to the objective set out in Article 11(1)(a) since it also applies to operations which do not have as principal objective tax evasion or tax avoidance and less restrictive measures might be implemented to ensure the future taxation of the latent capital gains (e.g. declarative obligations).	

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>**9.1 Avoidance of economic double taxation at the level of the transferring company**</u> With regards to transfer of assets, the transferring company must commit itself to: (a) hold for three years the shares received in exchange of the transfer of assets (Section 210 B, para. 1-a) (please refer to our comments under 11.4 for more details on the issue of the compatibility of such holding requirement with the Merger Directive); (b) calculate the capital gains deriving from the disposal of those shares on the basis of their value for tax purposes as recorded in its own accounts at the time of the transfer (Section 210 B, para.	FTC, Section 210 B

1-b). As a consequence, the capital gain corresponding to the difference between the value for tax purposes of the transferred assets and liabilities, which usually correspond to the net accounting value, and the real value of the shares received in exchange would be taxed at the level of the transferring company when those shares would be disposed of. Hence, French legislation does not provide for the avoidance of economic double taxation at the level of the transferring company.	

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
9.2 Further conditions for tax relief 9.2.1 Carry-over of assets and liabilities (including provisions and reserves) As for mergers and divisions, the company which receives a transfer of assets must commit itself to: (a) record in its accounts the provisions whose taxation has been deferred (Section 210 A, para. 3-a); (b) substitute itself to the transferring company in respect of the reintegration of results whose taxation has been deferred at the level of the transferring company (Section 210 A, para. 3-b); (c) calculate the capital gains deriving from the disposal of transferred non amortizable assets on the basis of their value for tax purposes as recorded in the transferring company accounts (Section 210 A, para. 3-c); (d) in cases where the operations are realized at real value, reintegrate over a fixed period of time in its taxable income the capital gains deriving from the transfer of amortizable fixed assets of the transferring company which have not been taxed at the level of the transferring company (Section 210 A, para. 3-d) (please refer to our comments under 4.1 for more details); (e) record in its accounts the transferred current assets at their value for tax purposes as recorded in the accounts of the transferring company (Section 210 A, para. 3-e) (please refer to our comments under 4.1 for more details on this issue in case of a operation realized at real value). Furthermore, in case of transfer of assets, the transferring company must commit itself to: (a) hold for three years the shares received in exchange of the transfer of assets (Section 210 B, para. 1-a) (please refer to our	FTC, Section 210 A FTC, Section 210 B FTC, Section 210 C FTC, Section 209 FTC, Section 220 quinquies

comments under 11.4 for more details on the issue of the compatibility of such holding requirement with the Merger Directive); (b) calculate the capital gains deriving from the disposal of those shares on the basis of their value for tax purposes as recorded in own accounts at the time of the transfer (Section 210 B, para. 1-b). In case of a transfer of shares, deemed to constitute a transfer of a branch of activity (please refer to our comments under 2.4), to a foreign company, the French tax authorities require that: (a) the transferring company must commit itself to hold the shares received in exchange for three years; (b) the receiving company must commit itself to hold the received shares as long as being detained by the transferring company (please refer to our comments under 11.4 for more details on the issue of the compatibility of such holding requirements with the Merger Directive). Finally, from a practical point of view, in order to secure the tax treatment of the operation and avoid any calling into question by the French tax authorities of the applicability of the favourable tax merger, it is necessary to require a prior consent from the French tax authorities. Indeed, pursuant to Section 210 B of the FTC, the favourable tax merger regime should apply if the division or partial transfer of assets relate to a complete branch of activity. Since the transfer should relate to all the assets and liabilities relating to the branch of activity but only such assets and liabilities, the existence of accounts common to several activities require such validation (please refer to our comments under 4.2 for more details). <u>9.2.2 Carry-over of losses</u> With regards to carry-back losses, the transferring company may decide to retain the receivable which corresponds to the excess of taxes previously paid (Section 220 quinquies of the FTC). With regards to carried-forward losses, the transferring company may decide to retain such losses in order to offset them against its future taxable profits insofar as the transfer of assets does not entail a major change of activity (please note that such option may raise legal issues in presence of minority shareholders). In case such losses are transferred, it should be demonstrated that they are connected with the transferred activities (from a practical point of view, the amount of losses transferred in case of a division or a transfer of assets is determined under the conditions detailed under 5.3). <u>9.2.3 Other requirements</u> In case of transfers of assets realized by French legal entities to foreign legal entities, Section 210 C of the FTC requires that a prior ruling is	

granted by the French tax authorities (please refer to our comments under 11.4). Furthermore, special requirements are requested by the French tax authorities in case of a transformation of a French branch of a foreign legal entity into a French subsidiary by way of a transfer of assets (please refer to our comments under 11.4).	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
9.3 Tax deferral To the best of our knowledge, the case law of the ECJ relating to the deferral of taxation, in particular the judgment in Case C-470/04 'N' has not been taken into account into French legislation (please refer to our comments under 10b.5 for more details).	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
10.1 Loss recapture for permanent establishments in third Member States France does not apply a system of worldwide taxation. Hence, French legislation does not provide for the offset of losses incurred by foreign permanent establishments and correlatively does not provide for a loss recapture as envisaged by Article 10(1).	

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
10.2 Permanent establishment in the Member State of the receiving company In case of a foreign company which transfers its assets, or part of its assets which includes assets and liabilities allocated to a French permanent establishment, to a receiving company located in France, French favourable tax merger regime may apply as described previously: (a) the assets and liabilities of the transferring company would be transferred at book value or real value and would not trigger any taxation of the related capital gains insofar as the conditions for benefiting from the favourable tax merger regime are fulfilled;	

(b) the losses of the French permanent establishment may be transferred to the receiving company if a prior ruling from the French tax authorities is granted; (c) the transferring company or its shareholders may benefit from a tax deferral on the capital gains deriving from the operation. In case of a transfer of the branch of activity to a company in exchange for the shares of this company, the French tax authorities have previously required, in order to confirm the application of the favourable tax merger regime, to realize a two-steps operation: (i) the assets and liabilities of the branch of activity are transferred by the foreign company to a French company, and (ii) those assets and liabilities are further transferred by the receiving company to another French company. In such case, the ruling expressively requests that: (a) the French company which will act as an intermediary holding company of the French company carrying out the transferred activity, must commit itself to hold the shares received in exchange for a minimum period of time, and calculate the capital gains to be realized on the future disposal of those shares on the basis of the value for tax purposes of the assets transferred; (b) the foreign company will commit itself to hold the shares of the French holding company received in exchange for the transfer of the branch of activity as long as this company would hold the shares of the French company carrying out the transferred activity. Such two-steps operation aims at ensuring that the capital gains on the shares received in exchange for the transfer of assets, whose taxation is deferred by application of the favourable tax merger regime, would be taxed in case of a disposal of those shares. It should be noted that such transfer of a French branch of a foreign company to a French company does not fall within the scope of the prior ruling required by Section 210 C of the FTC since this provision only apply to mergers, divisions and transfer of assets whereby a foreign legal entity received the transferred assets. However, as for specific requirements deriving from the prior ruling set out by Section 210 C (e.g., holding commitment), those requirements may be considered as disproportionate to the objective set out in Article 11(1)(a) of the Merger Directive since they also apply to operations which do not have as principal objective tax evasion or tax avoidance and less restrictive measures might be implemented to ensure the future taxation of the latent capital gains (e.g. declarative obligations). Hence, these requirements may be regarded as contrary to the Merger Directive (please refer to our comments under 11.4 for more details on this compliance issue).	

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> France does not apply a system of worldwide taxation. Hence, French legislation does not provide for the taxation of unrealized capital gains as provided for by Article 10(2).	FTC, Section 209

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
<u>10.4 Tax deferral</u> To the best of our knowledge, the case law of the ECJ relating to the deferral of taxation, in particular the judgment in Case C-470/04 *'N'*, has not been taken into account into French legislation (please refer to our comments under 10b.5 for more details).	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
<u>10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies</u> Article 10(a) of the Merger Directive has not been implemented into French legislation. Indeed, as previously mentioned, French legislation does not recognize the concept of tax transparency but recognize a semi-transparency concept (or translucency concept) in which the amount of taxable income is determined at the level of the entity but the tax is calculated at the level of its partners on the amount of taxable income attributed in proportion of their rights. Furthermore, French tax authorities usually rely on a legal analysis of the transparent entity and its comparability to similar French entities, especially in regards of the partners' responsibilities. For instance, for treaty purposes, French tax authorities determines whether or not the foreign partnership qualifies as a resident for treaty purposes by reference to French domestic law by comparing the foreign partnership to French entities by reference to company law criteria (e.g. (un)limited liability of the partners). The foreign entity is then treated for tax purposes similarly to the comparable French entity. It should be noted that this position of the French tax authorities has been	

recently modified. Administrative guidelines 4 H-5-07, introduces, under certain conditions, the recognition of the transparency approach for French-source passive income (dividends, interest and royalties) derived by foreign and French-resident partners of a foreign partnership. Accordingly, France waives in certain situations the comparison method under which, the foreign partnership is classified by reference to French entities: for the purposes of these guidelines, foreign partnerships are defined as foreign entities treated as transparent for tax purposes in the country where they are established. However, this new approach only applies in respect of tax treaty provisions and not in respect of domestic regulations and thus does not affect domestic regulations implementing the Merger Directive. Hence, for the purposes of provisions implementing the Merger Directive, the French tax authorities still rely on the comparison method. As a consequence, to the best of our knowledge, the French tax authorities should not regard any non-resident transferring company as 'fiscally transparent on the basis of that State's assessment of the legal characteristics of that company arising from the law under which it is constituted'. Finally, existing French regulations may be viewed as more favourable that the provisions of Article 10(a), especially those relating to the notional tax credit, in respect of individual shareholders.	

How have the 'profits' of an <u>acquired</u> company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
<u>10a.2 Tax base for notional tax credit</u> Since Article 10(a) of the Merger Directive has not been implemented into French legislation (see our comments under 10a.1 for more details), the concept of 'profits of an acquired company' is not defined in French legislation.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an <u>acquired</u> company?	Reference
<u>10a.3 Determination of notional tax credit</u> Since Article 10(a) of the Merger Directive has not been implemented into French legislation (see our comments under 10a.1 for more details), there is no rule relating to the determination of the notional tax credit.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders Article 10(a) of the Merger Directive has not been implemented into French legislation (see our comments under 10a.1 for more details).	

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company Article 10(a) of the Merger Directive has not been implemented into French legislation (see our comments under 10a.1 for more details).	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation As a preliminary remark, it should be noted that, for provisions of the Merger Directive introduced in 2005, either implemented or not into French legislation, there are few available examples and thus little experience of the French tax authorities practice. According to French legislation, the transfer of the head office of a legal entity outside France should trigger the immediate taxation of the profits of the current fiscal year, the profits which benefited from a tax deferral regime, and the unrealized capital gains on the assets. However, pursuant to Section 221-2, subparagraph 3, of the FTC the transfer of the head office of a legal entity, whatever its legal form is, to another Member State does not trigger the consequences of a cease of business activity. The tax consequences of such transfer are analyzed by the French tax authorities in respect of the principle of continuation of the taxpayer personality. Such principle implies that available tax losses remain at the permanent establishment and that the value of assets and liabilities registered in the balance sheet of the company are recorded as such in the balance sheet of the permanent establishment.	FTC, Section 221-2

Hence, the transfer of the head office of a legal entity to another Member State does not trigger any immediate taxation insofar as the assets and liabilities of the legal entity remain connected with a French permanent establishment of the legal entity (i.e., the assets and liabilities of the legal entities are registered in the balance sheet of the French permanent establishment). It should be noted that the application of Section 221-2, subparagraph 3, of the FTC only provide for a tax deferral of the unrealized capital gains relating to the assets allocated to the French permanent establishment. Indeed, as specified in draft administrative guidelines, which have been released but would not be published in their current drafting, in case their taxation is granted to France by the relevant the tax treaty, the capital gains deriving from the future disposal of such assets would be calculated on the basis of the net accounting value of those assets as recorded in the company accounts at the time of the transfer. In respect of assets and liabilities which remain effectively connected with a permanent establishment of the legal entity whose head office is transfer red abroad, French legislation may be regarded as complying with Article 10b of the Merger Directive which prohibits the immediate taxation of the capital gains relating to such assets and liabilities. In respect of other assets and liabilities of the legal entity whose head office is transferred abroad, the question whether exit taxation such as the one resulting from French legislation is contrary to EC law, especially the freedom of establishment principle, has not been answered yet by the ECJ. Indeed, the existing ECJ case law on exit taxation relates only to the transfer of domicile of individuals (ECJ, C-9/02, 11 March 2004, Lasteyrie du Saillant; ECJ, C-470/04, 7 September 2006, 'N'). Furthermore, the '*Daily Mail*' decision (ECJ, C-81/87, 27 September 1988, '*Daily Mail*') and the provisions of the Merger Directive may have been interpreted as authorizing exit taxation.	

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
<u>10b.2 The term 'head office'</u> Section 221-2, subparagraph 3, of the FTC does not specify if this provision refers to the place of effective place of management or the statutory registered office. Furthermore, both terms are used in the draft administrative guidelines. Hence, Section 221-2 of the FTC may be interpreted as covering either the transfer of registered office or the transfer of the effective place of management, depending on the case at hand. Furthermore, with regards to the transfer of the registered office of an SE or an SCE, it should be noted that French legislation requires, as authorized by Article 7 of the Council Regulation 2157/2001 on the Statute for a European company (SE), that the registered office and the place of management of such company should be the same (French	FTC, Section 221-2

Commercial Code, Section L 229-1). Hence, in such a case, Section 221-2 of the FTC would nevertheless apply.	

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
<u>10b.3 Head office and tax residency</u> <u>10b.3.1 Domestic law</u> With regards to the taxation of legal entities, France relies on the territoriality principle as defined in Section 209 of the FTC. According to this provision, French corporate income tax apply to benefits realized by an organization exploited in France ('territoriality principle') and to benefits attributed to France by application of a tax treaty provisions. The concept of 'organization exploited in France', which is not defined by the law, has been defined by French case law as: (a) establishments located in France, defined as a permanent and independent facilities (e.g. plant, branch, etc.); (b) agent; (c) operations representing a complete commercial process. Hence, French domestic legislation does not rely on the statutory registered office or the effective place of management for the determination of the tax residency of legal entities. <u>10b.3.2 Double tax treaties</u> With regards to double tax treaties, France tends to use the OECD Model Convention which Article 4(3) states that 'where (…) a person other than an individual is a resident of both contracting States, then it shall be deemed to be a resident only of the State in which its place of effective management is located'.	FTC, Section 209 FTC, Section 221-2

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>10b.4 Assets and liabilities not effectively connected with a permanent establishment</u> In case of a transfer of the effective place of management of a company, the assets and liabilities of the legal entities which are not registered in the balance sheet of the French permanent establishment are subject to immediate capital gain taxation. In case of a transfer of the registered office of a company, with its place of	

effective management remaining located in France, the assets and liabilities of the legal entities are subject to immediate capital again taxation only if they do not remain allocated to one of the permanent establishments in France of the company. Such exit taxation may be regarded as complying with Article 10b of the Merger Directive which prohibits the immediate taxation of the capital gains relating to such assets and liabilities. Furthermore, the question whether such exit taxation is contrary to EC law, especially the freedom of establishment principle, has not been answered yet by the ECJ. Indeed, whereas the existing ECJ case law on exit taxation relates only to the transfer of domicile of individuals (ECJ, C-9/02, 11 March 2004, '*Lasteyrie du Saillant*'; ECJ, C-470/04, 7 September 2006, '*N*'), the '*Daily Mail*' decision (ECJ, C-81/87, 27 September 1988, '*Daily Mail*') and the provisions of the Merger Directive may have been interpreted as authorizing exit taxation.	

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the '*N*' case?	Reference
<u>10b.5 Tax deferral</u> To the best of our knowledge, the case law of the ECJ relating to the deferral of taxation, in particular the judgment in Case C-470/04 '*N*', has not been taken into account into French legislation. However, it should be noted that the publication of the released draft administrative guidelines commenting Section 212-2 of the FTC has been deferred because the French tax authorities planned to discuss with the European Commission the consequences of the principles set out in the '*N*' decision.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
<u>10c.1 The term 'comparable circumstances'</u> The term 'comparable circumstances' has not been implemented *per se* into French legislation. As previously mentioned, French tax rules provide companies liable to corporate income tax which have realised tax losses during a fiscal year with the possibility to: (a) carry-forward these losses so that they may be offset against future tax profits (FTC, Section 209-I);	FTC, Section 209-I FTC, Section 220 quinquies

(b) carry-back these losses so that they may be offset against tax profits of the three previous fiscal years, thus creating a receivable against the Treasury equals to the excess of taxes paid in respect of these fiscal years (FTC, Section 220 quinquies). With regards to carry-back losses, the corresponding receivables owned by the company which transfers its head office in another Member State should only be allocated to its French permanent establishment. With regards to carry-forward losses, the draft administrative guidelines provide that the company which transfer its head office in another Member State continues to benefit in France, through its French permanent establishment, from its carried-forward losses. Hence, French legislation should be considered as compliant with the requirement set out in Article 10c(2) of the Merger Directive to provide the French permanent establishment of a company transferring its head office to another Member State with the possibility to take over the carried-back losses or the carried-forward losses of that company.	

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Loss recapture for permanent establishments France does not apply a system of worldwide taxation. Hence, French legislation does not provide for the offset of losses incurred by foreign permanent establishments of a French resident company and correlatively does not provide for a recapture of such losses.	

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
10d.1 Deemed liquidation As previously mentioned, pursuant to Section 221-2, subparagraph 3, of the FTC the transfer of the registered office of a legal entity to another Member State is not considered as a deemed liquidation and does not trigger the consequences of a cease of business activity, insofar as all its assets are not disposed of or transferred outside of France. In case all the assets of the company transferring its head office in another Member State are disposed of or are transferred outside of France, the operation triggers the immediate taxation of (a) the profits of the current fiscal year;	FTC, Section 221-2

(b) the profits which benefited from a tax deferral regime, and (c) the unrealized capital gains on the assets (please refer to Question 10.b.1 for our comments on the compatibility of such immediate taxation with EC law). Furthermore, as specified in the draft administrative guidelines, the transfer of the registered office of a legal entity to another Member State is not considered as a deemed distribution and does not trigger any immediate taxation at the level of the shareholders of this entity.	

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>**10d.2 Tax treatment of third country residents**</u> As for shareholders resident in France or in other Member States, the transfer of the registered office of a legal entity to another Member State is not considered as a deemed distribution and does not trigger any immediate taxation at the level of the shareholders of this entity.	FTC, Section 221-2

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>**11.1 Transposition of anti-abuse provisions**</u> <u>11.1.1 Implementation of Article 11(1)(a) into French legislation</u> As stated in administrative guidelines 4 I-1-93, the Merger Directive has been interpreted by French tax authorities as authorizing Member States to: (a) subordinate the application of the favourable tax merger regime to specific rules for the calculation of depreciation, provisions and capital gains relating to assets and liabilities transferred; (b) deny the application of the favourable tax merger regime to operations driven by tax evasion or tax fraud. Thus, Section 210 C of the FTC may be regarded as implementing Article 11(1)(a) of the Merger Directive. Indeed, Section 210 C of the FTC states that the favourable tax merger regime may apply to the transfer of assets by way of a merger, a division or a transfer of assets realized by French legal entities to receiving foreign	FTC, Section 210 B FTC, Section 210 C FTC, Section 1649 nonies-A BOI 13 D-1-00 BOI 4 I-2-00

legal entities only if a prior ruling is granted by the French tax authorities. As set out in Section 210 B of the FTC, such ruling would be granted if: (a) the operation is justified by economical reasons; (b) the operation is not motivated by fraud or tax evasion; (c) the operational modalities ensure the future taxation of the latent capital gains whose taxation would be deferred by application of the favourable tax merger regime. However, whereas Article 11(1)(a) states that the fact that an operation is not carried out for valid commercial reasons may constitute a presumption that the operation is not principally motivated by tax evasion or tax avoidance, French legislation regards the valid commercial reasons requirement and the non-tax driven requirement as cumulative. Even if such requirements are considered as cumulative by the French tax authorities, those requirements would be appreciated globally by French courts according to previous case law. Hence, the existence of a valid economical reason would impede the recognition of a fraud or tax evasion motivation. The third requirement, which aims at ensuring future taxation in France, generates most problems as additional requirements, such as the subordinated holding requirement, derive from it (please refer to our comments under 11.4, especially 11.4.3 for more details on these additional requirements). Furthermore, the French tax authorities have at least once refused to grant a ruling for a transfer of shares to a company located in another Member State arguing that the contemplated operations did not ensure the future taxation of the capital gains whose taxation would be deferred and did not preserve the taxing rights of France, even if the companies part of the operation have committed themselves to the usual holding requirements. Hence, the compliance of this third requirement with the Merger Directive remains doubtful. <u>11.1.2 Overview of the regime of the ruling requested by Section 210 C</u> It should be noted that the rejection of such ruling by the French tax authorities must be motivated and may be contested before French administrative courts. Furthermore, as stated in Section 1649 nonies-A of the FTC, in case the participants of a merger or assimilated operation do not respect the requirements specified in the ruling or the commitments taken in order to obtain the ruling, the benefits of the favourable tax merger regime may be cancelled by the French tax authorities either entirely, or, upon a discretionary decision of the French Minister of Finances, partially. Hence, in such case, all or part of the taxes, which have been deferred by application of the favourable tax merger regime, are immediately due. In regards of those practical consequences of the cancellation of a ruling, it should be noted that the French Supreme Court has decided that, in case the requirement to hold the shares received in exchange of the transfer of assets is not respected, the related capital gain taxes should be calculated on the basis of the tax rules existing at the date at which such requirement	

is no longer respected, and not on the basis of the tax rules existing at the date of the transfer of assets (CE, 13 July 2007, n°289658, Transalliance).	

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' (*'Kofoed'*, paragraph 46)?	Reference
11.2 General anti-abuse provisions Even if Section 210 C of the FTC may be regarded as implementing Article 11(1)(a) of the Merger Directive, the French tax authorities may also rely on the concept of abuse of law as set out in Section L 64 of the FTPC. Pursuant to Section L 64 of the FTPC, as interpreted by French case law, the French tax authorities may contest the tax consequences of an operation if they demonstrate that such operation is fictive from a legal point of view, or has been realized in order to benefit from the literal application of the law against the objectives of its authors and is only driven by the avoidance of the tax burden that would have normally been supported. However, from a practical point of view, a merger or assimilated operation should not be considered as fictive from a legal point of view. Furthermore, except for instance the case of shell companies with carried-forward losses or pure holdings, a merger or assimilated operation should not be regarded as driven only by tax reasons since such operation most often triggers important legal and economical consequences.	FTPC, Section L 64

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' With regards to French legislation relating to the favourable tax merger regime, no particular actions have been taken yet in order to implement the 'wholly artificial arrangement' concept defined in the ECJ case law. Indeed, as previously stated, French anti-abuse regulations are very close to the principles set out in the 'Cadbury' decision and French case law has developed a similar concept for years. In respect of the abuse of law theory as set out in Section L 64 of the FTPC, it should be noted that the French Supreme Court has decided that such theory, as interpreted in French case law, is compatible to the ECJ case law since it targets wholly artificial arrangements which aim at benefiting from the literal application of French law against the objectives of its authors (CE, 18 May 2005, n°267087, SA Sagal). Hence, provided that it is interpreted and applied accordingly, the abuse of	FTPC, Section L 64 FTC, Section 210 C BOI 13 D-1-00, n°16y

law theory may be regarded as in line with the ECJ case law relating to the wholly artificial arrangement. In respect of the anti-abuse provision set out in Section 210 C of the FTC, and specially the requirement that the operation is not motivated by tax fraud or evasion, administrative guidelines 13 D-1-00 state that the concept of a fraud or tax evasion motivation is more extensive than the concept defined for the application of Section L 64 of the FTPC. Hence, based on these guidelines, we may consider that the 'wholly artificial arrangement' concept as set out by the ECJ has not yet been implemented in the specific anti-abuse provision of Section 210 C of the FTC. It should be noted that, in the course of the prior rulings requested by Section 210 C of the FTC, the French tax authorities may restrain the 'tax fraud or evasion motivation' to 'wholly artificial arrangement'. However, based on our experience, French tax authorities have not yet taken into account the ECJ case law when characterizing tax fraud or evasion.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
<u>**11.4 Specific anti-abuse provisions**</u> <u>11.4.1 General requirements for benefiting from the favourable tax merger regime</u> According to French tax rules, the favourable tax merger regime may apply only if several requirements are fulfilled, depending on the operation contemplated: (a) in case of transfer of assets and divisions, the transferring company or the shareholders of the transferring company must commit itself to hold for three years the shares received in exchange of the transfer of assets (Section 210 B, paragraph 1-a, of the FTC) (please refer to our comments under 4.9 for more details); (b) in case of transfer of assets and divisions, a prior ruling may be required (Section 210 B, paragraph 3 of the FTC); (c) in case of mergers, divisions or exchange of shares, the shareholder must (i) fill-in with its annual tax return a special statement in order to follow-up the capital gains whose taxation has been deferred for every years until the year during which the shares have been disposed of , and (ii) maintain a register of the capital gains whose taxation has been deferred which specifies the date of the operation, the book value of the shares received, their value for tax purposes and their exchange value (Sections 38-7 and 38-7 bis of the FTC) (please refer to our comments under 8.3	FTC, Section 210 A FTC, Section 210 B FTC, Section 210 C FTC, Section 38-7 FTC, Section 38-7 bis FTC, Section 209-II BOI 13 D-1-00

for more details);

(d) in case of transfers of assets followed by a distribution of the shares received by the transferring company to its shareholders, the tax deferral of the capital gains deriving from such distribution of shares is subject to a prior ruling to be granted by the French tax authorities, which may require that the shareholders commit themselves to hold the distributed shares for three years (please refer to our comments under 8.3 for more details);

(e) in case of a transfer of shares, deemed to constitute a transfer of a branch of activity to a foreign company, the French tax authorities require that the transferring company commits itself to hold the shares received in exchange for three years and the receiving foreign company commits itself to hold the received shares as long as being detained by the transferring company (such requirement aims at impeding any further sale by the receiving company of the shares received: the sale of shares must be realized by the transferring company established in France so that France ensures its taxing rights, the taxation being only postponed until the sale of the shares by the transferring company) (please refer to our comments under 4.9);

(f) in case of exchange of shares, the tax deferral does not apply if one of the party transfers shares which have been issued less than three years before by way of a capital increase realized by either (i) a company which holds directly or indirectly more than 5% of the capital of the company receiving those shares, or (ii) a company in which 5% or more of the capital is held directly or indirectly by the company receiving those shares (FTC, Section 38-7);

(g) in respect of transfer of losses, (i) a prior ruling is required and (ii) the activity, which has generated the losses to be transferred, must be maintained by the receiving company for a minimum period of three years (the French tax authorities consider that such requirement is not fulfilled in case of a transfer of a pure holding or a company whose activity is limited to the holding of real estate properties) (Section 209-II of the FTC) (please refer to our comments under 6.4).

<u>11.4.2 Prior ruling requirement set out by Section 210 C</u>

As previously explained, Section 210 C of the FTC may be regarded as implementing Article 11(1)(a) of the Merger Directive.

Indeed, Section 210 C of the FTC states that the favourable tax merger regime may apply to the transfer of assets by way of a merger, a division or a transfer of assets realized by French legal entities to receiving foreign legal entities only if a prior ruling is granted by the French tax authorities.

<u>11.4.3 Requirements deriving from the prior ruling set out by Section 210 C</u>

Furthermore, as set out in Section 210 B of the FTC, the prior ruling required by Section 210 C of the FTC would be granted if:

(a) the operation is justified by economical reasons;

(b) the operation is not motivated by fraud or tax evasion;

(c) the operational modalities ensure the future taxation of the latent capital gains whose taxation would be deferred by application of the favourable tax merger regime.

As previously mentioned, whereas Article 11(1)(a) states that the fact that an operation is not carried out for valid commercial reasons may constitute a presumption that the operation is not principally motivated by tax evasion or tax avoidance, French legislation regards the valid commercial reasons requirement and the non-tax driven requirement as cumulative. However, even if such requirements are considered as cumulative by the French tax authorities, those requirements would be appreciated globally by French courts according to previous case law. Hence, the existence of a valid economical reason should impede the recognition of a fraud or tax evasion motivation.

Furthermore, the French tax authorities have interpreted those requirements as implying that the companies part of the operation take holding period commitments.

For instance, the administrative guidelines 13 D-1-00 state that the transferring company must be implicated in the transferred business over a certain period of time and thus the transferring company or its shareholders receiving the shares in exchange for the transfer of assets must commit themselves to hold such shares for a certain period of time to be specified in the ruling (BOI 13 D-1-00, n°11-12).

For instance, in case of a division or transfer of assets followed by a distribution of the shares received by the transferring company to its shareholders (please refer to our comments under 8.1 for more details), or a transfer of those shares, the commitment to hold those shares for a certain period of time should be taken by the shareholders receiving the shares, or the company receiving the shares. Furthermore, the administrative guidelines 13 D-1-00 specify that the whole chain of participations between the activities kept and the activities transferred should be subject to such a holding requirement.

Hence, for the French tax authorities, the requirement of such holding period commitments derives from the requirement set out in Section 210 B of the FTC and should thus be viewed as authorized by Article 11(1)(a) of the Merger Directive. However, such requirement may be considered as disproportionate since it also applies to operations which do not have as principal objective tax evasion or tax avoidance and less restrictive measures might be implemented to ensure the future taxation of the latent capital gains (e.g. declarative obligations). Hence, the requirement of such holding period commitments may be viewed as contrary to the Merger Directive.

Finally, it should be noted that this doctrine of the French tax authorities, which aimed at preserving the taxing rights of France, has not been modified in spite of the recent reform of the taxation of long term capital

gains, which are now subject to a 0% tax rate, with a 5% of the expenses incurred by the company added-back to the taxable income subject to the normal corporate tax rate. <u>11.4.4 Specific requirements</u> In case of the transformation of a French branch of a foreign company into a French subsidiary by way of a transfer of the branch of activity to a company in exchange for the shares of this company, the French tax authorities have previously required, in order to confirm the application of the favourable tax merger regime, to realize a two-steps operation: (a) the assets and liabilities of the branch of activity are transferred by the foreign company to a French company; (b) those assets and liabilities are further transferred by the receiving company to another French company. Furthermore, in such case, the ruling requested that: (a) the French company which will act as an intermediary holding company of the French company carrying out the transferred activity, must commit itself to hold the shares received in exchange for a minimum period of time, and calculate the capital gains to be realized on the future disposal of those shares on the basis of the value for tax purposes of the assets transferred; (b) the foreign company will commit itself to hold the shares of the French holding company received in exchange for the transfer of the branch of activity as long as this company would hold the shares of the French company carrying out the transferred activity. Such two-steps operation aims at ensuring that the capital gains on the shares received in exchange for the transfer of assets, whose taxation is deferred by application of the favourable tax merger regime, would be taxed in case of a disposal of those shares. It should be noted that such transfer of a French branch of a foreign company to a French company does not fall within the scope of the prior ruling required by Section 210 C of the FTC since this provision only apply to mergers, divisions and transfer of assets whereby a foreign legal entity received the transferred assets. However, as for specific requirements deriving from the prior ruling set out by Section 210 C (e.g., holding commitment), those requirements may be considered as disproportionate to the objective set out in Article 11(1)(a) of the Merger Directive since they also apply to operations which do not have as principal objective tax evasion or tax avoidance and less restrictive measures might be implemented to ensure the future taxation of the latent capital gains (e.g. declarative obligations). Hence, these requirements may be regarded as contrary to the Merger Directive. Furthermore, as for the requirements deriving from Section 210 C, it should be noted that the doctrine of the French tax authorities, which aimed at preserving the taxing rights of France, has not been modified in spite of the recent reform of the taxation of long term capital gains, which	

are now subject to a 0% tax rate, with a 5% of the expenses incurred by the company added-back to the taxable income subject to the normal corporate tax rate.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' As previously mentioned, Sections 210 C and 210 B of the FTC may be regarded as implementing Article 11(1)(a) of the Merger Directive by requiring a prior ruling from the French tax authorities in respect of operations whereby assets and liabilities are transferred by French legal entities to foreign legal entities. However, whereas Article 11(1)(a) states that the fact that an operation is not carried out for valid commercial reasons may constitute a presumption that the operation is not principally motivated by tax evasion or tax avoidance, French legislation regards the valid commercial reasons requirement and the non-tax driven requirement as cumulative. Indeed, as stated in Section 210 B, paragraph 3, of the FTC, the prior ruling would be granted if the following requirements are fulfilled: the operation is justified by economical reasons, such as operating a autonomous activity at the level of the receiving company, or improving the business structures, or an association between the companies, the operation is not motivated by fraud or tax evasion, and the operational modalities ensure the future taxation of the latent capital gains whose taxation would be deferred by application of the favourable tax merger regime. As previously mentioned, it should be noted that, even if such requirements are considered as cumulative by the French tax authorities, contrarily to the wording of Article 11(1)(a), those requirements would be appreciated globally by French courts according to previous case law. Hence, the existence of a valid economical reason would impede the recognition of a fraud or tax evasion motivation. Furthermore, as a preliminary remark, it should also be noted that the French 'Conseil Constitutionnel' has specified that the requirement of an economical reason set out in Section 210 B of the FTC authorizes the French tax authorities to verify the existence of an economical reason for the contemplated operation but does not authorize the French tax authorities to appreciate the opportunity of such operation (Conseil Constitutionnel, 29 December 1999, n°99-424 DL, Finance Bill for 2000). The requirements set out in Section 210 B of the FTC have been detailed in administrative guidelines 13 D-1-00 which states that the prior ruling would be granted if: (a) the operation is justified by a valid economical reason; (b) the assets transferred allow the receiving company to exercise the received activity by its own means or to improve its structures;	FTC, Section 210 B FTC, Section 210 C BOI 13 D-1-00, n°5-19

(c) the operation is justified by an association between the companies part of the operation; (d) the operation is not motivated by fraud or tax evasion; (e) the operational modalities ensure the future taxation of the latent capital gains whose taxation would be deferred by application of the favourable tax merger regime. The first three requirements set out in the administrative guidelines may be regarded as relating to the economical reason requirement set out in Section 210 B of the FTC. With regards to the valid economical reason requirement, the administrative guidelines 13 D-1-00 only provide with some examples in which such requirement is considered as fulfilled: the regrouping of similar or related activities carried out by the receiving company or, for intra-group operations, in case of a rationalizing of the commercial or industrial activities structures (BOI 13 D-1-00, n°5-7). With regards to the assets transferred, the administrative guidelines specify that, even if such assets do not constitute a complete branch of activity, the completion of the operation must either provide the receiving with the means sufficient for realizing the received activity, or, aim at creating or extending a business or improving its existing structure (BOI 13 D-1-00, n°8-10). With regards to the association requirement, the administrative guidelines specify that the transferring company must still be implicated in the transferred business. As a consequence, as specified, a ruling would be granted if such implication is maintained over a certain period of time, thus implying commitments to hold the shares received in exchange for the transfer of assets for a certain period of time (BOI 13 D-1-00, n°11-13) (Please refer to 11.4, especially 11.4.3, for our comments on the compatibility of such holding commitments with the Merger Directive).	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
<u>11.6 Burden of proof</u> As previously mentioned, Section 210 C of the FTC requires a prior ruling from the French tax authorities in respect of operations whereby assets and liabilities are transferred by French legal entities to foreign legal entities (please refer to Question 11.1 for our comments on the compatibility of this requirement with the Merger Directive). In order to obtain such ruling, the companies parties at the contemplated operation should fill in a form, provided in the Annex to the administrative guidelines 13 D-1-00, in which they must provide organizational charts before and after the completion of the operation, details about the transferring company, the activity to be transferred, the receiving company, the nature and value of the assets to be transferred, and the	FTC, Section 210 C FTC, Section 1649 nonies BOI 13 D-1-00

remuneration of the transfer, the reasons for the operation, etc. With regards to the reasons for the realization of the operation, the French tax authorities would examine if the economical reason requirement is fulfilled and may ask for additional information. However, should the French tax authorities reject the ruling because they consider that the contemplated operation does not fulfil the economical reason requirement, they would have to motivate the rejection, which may be contested before the French administrative courts.	

GERMANY

Abbreviations

English	German	English	German
CITA	KStG	Corporate Income Tax Act	Körperschaftsteuergesetz
DTC	DBA	Double Tax Convention	Doppelbesteuerungsabkommen
EEA Agreement	EWR-Abkommen	European Economic Area Agreement	Abkommen über den Europäischen Wirtschaftsraum
ECSI Act	EuroGenEinfG	European Cooperative Society Implementation Act	Gesetz zur Einführung der Europäischen Genossenschaft und zur Änderung des Genossenschaftsrechts
FLG	BGBl	Federal Law Gazette	Bundesgesetzblatt
FTA	AStG	Foreign Tax Act	Außensteuergesetz
FTG	BStBl	Federal Tax Gazette	Bundessteuerblatt
GAAP	GoB	Generally Accepted Accounting Principles	Grundsätze ordnungsgemäßer Buchführung
GCC	HGB	German Commercial Code	Handelsgesetzbuch
GmbH Act	GmbHG	Limited Liability Company Act	Gesetz betreffend die Gesellschaften mit beschränkter Haftung
GTC	AO	General Tax Code	Abgabenordnung
ITA	EStG	Income Tax Act	Einkommensteuergesetz
ITD	EStDV	Income Tax Directive	Einkommensteuer-Durchführungsverordnung
ITR	EStR	Income Tax Regulations	Einkommensteuer-Richtlinien
MD	FRL	Merger Directive	Fusionsrichtlinie
RA	UmwG	Reorganization Act	Umwandlungsgesetz
RTA	UmwStG	Reorganization Tax Act	Umwandlungs-Steuergesetz
SCA	AktG	Stock Corporation Act	Aktiengesetz
SCEImpl. Act	SCEAG	SCE Implementation Act	SCE-Ausführungsgesetz
SE	SE	Societas Europaea	Europäische Aktiengesellschaft
SEImpl. Act	SEAG	SE Implementation Act	SE-Ausführungsgesetz

English	German	English	German
SETI Act	SEStEG	SE Tax Introduction Act	Gesetz über steuerliche Begleitmaßnahmen zur Einführung der Europäischen Gesellschaft und zur Änderung weiterer steuerrechtlicher Vorschriften
BLI Act	StandOG	Business Location Improvement Act	Standortsicherungsgesetz
TTA	GewStG	Trade Tax Act	Gewerbesteuergesetz

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.

<u>Overall state of implementation</u>

The Merger Directive was implemented by the Tax Amendment Act 1992 (Federal Law Gazette I 1992 p. 297), dated 25 February 1992, and the so-called SETI Act (Federal Tax Gazette I 2006 p. 2782), dated 7 December 2006.

With the Tax Amendment Act 1992, the Merger Directive was implemented by adding two paragraphs to Sec. 20 RTA (Sec. 20(6 and 8)). It transposed only the requirements of transfer of assets and exchange of shares into German law, but not the requirements of merger and division/partial division. The Tax Amendment Act 1992 came into effect on 1 January 1995. With the BLI Act, dated 13 September 1993 (Federal Law Gazette I 1993 p. 1569) these provisions were integrated into Sec. 23 RTA.

The SETI Act came into effect on 13 December 2006 and is applicable for transactions occurring after 1 January 2007. Based on the Merger Directive, Sec. 12 CITA and Sec. 1 ff. RTA were amended accordingly.

Please note that the SETI Act has been designed not only to cover EU/EEA reorganizations but also to a limited extent also to third country reorganizations (see no. 1.2).

Guidance issued by the tax administration relevant for the interpretation of the implementation of the Merger Directive is included in the following publications:

(a) Ministry of Finance Circular of 25 March 1998, Federal Tax Gazette I 1998 p. 268, regarding the Reorganization Tax Act 1995 (RTA 1995); Questions under discussion and interpretative questions. The circular was adjusted by the Ministry of Finance Circular of 16 August 2000, Federal Tax Gazette I 2000 p. 1253.

(b) Ministry of Finance Circular of 16 December 2003, Federal Tax Gazette I 2003 p. 786, regarding questions under discussion raised by the Tax Reduction Act and the Development of Companies Taxation Act.

(c) Ministry of Finance Circular of 4 September 2007, Federal Tax Gazette I 2007 p. 298, regarding the transfer of assets under the SETI Act; Documentation requirements according to Sec. 22(3) RTA.

(d) Ministry of Finance Circular of 24 December 1999, Federal Tax Gazette I 1999 p. 1076, regarding the tax treatment of permanent establishments.

As outlined in the explanatory memorandum to the SETI Act it is the position of the German legislator that German tax law is compliant with the Merger Directive as a result of the implementation of the Merger Directive by the SETI Act.

Directive 2005/56/EC on cross-border mergers of limited liability companies was implemented in Sec. 122a seq. RA effective as from 25 April 2007.

Survey of the Implementation of Council Directive 90/434/EEC

(The Merger Directive, as amended)

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Prior to the implementation of the Directive a cross-border EU merger could only be performed with reference to Primary EC law (Article 43 EC – freedom of establishment, see ECJ case C-411/03 '*Sevic*') and the following SE- and SCE-Regulations. The SE-Regulation (No. 2157/2001) was implemented into German domestic law by the SEImpl. Act (Federal Law Gazette I 2004 p. 3675), dated 22 December 2004. The SCE-Regulation (No. 1435/2003) was implemented into German domestic law by the SCEImpl. Act (Federal Law Gazette I 2006, p. 1911), dated 14 August 2006, adjusted by Article 12 (11) of the Law dated 10 November 2006 (Federal Law Gazette I 2006, p. 2553) and the ECSI Act (Federal Law Gazette I 2006 p. 1911), dated 14 August 2006. Cross-border divisions/partial divisions are still not laid down by German company law. Because the RTA refers to reorganizations under the RA, the implementation of the Merger Directive in German tax law could not cover German cross-border divisions/partial divisions. Insofar as such reorganizations must be allowed from a legal point of view under reference to EC Primary law, the provisions of the RTA must be read in a way covering such reorganizations.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> The expression 'in which companies from two or more Member States are involved' has been interpreted as comprising only the companies directly involved in the transaction and not the parent companies. The transferring and the receiving companies must be companies established in accordance with the legislation of a Member State or any EEA State within the meaning of Article 48 EC or Article 34 EEA Agreement. The registered office and place of management of the transferring company and the receiving company must both be located within the EU although not necessarily within the same Member State. Example: A GmbH managed in Germany and with its place of incorporation in Germany will be merged with a UK Limited company incorporated in the UK but managed outside the EU/EEA. The RTA would not apply in this case.	Sec. 1(2) no. 1 RTA

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or from a third (non-EU) State or from third States? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third State or from third States?	Reference
<u>**1.2 Foreign Member State and third state merger**</u> The RTA would apply under certain circumstances also for foreign transactions comparable to a merger, division and partial division within the meaning of Sec. 2 and Sec. 123(1) and (2) RA: (a) The foreign merger would be within the scope of the German RTA if the merging companies were from Member States or EEA States. (b) The German RTA would not apply if only one of the merging companies were from a single Member State or an EEA State. (c) The German RTA would also not apply if one of the merging companies were from a third (non-EU/EEA) State. The aforementioned rules apply *mutatis mutandis* to division/partial divisions. Sec. 12(2) CITA provides in the event that the RTA is not applicable but the assets and liabilities of a corporate entity subject to limited tax liability are in their entirety transferred to another corporate entity of the same foreign State by a transaction comparable to a merger within the meaning of the RTA that the assets transferred have to be assessed at book value, provided that: (a) it is ensured that they will later be subject to German corporate income tax with the corporate entity receiving the assets; (b) there is no limitation as to the right of Germany to tax the transferred assets with the receiving corporate entity; (c) no consideration is granted, or such a consideration consists in shares; and (d) the receiving and the transferring legal entity do not qualify as entities for which the RTA applies. The application of this rule for shareholders does not require that the merging corporate entities are subject to limited tax liability in Germany. It is also not required for this rule to apply that the merging corporate entities are entities of the same state. The tax treatment of the shareholders would be equal to Sec. 13 RTA, which means that the shares in the receiving company can be taken over	Sec. 1(1) no. 1 RTA Sec. 12(2) CITA

by the shareholders of the transferring company at book value of the shares in the merged company (transferring company) provided that Germany maintains the taxation right for the shares. This rule is not applicable for a division/partial division of a company in a third State. As a result, in case of a merger of companies from the same third State, the tax treatment would be comparable to the benefits of a merger under the Merger Directive.	

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
<u>**2.1 The term 'securities'**</u> <u>2.1.1 Concept</u> With respect to securities ('*Anteile*') in the meaning of the RTA reference can be made to the definition in the RA and to German company law like the SCA. Securities mean in case of a *corporation* a share in the registered equity and in case of other legal entities the rights representing the membership in this legal entity. German administrative guidelines further clarify that the term 'securities' refers to shares in a corporation as well as to memberships for example in case of a mutual insurance society ('*Versicherungsverein auf Gegenseitigkeit*'). We would like to note that in the German tax literature it is controversially discussed if '*Genussrechte*' (jouissance rights) would fall under the term '*Anteile*' in the meaning of the RTA. In case of a merger or a division/partial division the RTA refers to securities of the receiving company, which can either be new shares ('*neue Anteile*') of the receiving company or existing shares of the receiving company which it holds. In case of a 100 per cent upstream merger no shares are issued. In case of a transfer of assets and an exchange of shares the RTA only refers to new securities of the receiving/acquiring company which means new shares issued in exchange of a contribution in kind. <u>2.1.2 Conclusion</u> The national definition of the term '*Anteile*' (shares) is compliant with the term 'securities'. However, the requirement to issue new shares in respect of transfers of assets and exchanges of shares is not stipulated in the Merger Directive. As a consequence, German tax law disallows for such reorganizations the benefits of the Merger Directive if the acquiring company does not increase its registered capital. As such a requirement is not mentioned in the Merger Directive and can also not be interpreted in the Merger Directive the requirement under German law to issue new shares is not regarded as being compliant.	Sec. 13(1) RTA Sec. 15(2) 4th sentence RTA, (Ministry of Finance Circular of March 25, 1998, ref. 13.02) Sec. 20(1) RTA Sec. 21(1) RTA Sec. 2 RA

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' 2.2.1. Concept It must be distinguished between the treatment of cash payments under the RA and under the RTA. 2.2.1.1 RTA The RTA does not provide for a 10 per cent cap or any other cap on cash payments for any reorganization. The 10 per cent cap can only be indirectly applicable for mergers/divisions/partial divisions as Sec. 1 RTA provides that the RTA only applies to mergers/divisions/partial divisions within the meaning of the RA. For the exchange of shares no cap for cash payments exists. For the tax treatment of payments (other considerations in the meaning of the RTA) see 8.2 below. 2.2.1.2 RA Only for the specific case of a reorganization without an increase of capital the RA provisions for cash payments exist for mergers, divisions and partial divisions in Sec. 54 (4) RA, Sec. 68 (3) RA and Sec. 125 RA. According to these provisions additional cash payments stipulated in the merger/division/partial division agreement must not exceed one-tenth of the total value of the shares granted in the receiving company. This 10% cap has been interpreted as applying on an overall basis, i.e. as allowing a cash buy-out of minority shareholders. The cap is not applicable for the improvement of the share exchange ratio determined by the court in accordance with provisions of the German Act on Appraisal Proceedings (Sec. 15 RA). 2.2.2 Conclusion Germany exercises its option not to implement any cap on cash payments within the RTA which is compliant with the Merger Directive.	Sec. 54(4) RA Sec. 68(3) RA Sec. 125 RA Sec. 15 RA Sec. 11(2) no. 3 RTA Sec. 20(1), (3) 3rd sentence RTA Sec. 21(1) 3rd sentence RTA Article 2 lit. a Merger Directive Article 2 lit. c and d Merger Directive (Ministry of Finance Circular of March 25, 1998, ref. 11.05/08)

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
<u>2.3 Further types of merger</u> <u>2.3.1. Transfer of assets and liabilities from and to specific legal entities</u> The RTA extends the merger rules to a specific transfer of assets and liabilities between certain legal entities as defined in the RA without the exchange of securities representing the capital of the other legal entity or a membership right, respectively (‘*Vermögensübertragung*’). It also extends the rules applicable for divisions/partial divisions to the partial transfer of assets and liabilities (‘*Teilübertragung*’), but not to the transfer of assets in exchange for shares. A complete/partial transfer of assets and liabilities shall each time only be possible (a) by a corporation (‘*Kapitalgesellschaft*’) to the Federal Government (‘*Bund*’), a State Government (‘*Bundesland*’), a Regional Authority or an Association of Regional Authorities; (b) by a stock insurance company to mutual insurance societies or public law insurance companies; (c) by a mutual insurance society to stock insurance companies or public law insurance companies; (d) by a public law insurance company to stock insurance companies or mutual insurance societies. <u>2.3.2 Merger with partnerships</u> The RTA also applies to mergers from a company to a partnership or individual and to a conversion of a company into a partnership (Sec. 3 to 10 RTA). It also provides for rules for the transfer of branches of activities, interests in a partnership into a partnership (Sec. 24 RTA) and the transformation of a partnership into a company (Sec. 25 RTA which stipulates that Sec. 20 to 23 RTA apply *mutatis mutandis*). Even if these types of reorganizations are not covered by the Merger Directive there are single commentaries in the tax literature stating that because the intention of the SETI Act was to bring the RTA in compliance with EC law at least all types of reorganizations in the RTA must be interpreted in the light of EC law. This interpretation is of relevance for our survey in case of pure national reorganizations (reorganizations for which the Merger Directive and Primary EC law is directly not applicable) and reorganization of types of entities not covered by the Merger Directive (e.g. partnerships under German company law). In our view based on the intention of the German legislator as well as the judgments of the ECJ in cases C-197/89 ‘*Dzodzi*’ and especially C-28/95 ‘*Leur-Bloem*’ this interpretation can only be followed for types of reorganizations covered by Article 1 to 3 of the Merger Directive and for	Sec. 11(1) 1st sentence RTA Sec. 15(1) 1st sentence RTA Sec. 174(1), (2) RA Sec. 175 RA Sec. 3 ff. RTA

such provisions applicable for both, domestic reorganizations and reorganizations covered by the Merger Directive/Primary EC law. 2.3.3 Conclusion As a result we do not share, for example, the view that national reorganizations not covered by the Merger Directive itself must be interpreted in the light of the Merger Directive. For example, the taxation rules for a distribution of equity in case of a merger of a corporation into a partnership (Sec. 7 RTA and Sec. 8a CITA providing for a treatment of 5 per cent of the profits as non deductible expenses in case of corporate shareholders) cannot be treated in a broader context as a violation of the Merger Directive. However, if a provision in the RTA is applicable for a reorganization covered by the Merger Directive as well as for a domestic reorganization we are of the opinion that the '*Leur-Bloem*' principle should apply, i.e. a common interpretation of the technical term should be used.	

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares To determine whether or not the contribution is a qualifying exchange of shares, i.e. one that qualifies for the relief, all contributions forming part of a single transaction (contribution in kind to establish the acquiring company or one and the same increase of the registered capital of the acquiring company) will be included in determining the exchange is a qualifying exchange. An exchange will be a qualifying exchange if the conditions are met with respect to the acquiring shareholder after that transaction.	Sec. 21(1) 2nd sentence RTA

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
2.5 Consolidation of qualifying holding If the acquiring company already owns a majority holding any further exchanges of shares (including the contribution of non-voting shares) would be treated as a qualifying exchange of shares.	Sec. 21(1) 2nd sentence RTA

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 *'Andersen og Jensen'*. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
2.6 The term 'branch of activity' 2.6.1 The domestic concept The RTA uses the term '*Teilbetrieb*' for a branch of activity and '*Betrieb*' for all branches of activities of a company. The term is also found in Sec. 15 ff. ITA. In the RTA '*Teilbetrieb*' is mentioned in context with the rules applicable for division and the rules applicable for the transfer of assets. The term is not defined. In this context it is our understanding of the Merger Directive that branch of activity (*'Teilbetrieb)'* has the same meaning for division and transfer of assets, i.e. for the application of the Merger Directive both forms of reorganization require that a branch of activity (*'Teilbetrieb'*) will be contributed. According to the interpretation of the tax authorities a contribution of a '*Teilbetrieb*' is only met where all essential assets of a business are contributed. Assets not essential for that particular business may be held back. The question whether or not an asset is essential for a '*Teilbetrieb*' will be determined on the basis of its function for the business contributed (so-called functional view). 2.6.2 Potential conflicts 2.6.2.1 Concept German commentators of the RTA are of the opinion that the definition 'branch of activity' and '*Teilbetrieb*' might principally differ with respect to the following: (a) the requirements for an independent business; (b) the qualifying assets to be transferred; (c) the allocation of assets which do not qualify per se as assets of a branch; (d) the allocation of liabilities. These are discussed in more detail below: 2.6.2.1.1 Separated Business The Merger Directive defines a branch of activity from an organizational point of view only, that is to say an entity capable of functioning by its own whereas the '*Teilbetrieb*' also requires that the branch is effectively separated from any other branches at least at the merger date.	Sec. 15(1) 1st sentence RTA Sec. 20(1) RTA (see Ministry of Finance Circular dated March 25, 1998, ref. 20.08) (see Ministry of Finance Circular dated March 25, 1998, ref. 15.08)

<u>2.6.2.1.2 Qualifying Assets</u> The Merger Directive does not require that the legal ownership of the qualifying assets is transferred. It is sufficient that the use of such assets by the branch is sufficiently secured. However, for the transfer of a '*Teilbetrieb*' the transfer of the legal title of all essential assets is required. This might have the consequence that, in case of assets which cannot be divided but are essential assets for more than one '*Teilbetriebe*' ('*spaltungshindernde Wirtschaftsgüter*'), a division/partial division is excluded. For the determination of which assets belong to a branch, the Merger Directive focuses on the perspective of the acquiring company, whereas the term '*Teilbetrieb*' focuses on the perspective of the transferring company. For the determination of which assets belong to a branch under the Merger Directive, reference is made to the relationship of the assets to the branch (*'Andersen og Jensen'*, paragraph 24: A transfer of assets must encompass all the assets and liabilities relating to a branch of activity. Only an entity capable of functioning by its own means constitutes such a branch). The '*Teilbetrieb*' refers to the functional need for the branch only. In case of a '*Teilbetrieb*' assets will be categorized as essential assets, non essential assets and neutral assets (see also under 'Allocation of Liabilities' below). <u>2.6.2.1.3 Allocation of Assets</u> For the transfer of a branch in the meaning of the Merger Directive it is not relevant whether or not and to what extent the assets transferred carry hidden reserves. For the definition of the '*Teilbetrieb*' the situation is less certain. <u>2.6.2.1.4 Allocation of Liabilities</u> For the transfer of a branch in the meaning of the Merger Directive it is necessary that the assets and liabilities relating to a branch of activity should be transferred in their entirety. If the transferring company retains the proceeds of a large loan contracted by it and transfers the obligation deriving from that loan to the company to which the assets are transferred, those two elements are dissociated (*'Andersen og Jensen'*, paragraph 25, 26). For the term '*Teilbetrieb*' liquid assets, receivables and liabilities are in principle so-called neutral assets, i.e. their allocation to branches is within the discretion of the transferring company. <u>2.6.2.2 Conclusion</u> The tax authorities outlined in the Circular of August 16, 2000, that '*Teilbetrieb*' in the meaning of the RTA must be interpreted commonly according to the national law. That means German tax authorities would interpret the term '*Teilbetrieb*' in the meaning of the Merger Directive in the same way as the term '*Teilbetrieb*' according to national law. In our view this is not compliant with the Merger Directive as the term '*Teilbetrieb*' as defined in Article 2(i) Merger Directive appears to be much	(see Ministry of Finance Circular dated August 16, 2000)

broader than the German definition. Due to this uncertainty in practice, companies have been forced to request a binding opinion from the tax authorities to avoid tax risks caused by different interpretations. 2.6.3 Application of the Merger Directive on domestic reorganizations 2.6.3.1 Concept As far as the provisions in the RTA apply simultaneously to domestic and international reorganizations some German commentators are of the opinion that the interpretation of terms might be different. They hold the position that this view should not violate EC law as outlined in the Case C-28/95 '*Leur-Bloem*', paragraph 32 because the German legislator accepted a different view of domestic and international reorganizations under the RTA. He wanted on the one side to apply the common understanding of the '*Teilbetrieb*' in a domestic context and on the other side implement the definition of the branch in the meaning of the Merger Directive, but only for international reorganizations. 2.6.3.2 Conclusion We are of the opinion that for domestic reorganizations the RTA must be interpreted in the light of the Merger Directive as far as domestic and cross-border transactions are covered by one and the same provision (see 2.3.3).	

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
3.1 Types of entities German legislation applies the Merger Directive to all companies established in accordance with the legislation of a Member State or any EEA State within the meaning of Article 48 EC and Article 34 of the EEA Agreement whose registered office and place of management are located within the territory of any of these States. Therefore, at least all companies listed in the Annex are principally covered.	Sec. 1 (2) no. 1, 2 RTA

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
3.2 Transparent entities German tax law only recognizes foreign companies as corporations in the meaning of the German corporate tax law if they meet the so-called '*Typenvergleich*', which is a comparison test that compares the legal characteristics of the foreign corporation in question with the legal	Sec. 1 (1) CITA

characteristics of a German corporation subject to Sec. 1 (1) CITA (see no. 4.8). This test applies to companies involved in mergers, divisions, partial divisions and share exchanges in the same way. The categorization under foreign tax law has no impact on the qualification of the entity under German tax law. Example: The Hungarian partnerships (közkeresti társaság/kkt and betéti társaság/bt) are listed in the Annex of the Merger Directive under lit p and are subject to corporate income tax in Hungary, but are principally treated as transparent partnerships for German tax purposes.	

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
<u>3.3 Qualification of tax residency</u> <u>3.3.1 Tax residency under domestic law</u> A corporation is tax resident in Germany if its place of management and/or its statutory seat are in Germany. <u>3.3.2 Tax residency under DTCs</u> German DTCs provide for the following tie-breaker criterion to determine the tax residency of a corporation: Where by reason of tax residency on grounds of place of management or any other criterion of a similar nature a person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident only of the State in which its place of effective management is situated. <u>3.3.3 Statutory seat under domestic company law</u> A corporation can be reorganized under the RA if its seat is in Germany. Seat should be defined as the statutory seat of the company. In this context the following should be noted: Germany currently follows the seat theory (‘*Sitztheorie*’). Under this doctrine a company incorporated under German Company law must have in principle its place of effective management and its statutory seat in Germany to be recognized as a German legal entity. If it transfers its statutory seat to another country it will be treated as being liquidated. The same applies in case of a transfer of its place of effective management with the exception that the company remains in existence if the state to which the place of effective management has been transferred follows the incorporation theory (‘Gründungstheorie’). In this case the company remains in existence as a legal entity and remains a qualifying entity under the RA/RTA. According to a new proposal released by the Federal Ministry of Justice on January 7, 2008 (‘Referentenentwurf Gesetz zum Internationalen	Sec. 1(1) CITA Sec. 1(1) 1st sentence no. 1 and 3 RTA Sec. 1 RA Article 4 (3) of various German DTCs (Circular of March 25, 1998, ref. 01.03 for dual resident companies)

Privatrecht der Gesellschaften, Vereine und juristischen Personen') Germany will introduce the incorporation theory by the end of 2008. In case a foreign company transfers its place of effective management to Germany and if the Member State where the company has its statutory seat follows the incorporation theory, the company will be recognized under German law as a foreign legal entity. The SE and SCE can transfer their statutory seat within the EU (see Article 8 SE-Regulation and Article 7 SCE-Regulation). Such transfer does not lead to a liquidation of the respective entity nor to the creation of a new juridical entity.	

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject-to-tax clause 3.4.1 Concept The subject-to-tax clause of Article 3(c) Merger Directive was not implemented in the RTA. As a result, the RTA applies in principle also to a merger or a division/partial division including corporations which are (partially) exempt from corporate income tax but listed in Article 3(c) of the Merger Directive. However, in case the receiving company is tax exempt with an asset received (the German taxing right for a gain on the disposal or use of an asset is excluded or limited after the transfer) the transferring company must value the transferred asset at its fair market value, and any capital gain would be taxed. This is because it is not assured that the asset will be subject to corporate taxation at the level of the receiving company 3.4.2 Conclusion This limitation is within the scope of Article 3(3) Merger Directive. The implementation is in accordance with Article 3(c) Merger Directive.	Sec. 1 RTA Sec. 11(2) no. 1, 2 RTA

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
3.5 Shareholder requirements The ownership of a company by EU or EEA nationals or residents is not relevant for the application of the RTA.	Sec. 1 RTA

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
4.1 The concepts of 'real values' and 'value for tax purposes' 4.1.1. Interpretation 4.1.1.1 Real value The RTA in the now amended version through the SETI Act uses the term 'real value' as fair market value of the assets and liabilities ('gemeiner Wert'). This is the value to be paid by selling the single asset at market price. This value principally includes a profit mark up. The valuation at fair market value does not take into account any valuation made under foreign law. Some elements for the determination of the real value are subject to discussion in the tax literature and, as yet, there is no consensus. Furthermore, there is no administrative guidance existing interpreting the concept of real value of the Merger Directive. As an exception from this rule goodwill will be determined as the difference between the value of the branch of activities transferred as a whole and the sum of the values of the assets and liabilities. The value of the branch of activities transferred will be determined on the income approach ('Ertragswertverfahren' following the principles of IDW S1-Standards). The fair market value of the assets and liabilities cannot exceed the value of all branches of activities, which means that a negative goodwill could be generated under certain circumstances. We note that this valuation differs from the valuation of an asset under the going concern method ('Teilwert'), as used in the original implementation law (i.e. the Tax Amendment Act 1992). According to the going concern method the 'value' would on the one hand not include a profit mark up but on the other hand take into account the value of that asset to the business. 4.1.1.2 Value for tax purposes 'Value for tax purposes' has been interpreted as the tax book value of the assets in the books of the transferring company at the time of the merger, division or partial division. As an exception to this rule intangible assets not acquired for a consideration or self-developed will be taken into consideration. 4.1.1.3 Conclusion In our view the valuation at fair market value of the single asset could be regarded as a potential violation of the concept of real value under Article 4 of the Merger Directive as it includes, for example, a profit mark up. The intention of the Merger Directive is not that single assets will be transferred but principally branches of activities. Based on this concept	Sec. 11(1) 1st sentence, and Sec. 11(2), 1st sentence RTA Sec. 15(1) 1st sentence, 2nd sentence RTA Sec. 9(2) Valuation Act (Regierungsentwurf des SEStEG v. 12.7.2006, BT-Drs. 16/2710, 37) Sec. 10 Valuation Act Article 4 Merger Directive

the valuation at going concern values should be the appropriate concept. <u>4.1.2. Implementation</u> <u>4.1.2.1 Concept</u> The value concept has been transposed in domestic law by the following concept: In case of a merger, division or partial division the transferred assets may be uniformly reported at book value or any higher value, however, at maximum at their fair market value in the closing tax balance sheet of the transferring company. The valuation below the fair market value is dependent from the following requirements: (a) it is assured that the assets will later be subject to corporate income tax with the receiving corporate entity, (b) the right of Germany to tax the gain on the disposal of the transferred assets with the receiving corporate entity is not excluded or limited, and (c) there is no consideration, or the consideration consists in shares. <u>4.1.2.2 Conclusion</u> For the incompliance of the concept see under 4.7 below.	

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
<u>4.2 Specific guidance for divisions/partial divisions</u> <u>4.2.1 Concept</u> The valuation of assets in case of divisions and partial divisions follows the same rules applicable for mergers. In case of a division, the Merger Directive requires the transfer of all of the assets and liabilities of the transferring company to two or more existing or new companies. Under the RTA it is required for a division that the assets transferred must each be branches of activities (‘*Teilbetriebe*’). <u>4.2.2 Conclusion</u> It is has been discussed by German commentators whether or not a tax-neutral division requires that always branches of activities must be transferred although no consensus has been formed. In our view a differentiation between the partial division, which requires that at least one branch of activity must be retained by the transferring company and at least one branch of activity must be transferred to the acquiring company, and a division is not justified. The division requires the transfer of branches of activities to the acquiring companies involved. Article 2 lit.	Sec. 15 (1) 1st sentence RTA

f of the Merger Directive states that the receiving company must either receive (all) assets and liabilities or one or more branches of activity.	Article 2 lit. f of the Merger Directive

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' 4.3.1. Concept of 'permanent establishment' According to the RTA the valuation below the fair market value is inter alia dependent from the assurance that the assets will later be subject to German corporate income tax with the receiving company and that the right of Germany to tax the gain on the disposal of the transferred assets with the receiving company is not excluded or limited. To be taxable in Germany the assets of a foreign company must be allocated to a permanent establishment of the receiving company in Germany following German domestic tax rules as well as the applicable German DTC, if any. According to domestic law, under Sec. 12 1st sentence GTC every fixed business facility or installation serving a business purpose is a permanent establishment. 4.3.2. Concept of 'effectively connected' The concept of the allocation of assets effectively connected with a permanent establishment is outlined in the Circular of December 24, 1999, ref. 2 to 4. No. 2.4 states the following: Business assets may only be allocated either to the head office or to the permanent establishment. The positive and the negative business assets which are used only by the permanent establishment are allocated to it (functional approach). Above all, this includes business assets which are to be exclusively exploited and used by the permanent establishment. Such business assets from which income is derived and for whose generation the permanent establishment's activity has largely contributed are also to be allocated to the permanent establishment. For the allocation of the assets the actual circumstances and particularly the structure, organization and functions of the permanent establishment in the entire enterprise are decisive. If the business assets fulfill the function attributed to them (functional approach) both as part of the business assets of the head office and of a permanent establishment, then management must decide where assets are allocated (formal approach) (Federal Tax Court of April 1, 1987, Federal Tax Gazette 1997 II p. 550); entries on the books are only indicative, and do not absolutely determine the allocation. Possible revenues or expenses arising from this determination are to be	Sec. 11(1) 1st sentence, and Sec. 11(2) 1st sentence RTA Sec. 15(1) 1st sentence RTA Article 4(1) lit. b Merger Directive Sec. 12 1st sentence GTC (Federal Fiscal Court of July 29, 1992, Federal Tax Gazette II 1993 p. 63) (see Ministry of Finance Circular of December 24, 1999, ref. 2.6.1.)

apportioned between head office and permanent establishment according to actual use. This also applies in the case of these business assets being disposed of. The income earned by a permanent establishment generally belongs to its business assets to the extent that they are used as part of the permanent establishment's business activity or finance investments concluded or provided for in the foreseeable future. The surplus means going beyond that are to be allocated to the head office. An allocation of business assets to a permanent establishment using such business assets does not apply, if (a) the business assets are only temporarily relinquished to the permanent establishment and if this relinquishment would have occurred between third parties on the basis of a hire, lease or similar legal relationship, or (b) the business assets are such that they are used by several permanent establishments simultaneously or successively, and their expenditures and revenues are allocated in accordance with an apportionment procedure within the enterprise. Following the view of a functional allocation of assets between the head office and a permanent establishment, goodwill and other intangible assets as well as tangible assets serving the company as a whole cannot be allocated to a single permanent establishment, but should principally be allocated to the head office (so called central function of the head office ('Zentralfunktion des Stammhauses'). According to the opinion of the German tax administration it is principally not possible to allocate functions like financing, holding or licensing to a permanent establishment. <u>4.3.3 Conclusion</u> We consider the extensive allocation of assets to the head office by the principles elaborated by the German tax administration (functional approach) as being potentially incompliant with Article 4 (1) lit. b of the Merger Directive as it would lead to a significant restriction of a tax exempted EC outbound merger in contrast to the more practical approach of the formal method. In practice, to avoid significant tax exposures either a pre-merger structuring could be required or the request for a binding rule must be filed. As an example for the former possibility, the transferring company could transfer branches of activities including the financing, holding and licensing functions at book value to a partnership in exchange for an interest in the partnership before merging into a company tax resident in another Member State.	

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief 4.4.1 Concept The RTA provides for a recapture provision in case of shares in the receiving company owned by the transferring company. Such shares are to be reported at least at book value increased by tax effective depreciation (could be created until the year 2001) as well as deductions resulting from roll-over relief (Sec. 6b ITA, could be created before the year 1999) and similar tax-effective deductions made in previous years, at maximum at fair market value. The impact of this rule is limited especially because of the general applicable tax recapture clauses in case of prior depreciation and the expiration of the above mentioned rules. The profit thereof is part of the principally taxable transferring profit ('Übertragungsgewinn') of the transferring company but is tax exempt under Sec. 8b (2) 4th and 5th sentence CITA with the exception that 5 per cent thereof will be treated as non-deductible expenses. 4.4.2 Conclusion The 5 per cent rule leads to a taxation of 5 per cent of the resulting profit. The Merger Directive states under Article 4 (1) lit. a that a merger or division shall not give rise to any taxation of capital gains calculated by reference to the difference between the real value of the assets and liabilities transferred and their value for tax purposes. The recapture clause results in an adjustment of the value for tax purposes as outlined in Article 4 (1) lit. a of the Merger Directive. In our view, it is doubtful whether the provision is compliant with the Merger Directive because the shares in the receiving company remain in existence after the merger and, therefore, there is no factual need to disclose hidden reserves in such shares (the situation would be different in case of a merger and shares of the transferring company owned by the receiving company).	Sec. 11(2) 2nd sentence RTA Article 4(1) lit. b Merger Directive Sec. 8b (2) 4th and 5th sentence CITA

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment 4.5.1 Concept In case Germany would lose the right to tax the gain on the disposal of the transferred assets with the receiving company or such right would be limited, the respective transferred assets, including any intangible assets not acquired for a consideration or self-developed must be valued at fair market value in the closing balance sheet of the transferring company and	Sec. 11(2) RTA

will be taxed. 4.5.2 Conclusion For the valuation of this rule as doubtfully compliant with EC law see below no. 4.7.	

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company 4.6.1 Concept The RTA provides that the share of the merger profit equal to the holding of the receiving company in the transferring company would follow the rules applicable for the taxation of capital gains from the disposal of shares. As a result such portion of the merger profit would be tax exempted, however 5 per cent thereof would be treated as non deductible expenses. This would result in a taxation of 5 per cent of the respective portion of the merger profit. 4.6.2 Conclusion As the 5 per cent rule is not included in the Merger Directive this provision is incompliant with Article 7 (1) of the Merger Directive insofar as the receiving company holds a qualifying majority in the transferring company (currently 15 per cent, as from 2009 10 per cent).	Sec. 12(2) 2nd sentence RTA Article 7(1) Merger Directive Sec. 8b CITA

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral 4.7.1 Concept The German legislator took the position that the principles outlined by the ECJ in the case C-470/04 '*N*' only apply to individuals and have no impact on the interpretation of the Merger Directive. According to the judgment of the ECJ in the '*N*' case, para. 39, the exit taxation could hinder the exercise of the freedom of establishment which required that the former state of residence of the taxpayer had to postpone the taxation to the date of the disposal of the asset. Even if this case applies to an individual who transferred its place of residence to another Member State and not to a transfer of assets to another Member State and another company as a result of a merger, division or partial division the reasoning behind the judgment can in our view be applied to such transactions.	Sec. 11(1) (2) RTA Sec. 15(1) 1st sentence RTA Article 4(1) Merger Directive

The taxation of the aforementioned assets at the merger date goes in our view beyond what is necessary to attain the objectives it pursues and could be avoided by granting the receiving company the right to postpone the tax payment as it is the case for the exit tax according to Sec. 6(5) FTA or by setting up a deferred item comparable to Sec. 4g ITA. Based on the latter rule the taxpayer may on request set up a deferred item in the amount of the difference between the book value and the fair market value for a fixed asset in so far as the asset is to be deemed withdrawn from his business as a consequence of its allocation to a permanent establishment of the same taxpayer in another Member State resulting in a loss or limitation of the German taxation right with respect to subject asset. The deferred item has to be reversed in the fiscal year of its formation and in the following four fiscal years by each time one-fifth with profit-increasing effect. The provision is subject to certain requirements, inter alia the taxpayer has to keep records showing the setting-up and reversal of the deferred items. He shall also be obligated to inform the tax authorities immediately of events resulting in a full reversal. The German legislator argued that an immediate taxation would be required because a tax deferral would be difficult to administer within the EU. Despite of Directive 76/308/EWG and Directive 77/799/EWG a collection of taxes in another Member State would not be possible. German commentators take the position that the concept to tax the transfer of all assets not effectively connected with a permanent establishment of the receiving company in Germany is in accordance with the Merger Directive but it is not clear whether or not a tax deferral is required in the light of Article 43 and 48 EC. <u>4.7.2 Conclusion</u> In our view the immediate taxation of such assets is doubtfully compliant with Article 43 and 48 EC. This applies to all reorganizations available under the Merger Directive.	(Explanatory memorandum SETI Act, BT-Drs. 16/2710, 26)

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
<u>4.8 Criteria to determine tax transparent entities</u> <u>4.8.1 Concept</u> The criteria by which an entity is defined as transparent can be found in the Ministry of Finance Circular of March 19, 2004 in connection with a discussion of the qualification of a US LLC. The criteria listed (i.e. the management by the shareholders or by non-shareholders, the kind of shareholders' contribution – cash, in kind and/or services provided for the company –, the limited or unlimited liability of the shareholders, the kind of termination of the company, the possibility to transfer ownership rights) refer to the legal characteristics of the entity and can be used as general guideline for the categorization of foreign entities, which must be done for	Sec. 20(8) RTA Article 43 and 48 EC (Federal Law Gazette 2004 I p. 411)

each single entity. Some additional guidance and help come from Table 1 and 2 which are attached to the Ministry of Finance Circular of December 24, 1999. These two tables list for a large number of foreign countries the legal entities which are commonly known in the respective country, and they show the comparable German legal entity. Thus, these tables serve as a guideline in determining the comparability of a foreign legal entity with the German legal entities. The RTA provides that in the event that a non-resident transferring or acquired company within the meaning of Article 3 Merger Directive is to be considered as fiscally transparent, the foreign tax which would have been levied pursuant to the legislation of the other Member State if the transferred assets to be attributed to a permanent establishment located in another Member State had been disposed of at fair market value is, by virtue of Article 10a Merger Directive, to be credited against the corporate income tax or income tax allocable to the transfer profit (by appropriately applying Sec. 26(6) CITA and Sec. 34c and Sec. 50(6) ITA). As a result of the tax transparency principle, tax transparent entities will be treated as it is the case for partnerships which are under German tax principles tax transparent entities. In case of tax transparency it is decisive if the income /assets can be allocated to a foreign permanent establishment or not. For income from a foreign permanent establishment German DTCs principally apply the tax exemption method. Only in case of so-called passive income the tax credit method applies resulting in a German taxation right. Article 10a Merger Directive is only of relevance for such assets/income which cannot be allocated to a foreign permanent establishment or, if the income/asset is allocated to a foreign permanent establishment, for which the tax exemption method is not applicable. In both cases the German tax treatment could be potentially incompliant because of the taxation of assets (see in detail under no. 4.7.1) and the limited benefit under the German tax credit method (see in detail under no. 10a. 3). 4.8.2 Conclusion For the reasons outlined under no. 4.7.1 and no. 10a.3 it is doubtful if the immediate taxation and the limited benefit from the tax credit is compliant with Article 43 and 48 EC.	(Federal Law Gazette 1999 I p. 1076)

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief 4.9.1 Concept The receiving company shall inherit the tax attributes regarding the valuation of assets, the depreciation method, the reserves reducing the profits for tax purposes, etc. of the transferring company. In addition, the period for which the business assets and liabilities of the transferring	Sec. 12(3) RTA Sec. 15(1) 1st sentence RTA

company were held shall also be transferred to the receiving company. 4.9.2 Conclusion The implementation is in accordance with Article 4 of the Merger Directive.	

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
5.1 The term 'provisions and reserves' The term 'provision' follows German GAAP and is used in Sec. 249 GCC. Provisions must be set up especially for uncertain liabilities and for anticipated losses from uncompleted transactions. For tax purposes provisions will only be recognized if they meet the requirements of the ITA, for example of Sec. 6 (1) no. 3 lit. a ITA and Sec. 6a ITA. See also Sec. R 5.7 ITR. For example, provisions for anticipated losses from uncompleted transactions will not be recognized for tax purposes. Reserves are defined in Sec. 272 GCC. Reserves can only be created with taxable effect if specifically mentioned in the ITA or in administrative guidelines (see Sec. R 6.6 (4) ITR). For example, Sec. 6b (3) 1st sentence ITA allows the creation of a tax free reserve in the amount of capital gains realized by the disposal of certain assets. This reserve serves the transfer of hidden reserves of the disposed asset to other specific assets which the taxpayer must acquire within a four-year period.	German GAAP Sec. 249 GCC Sec. 272 GCC Sec. 6 (1) no. 3 lit. a ITA; Sec. 6a ITA; Sec. R 5.7 ITR Sec. 6b (3) 1st sentence ITA

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments There is no specific regulation in the RTA as German tax authorities require the application of the direct method to calculate profits of a permanent establishment. Because all of the DTCs between Germany and the other 26 Member States provide in principle for the exemption method for permanent establishments in the other Contracting State, the distinction is only of relevance if the exemption method is subject to an activity clause (for example this is the case with Portugal and Hungary) and if this condition is not met. The German DTCs contain a variety of different activity clauses. Based on an activity clause the tax exemption of certain income from the other Contracting State to the DTC will not apply and the income will be subject to taxation in Germany and the foreign taxes can be credited. For example, the tax exemption of income from a foreign permanent	Sec. 11 (3) RTA Sec. 15(1) 1st sentence and Sec. 3 (3) RTA

establishment may not be granted if the German resident cannot prove that the receipts of the permanent establishment are derived exclusively or almost exclusively from producing or selling goods or merchandise, rendering services, or doing banking or insurance business within the other Contracting State (see Article 23 (1) lit. c DTC Hungary). In such a case tax effective provisions and reserves derived from the permanent establishment abroad must be disclosed in the closing tax balance sheet of the transferring company.	

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
<u>5.3 Allocation method for provisions and reserves</u> For the determination of what assets must or can be allocated to a '*Teilbetrieb*' a distinction is to be made between essential assets ('wesentliche Betriebsgrundlagen') and non-essential assets ('nicht wesentliche Betriebsgrundlagen') and neutral assets ('neutrales Vermögen'). Neutral assets can in principle be allocated in their entirety to a '*Teilbetrieb*'. For example, neutral assets are cash, receivables and liabilities. With respect to liabilities this applies irrespective of whether or not the securities for the obligation are allocated to a '*Teilbetrieb*', or irrespective of the purpose for which funds were raised. As an exception to this rule according to statements of the tax administration certain provisions should be allocated as follows: (a) Provisions for pensions should be allocated to the '*Teilbetrieb*' to which the employees entitled to the pension rights belong to or did belong to. (b) Liabilities resulting from a current employer-employee relationship must be allocated to the '*Teilbetrieb*' which takes over the employment contracts. The aforementioned examples must be interpreted under the functional approach method generally applied by the German tax authorities.	Sec. 15 RTA (Circular of the Ministry of Finance dated March 3, 1999 Federal Tax Gazette I 1998 p. 268 ref. 15.08) (Circular of the District Tax Office Magdeburg dated January 11, 1999, GmbHR 1999, p. 254) (Circular of the District Tax Office Hannover dated October 26, 2000, GmbHR 2000, p. 1275)

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
<u>5.4 Further conditions for carry-over of provisions and reserves</u> <u>5.4.1 Concept</u> With respect to provisions for pensions the RTA provides an exception to the rule that the valuation follows the real value concept by appropriately applying Sec. 6a ITA which provides for the provision of pensions a valuation under the going concern concept (for example an interest rate of 6 per cent p.a. must be used for the valuation of the pension rights).	Sec. 3(1) 2nd sentence RTA Sec. 11(1) 2nd sentence RTA Article 4(1) Merger Directive Article 5 Merger

The valuation is based on very specific requirements outlined in the ITA and additional administrative guidelines. It regularly results in a value significantly below fair market value. As a result of this hidden charges are not considered for a valuation according to the RTA. We consider disregarding hidden charges as a violation of the principle of tax neutrality of reorganizations under the Merger Directive. 5.4.2 Conclusion The valuation of pensions under German tax law is potentially incompliant with Article 4(1) and Article 5 of the Merger Directive.	Directive

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry over of losses 6.1.1 Concept With the SETI Act Germany abolished Sec. 12 (3) RTA 1995 stating that the receiving company in a merger or division/partial division could have taken over any remaining loss relief on the condition that the business or part of the business that caused the loss continued to operate at a comparable level taking all business relationships into account, for a 5 year period following the date of the merger. Under the new regime any remaining losses/loss carry forwards of the transferring company cannot be taken over by the receiving company. As a result of this no carry over loss rule is existing for a domestic merger or division/partial division under the RTA which must be extended to cross border mergers or foreign mergers under the Merger Directive. In our view this approach should principally be in line with the Merger Directive. However, in practice this concept may discriminate foreign investors and be incompliant with Primary EC law. Usually foreign investors operate with permanent establishments or subsidiaries in Germany. Even if they are in principle entitled to benefit from German tax loss utilization strategies and the German Organschaft concept (disallowed for cross-border structures) in practice only large operations could do so. In order to benefit from the German Organschaft concept (for example use of pre-Organschaft losses of the controlling entity within the German Organschaft concept. By creation of an Organschaft of the controlling/parent company with pre-Organschaft tax loss carry forwards the profits of the controlled company could be offset with the existing tax loss carry forwards of the controlling company.) or from intra-group tax loss refreshing strategies like the disclosure of hidden reserves in years with operating tax losses generally requires extensive business activities in Germany. To complete the picture the following should be noted: As from the year 2008 Germany abolished the thin capitalization rules and introduced the interest limitation rule concept ('Zinsschranke'). According to this concept interest expenses not deductible in the year they occurred	Sec. 12(3) RTA 1995 Sec. 4(2) 2nd sentence RTA Sec. 12(3) RTA Sec. 15(1) 1st sentence RTA Sec. 20(9) RTA Article 43 and 48 EC (C-175/88 *Biehl* para. 13, C-386/05 *Stauffer* para. 31)

because of the limitations applicable under the 'Zinsschranke' can be carried forward and follow in principle the rules applicable for loss carry forwards. According to the RTA such an interest carry forward can also not be carried over to another company like it is the case for losses. Like in regard of the utilization of losses mainly German resident companies could use certain tax strategies to diminish negative tax impacts. Consequently, the disallowance of a loss and interest expense take-over would mainly impact investors from other EC Member States. Taking into account that it is primarily the obligation of the Member State where the losses were incurred to provide for a tax relief it could be argued that this is a hidden discrimination of foreign EC companies in the meaning of the current judgment of the ECJ. 6.1.2 Conclusion Overall there might be reasonable doubts existing that the denial of the loss/interest expense take-over is compliant with Article 43 EC. However, taking into account the current stand of EC Primary law these doubts are in our view not strong enough to evaluate the German principle as doubtfully compliant in the context with the purpose of this survey, i.e. to evaluate the implementation of the Merger Directive into German tax law.	

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment 6.2.1 Concept N/A. (please see 6.1). 6.2.2 Conclusion N/A.	

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets 6.3.1 Concept As a result of the SETI Act, Sec. 15 (4) RTA 1995 had been abolished. According to this provision prior to its change, any remaining loss deduction had to be divided into the portion of the assets transferred compared to the total assets of the transferring corporation prior to the division, as this will generally be expressed in the disclosures to the exchange ratios for the shares in the contract of division or acquisition or in the division plan. According to the revised Sec. 15 (3) RTA in case of a partial division, any	Sec. 15 (4) RTA 1995 Sec. 15 (3) RTA Article 43 and 48 EC

remaining loss carry forward of the transferring company shall be reduced at the ratio at which, taking the fair market value as a basis, the assets and liabilities pass over to another company. A loss carry over to such other company is no longer possible. This applies *mutatis mutandis* to interest expenses carried forward under the interest limitation rules. Because losses cannot be taken over by the receiving company in a domestic division/partly division, there is no carry over loss rule existing which must be extended to cross border divisions/partly divisions under the Merger Directive. 6.3.2 Conclusion Under the same preservations as mentioned above (no. 6.1) we would evaluate this rule as compliant with Article 43 and 48 EC.	

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses 6.4.1 Concept N/A. 6.4.2 Conclusion N/A.	

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Amended holding threshold 7.1.1 Concept The RTA provides that a profit (or loss) in the amount of the difference between the book value of the shares in the transferring company and the value at which the transferred assets are to be taken over, net of the cost of the transfer of assets and liabilities, shall be left out of account with the receiving company. This applies irrespective from a certain shareholding. Sec. 8b CITA shall be applied, providing that the profit within the meaning of the aforementioned rule, net of the proportional share of the cost of the transfer of assets and liabilities allocable to that profit, corresponds to the share of the receiving company in the transferring company. According to Sec. 8b (5) CITA 5 per cent of the gain shall be deemed expenses which must not be deducted as business expenses.	Sec. 12 (2) 1st sentence RTA Sec. 8b (5) CITA Article 43 and 48 EC Article 56 EC

The taxable effect resulting from the 5 per cent rule is that 5 per cent of the gain remains taxable at the level of the receiving company. In contrast to Article 4 (2) of the Parent-Subsidiary Directive the Merger Directive does not provide for a rule that a Member State shall retain the option of providing that a fixed amount of maximum 5 per cent of the capital gain can be regarded as management costs not deductible from the taxable profits. 7.1.2 Conclusion We are of the opinion that the 5 per cent non deductible expense rule is violating the Merger Directive and Article 43 and 48 EC and Article 56 EC.	

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses 7.2.1 Concept According to Sec. 12(2) 1st sentence RTA losses will be disregarded. 7.2.2 Conclusion The concept is in line with EC law.	Sec. 12(2) 1st sentence RTA

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder 8.1.1 Concept In the case of a merger/division/partial division the receiving company must take over the assets at the value shown in the closing tax balance sheet of the transferring company. In case of an exchange of shares the following applies. 8.1.1.1 Taxation at the level of the receiving/acquiring company The value at which the acquiring company assesses the transferred shares	Sec. 12(1), (2) RTA Sec. 15(1) RTA Sec. 21(2) RTA Sec. 8b(2), (3) CITA Sec. 3 no. 40 lit. a, d ITA

shall be deemed the purchase price of the transferred shares. In case of a corporate shareholder the sale of shares in a company is under German tax law exempt from taxation (but 5 per cent of the capital gains are treated as non tax deductible expenses). Therefore, as far as the receiving/acquiring company receives shares, an economic double taxation would be mitigated. <u>8.1.1.2 Taxation at the level of the shareholders</u> The value at which the acquiring company assesses the transferred shares shall be deemed the acquisition cost of the received shares for the transferring shareholder. In case the German right to tax the disposal of either the received shares at the level of the shareholder or the transferred shares at the level of the acquiring company is excluded or limited the shares transferred are valued at fair market value. As an exception to the rule in case of a qualifying exchange of shares on the request of the transferring shareholder the shares received by the transferring shareholder can be valued at book value or any value between book value and fair market value if the profits from the received shares can either be taxed or must not be taxed pursuant to Article 8 of the MD. In the latter case the gain of a subsequent disposal shall be taxed irrespective of a DTC. As a result a double book value carryover can be avoided in a cross border exchange of shares. With respect to a taxation of capital gains on a subsequent disposal of the shares the following applies. For a corporate shareholder any capital gain as well as any dividend income are principally tax exempt (but 5 per cent are treated as non tax deductible expenses). Consequently, the economic double taxation would be mitigated. For individuals, only 50 per cent (as from 2009: 60 per cent in case the shares are held in a business) of the dividend income is subject to taxation. As from 2009, dividends and capital gains from privately held shares are principally subject to a final withholding tax of 25 per cent (in addition 5.5 per cent thereof will be levied as solidarity surcharge). <u>8.1.2 Conclusion</u> The German tax law does not provide for a provision to avoid economic double taxation. However, the principle explained above leads to a mitigation of economic double taxation.	

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>8.2 Computation of the capital gain</u> <u>8.2.1 Concept</u> <u>8.2.1.1 Payment made by the receiving/acquiring company</u>	Sec. 11 (2) 1st sentence RTA 1995 Sec. 11 (2) no. 3 RTA (Ministry of Finance

With respect to a merger the Ministry of Finance Circular of March 25, 1998 stated under ref. 11.06 that cash payments made by the receiving company constitutes consideration in the meaning of Sec. 11 (2) 1st sentence RTA 1995. Under the new RTA such payments would qualify as consideration in the meaning of Sec. 11 (2) no. 3 RTA, and transferred assets must be valued in the closing balance sheet of the transferring company at book value plus the consideration. The consideration will be split between the assets transferred in relation to their fair market values. Commentators to the RTA differ between withdrawing shareholders and remaining shareholders. Only for the latter ones, they would treat the consideration as an additional remuneration for the transfer of the assets. For shareholders being bought out the remuneration would be part of the purchase price for the shares. At shareholders' level the remuneration would be treated for shareholders being bought out as proceeds from the disposal of the shares whereas for remaining shareholders the remuneration would be treated as dividend income. 8.2.1.2 Payment made by the transferring company According to the Ministry of Finance Circular of March 25, 1998, ref. 11.08 payments made to a shareholder of the transferring company by the transferring company are not treated as compensation in the meaning of Sec. 11 (2) RTA. Depending on the facts the transaction will be treated as an acquisition of own shares, a hidden dividend distribution or as a so-called other distribution. In case the shares will be acquired for redemption this will regularly be treated as a hidden dividend distribution. 8.2.1.3 Payments made by the shareholders of the receiving/acquiring or transferring company The payments to withdrawing shareholders by the shareholders of the receiving/acquiring or transferring company are not consideration in the meaning of Sec. 11 (1) no. 2 RTA 1995. They will be treated as proceeds for the disposal of the shares by the withdrawing shareholders and as acquisition costs at the level of the paying shareholders. 8.2.2 Conclusion In our view, the treatment of payments to shareholders by the receiving/acquiring company as additional remuneration for the transfer of assets is compliant with Article 4(1) and Article 8(1), (7) of the Merger Directive.	Circular issued March 25, 1999, ref. 11.05 to 11.11) Article 4 Merger Directive

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
8.3 Further conditions for tax relief	Sec. 13(2) no. 2 RTA Sec. Sec. 15(1)

8.3.1 Concept The shares in the receiving company are on request to be accounted for at book value of the shares in the transferring company if Germany has to apply Article 8 (6) of the Merger Directive. In case the merger results in a loss or limitation of the taxing right for the shares transferred, Germany taxes a gain from any subsequent disposal of the acquired shares in the same way as the disposal of the shares in the transferring company would have to be taxed. This applies irrespective of the provisions of a double tax convention. The rule applies *mutatis mutandis* to a division, partial division and exchange of shares. 8.3.2 Conclusion The concept is compliant with the Merger Directive and Primary EC law. For infringements of EC law by anti-abuse provisions see under no. 11.4 below.	RTA Sec. 15(2) RTA Sec. 21(2) no. 2 RTA Sec. 22(1), (2) RTA Article 8(1) RTA

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
9.1 Avoidance of economic double taxation at the level of the transferring company 9.1.1 Concept 9.1.1.1 Transfer of assets The value assessed on the receiving company for the transferred business assets and liabilities and of the shares issued shall be deemed to be the sales price of the assets by the transferring company. In the event that the German taxing right for the gain on the disposal of the transferred business assets and liabilities is excluded at the transfer date and that a taxing right is also not created by the transfer, the deemed acquisition cost of the shares with regard to the transferring company shall be equal to the fair market value of the business assets and liabilities at the date of transfer. 9.1.1.2 Exchange of assets The value at which the receiving company values the transferred shares shall be deemed the purchase price of the transferred shares and the acquisition cost of the received shares for the transferring company. 9.1.2 Conclusion As a result, in principle economic double taxation would not be avoided.	Sec. 20(3) 1st and 2nd sentences RTA Sec. 21(2) RTA

However, based on Sec. 8b(2) CITA for corporate shareholders capital gains from the disposal of shares are tax exempt (but 5 per cent of the capital gains will be treated as non deductible expenses. For anti-abuse provisions see under no. 9.2). Therefore, the economic double taxation is mitigated.	

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>9.2 Further conditions for tax relief</u> <u>9.2.1 Concept</u> In so far as in the case of a contribution in kind (transfer of assets) below the fair market value the transferor disposes of the received shares within a period of seven years from the transfer date, the gain resulting from the contribution is to be taxed retroactively in the fiscal year of the contribution as a profit of the transferring company. This gain shall be the amount by which the fair market value of the transferred business assets and liabilities, net of the cost of the transfer of assets and liabilities, at the transfer date exceeds the value assessed by the receiving company for the transferred business assets and liabilities, reduced by one-seventh for each time year expired since the transfer date. Any contribution gain shall be treated as deemed subsequent acquisition costs of the received shares. <u>9.2.2 Conclusion</u> For the incompliance of this provision with EC law see the comments under no. 11.4.1.2 below.	Sec. 22(1) RTA Article 11 Merger Directive

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>9.3 Tax deferral</u> <u>9.3.1 Concept</u> With respect to the contribution of a '*Teilbetrieb*' we refer to no. 2.6, the concepts of 'real values' to no. 4.1, 'effectively connected with the permanent establishment' to no. 4.3, the immediate taxation without tax deferral to no. 4.7 and the issuance of new shares to no. 2.2.2.2 The comments apply *mutatis mutandis*. <u>9.3.2 Conclusion</u> See above.	Sec. 20 RTA

Article 10 – Permanent establishment in a third Member State

<table>
<tr><th>Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.</th><th>Reference</th></tr>
<tr><td><u>10.1 Loss recapture for permanent establishments in third Member States</u>

<u>10.1.1 Concept</u>

<u>10.1.1.1 Tax credit method</u>

As far as the income from a permanent establishment in another Member State is not tax exempt under the applicable DTC and losses qualify for tax deduction under Sec. 2a(1), (2) ITA they are deductible at the level of the resident company. German tax law does not provide for a loss recapture rule in case of a reorganization of the permanent establishment.

<u>10.1.1.2 Tax exemption method</u>

Losses of tax exempt foreign permanent establishments may not be off-set against income of German resident companies and shall thereby not reduce the basis of assessment. As an exception to the rule, until 31 December 1998 losses of so-called active foreign permanent establishments could be temporarily off-set in Germany, subject to application by the taxpayer, until the foreign establishment generated a profit in a subsequent year. This provision was repealed with effect from 1 January 1999. Initially a transitional provision applied until the year 2008. Based on the Tax Amendment Act 2008 the respective profits will now remain taxable without a time limit.

The rule also applies if the permanent establishment will be transformed into a company, or transferred to a company or liquidated, or in case the company transfers its place of management or registered seat to another State resulting to a termination of the unlimited tax liability in Germany according to Sec. 1 CITA.

<u>10.1.2 Conclusion</u>

In our view these rules are compliant with Article 4 and Article 10(1) of the Merger Directive.</td><td>Sec. 52(3) ITA

Sec. 2a ITA

Sec. 1 CITA

Article 4 Merger Directive</td></tr>
</table>

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> <u>10.2.1 Concept</u> Same tax treatment as under 10.1. <u>10.2.2 Conclusion</u> See above.	Sec. 2a ITA

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> <u>10.3.1 Concept</u> Germany follows the concept of worldwide taxation. In the case of a merger of a company subject to unlimited tax liability in Germany, the corporate income tax levied on the transfer gain is to be reduced by the amount of foreign tax which would have been charged pursuant to the legislation of another Member State if the transferred assets had been disposed of at fair market value. This shall apply only in so far as the transferred assets are to be attributed to a permanent establishment of the transferring company in another Member State and Germany does not avoid double taxation with the transferring company by way of exemption. This rule applies *mutatis mutandis* to a division, a partial division and a transfer of assets (branch of activity). <u>10.3.2 Conclusion</u> The implementation is compliant with Article 10 (2) of the Merger Directive (for the doubtful compliance with Primary EC law see under 10.4.1).	Sec. 3(3) RTA Sec. 11(3) RTA Sec. 15(1) RTA Sec. 20(7) RTA Article 43 and 48 EC

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
10.4 Tax deferral 10.4.1 Concept The German legislator took the position that the principles outlined by the ECJ in the case C-470 *'N'* only apply to individuals and have no impact in the interpretation of the Merger Directive. Even if a notional tax credit is provided for in the RTA, our concerns with respect to the immediate taxation are the same as outlined under no. 4.7 above. 10.4.2 Conclusion It is doubtful if Sec. 20(7) RTA is compliant with Article 43 and 48 EC.	Sec. 3(3) RTA Sec. 11(3) RTA Sec. 15(1) RTA Sec. 20(7) RTA Article 43 and 48 EC

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies As outlined above (see no. 3.2) Germany applies the RTA to those companies which are regarded according to the '*Typenvergleich*' as non-transparent. Article 10a was implemented insofar only as it was absolutely necessary. Regardless of the Merger Directive foreign companies deemed fiscally tax transparent are treated as partnerships for German tax purposes. Reorganizations follow the rules applicable for partnerships. Article 24 RTA applies for the transfer of branches of activities or of an interest in a partnership to a partnership. The provision applies irrespective of the fact whether the receiving entity is governed by German or foreign company law.	Sec. 1 RTA Sec. 20(8) RTA Sec. 24 RTA

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit 10a.2.1 Concept Profit is the difference between fair market value and book value of the assets to be attributed to a permanent establishment located in another Member State. For the allocation of assets to a permanent establishment	Sec. 20(8) RTA

see no. 2.6, and for the definition of fair market value see no. 4.1. <u>10a.2.2 Conclusion</u> The concept is compliant with EC law.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an <u>acquired</u> company?	Reference
<u>10a.3 Determination of notional tax credit</u> <u>10a.3.1 Concept</u> In the event that a non-resident transferring or acquired company within the meaning of Article 3 of the Merger Directive is to be considered fiscally transparent, the foreign tax which would have been levied pursuant to the legislation of the other Member State if the transferred assets to be attributed to a permanent establishment located in another Member State had been disposed of at fair market value is, by virtue of Article 10a of the Merger Directive, to be credited against the corporate income tax or individual income tax allocated to the transfer profit by appropriately applying Sec. 26 (6) CITA as well as Sec. 43c and Sec. 50 (6) ITA. This means in essence that Germany would grant a tax credit on a per-country limitation basis. Following German tax principles an excess tax credit cannot be carried forward and would be lost. Consequently, if the resident shareholder of the deemed transparent company would offset the profits generated with current losses or available tax loss carry forwards the notional tax credit could not be used. But this would also be the case if the foreign tax had effectively been charged. Therefore, the rule is in our view in principle in line with the requirements of Article 10a(2) of the Merger Directive. As far as the transferred assets are valued above their book values Sec. 26 (6) CITA as well as Sec. 43c and Sec. 50 (6) ITA apply directly. It is discussed whether or not the German foreign tax credit system is in line with EC law. Commentators take the position that under EC law at least a per-community limitation is required and that a carry forward of foreign tax credits must be credited. We share this view. For example, in case the German company is even under consideration of the foreign taxable income in a loss position a notional tax credit would not be tax effective. But if the assets are transferred under foreign law at book value, a future economic double taxation of the same hidden reserves cannot be excluded. <u>10a.3.2 Conclusion</u> The concept is doubtfully compliant with EC law.	Sec. 20(8) RTA Sec. 26(6) CITA Sec. 43c ITA Sec. 50(6) ITA

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
<u>10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders</u> <u>10a.4.1 Concept</u> With respect to Article 10a (3) of the Merger Directive, Germany treats this transaction as a contribution to a non-resident foreign partnership governed by Sec. 24 RTA. This means that Germany exercised the right not to apply Article 8(1), (2) and (3) of the Merger Directive. In case of 10a (4) of the Merger Directive the fact that the receiving (deemed transparent) company would be deemed to be located in Germany has no effect on the tax treatment of the direct or indirect shareholders of this company. From a German tax perspective, this provision of the Merger Directive does not impact the German tax position of the shareholders since a tax transparent company is treated as a permanent establishment of its shareholders. The fact that a tax transparent entity would be treated as a resident company in Germany itself has no impact on the fact that the assets would be allocated to the permanent establishment where they belong to, which in the case of a non-German business would be outside of Germany. <u>10a.4.2 Conclusion</u> The concept is compliant with EC law.	Sec. 24(2) RTA

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
<u>10a.5 Comparison with a resident fiscally transparent company</u> Irrespective of the fact that the fiscally transparent company is resident or non-resident in Germany the same tax principle will apply for direct and indirect 'shareholders'. In both cases the decisive question is whether or not the received assets can be contributed to a permanent establishment of the 'shareholder' in Germany. In case of a transfer of a branch of activity from such 'shareholder' to a resident fiscally transparent company, the value at which the transferred business assets and liabilities are reported in the balance sheet of the partnership, including supplementary statements for its partners, would be deemed to be the purchase price for the transferor. The partnership must report the transferred assets and liabilities at fair market value. In derogation from this rule the received business assets and liabilities may on request be reported at book value or a higher value, although this	Sec. 24(2), (3) RTA

cannot exceed the fair market value, in so far as the German right to tax the transferred business assets and liabilities is neither excluded nor limited.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation 10b.1.1 Concept 10b.1.1.1 Level of the transferring company The transfer of a registered office of a SE would give rise to exit taxation as follows. In the event that the German taxing right for gains on the disposal or use of an asset is excluded or limited, this shall be deemed a disposal or transfer for use of that asset at fair market value. Because this rule is based on the assumption that the transfer of the registered office to another Member State does not lead to liquidation from a legal point of view, i.e. the legal entity remains in existence, it is from a German legal point of view currently only applicable to the SE and SCE. For proposed changes of the German company law for other companies see no. 3.3.3. 10b.1.1.2 Level of the shareholders The limitation or exclusion of the German taxing right for the gain on the disposal of the shares in a company in case of the transfer of the registered office or place of management of the company to another state will be treated as a disposal of the shares at fair market value. However, this will not apply in the case of a transfer of the registered office of a SE and a SCE to another Member State. Regardless of the provisions of any DTC, the gain on a subsequent disposal of the shares must in these cases be taxed in the same way as how these shares would have been taxed if no transfer of the registered office had occurred. 10b.1.2 Conclusion The exit taxation concept applies for the SE/SCE. For other German companies the transfer of the registered office to another Member State would currently result in a liquidation of that entity.	Sec. 12(1) CITA Sec. 17(5) ITA Sec. 15(1a) ITA Sec. 4(1) 4th Sentence ITA

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' There is no definition given for the term 'head office' ('*Hauptverwaltung*') in the national legislation or in administrative guidelines.	Sec. 2 SEImpl Act

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency 10b.3.1 Concept 10b.3.1.1 Tax residency under German tax law A company is taxable on its worldwide income if it has its place of management ('*Ort der Geschäftsleitung*') and/or its registered office ('*Sitz*') in Germany. Place of management refers to the central point of the top management of the corporation. This is the place where the management decisions are made which are necessary to conduct the business. Registered office is the place determined by the by-laws of the company. With respect to the SE it must be noted that its registered office must be located in the Member State in which the place of its head office ('*Hauptverwaltung*') is to be found. In practice the term 'head office' has the same meaning and content as the term 'place of management'. In case of the SE both the registered office and the head office must be in one and the same Member State (i.e. in Germany), so that also the place of management is in Germany. Both the existence of the SE's registered office and head office in Germany are the basis for its unlimited tax liability of the SE in Germany. The registered office of the SE can be transferred to another Member State without liquidation of the SE in the Member State from where its registered office is moved and also without creation of a new juridical person in the Member State to which the move happens. The transfer of the registered office also requires the move of the head office of the SE (and thus also of its place of management) so that its unlimited tax liability in the Member State which it leaves (i.e. Germany) is terminated. The clear objective of the SE-Regulation is to avoid a dual residency of a SE for tax purposes.	Sec. 2 SEImpl Act Sec. 5(2) SCA Sec. 1(1) CITA Sec. 10 GTC Sec. 11 GTC Article 4(3) of the DTCs with the other Member States Article 4 no. 24 of the OECD-Commentary

10b.3.1.2 Tax residence under German DTCs German DTCs at least with the other Member States follow Article 4 (3) OECD Model Convention stating that a legal person which is resident in both Contracting States shall be deemed to be a resident only of the State in which its place of effective management is situated. The place of effective management is the place where key management and commercial decisions are made which are required and are necessary for the conduct of the entity's business. Since, as discussed under 10b.3.1.1 above, the head office of a SE cannot remain in Germany if its registered office is transferred from Germany to another Member State, the taxing rights would be lost for Germany, if the registered seat of the SE is moved outside of Germany. The theoretical case that the head office is transferred to the other Member State, but the place of effective management remains in Germany, will be rather unlikely in practice. Thus, the transfer of the registered office of the SE from Germany to another Member State would also under the terms of the applicable DTC mean that Germany would lose its right for unlimited taxation. 10b.3.2 Conclusion Generally, the concept of 'head office' coincides with the criteria used to determine tax residence. However, there are potentially cases where, in theory, this is not the case.	

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
10b.4 Assets and liabilities not effectively connected with a permanent establishment 10b.4.1 Concept If the registered office of a SE is transfered any assets of the SE which are not connected to a permanent establishment which the SE retains in the Member State which it leaves (i.e. Germany), and which do not otherwise remain suject to German taxation (e.g. real estate located in Germany) shall be deemed as disposed of or transfered for used at fair market value. Any capital gain would be subject to taxation. 10b.4.2 Conclusion For the doubtful compliance of this rule with EC law see 4.5 and 10b.5.	

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
10b.5 Tax deferral 10b.5.1 Concept The German legislator took the position that the principles outlined by the ECJ in the case C-470 '*N*' only apply to individuals and have no impact in the interpretation of the Merger Directive. 10b.5.2 Conclusion In our view the exit tax without tax deferral is doubtfully compliant with Article 43 and 48 EC.	Sec. 12 (1) CITA Article 43 and 48 EC

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 The term 'comparable circumstances' The change of the tax status from unlimited tax liability to limited tax liability has no impact on the availability of German tax loss carry forwards of the SE/SCE, as well as for other German taxable persons.	Sec. 8c CITA

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Loss recapture for permanent establishments 10c.2.1 Concept Same tax treatment as under 10.1. 10c.2.2 Conclusion See above.	

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
10d.1 Deemed liquidation 10d.1.1 Concept The SE and SCE can transfer their statutory seat (and their head office, i.e. their place of effective management) within the EU (see Article 8 SE-Regulation and Article 7 SCE-Regulation). If only the statutory seat of a SE is transferred whilst the actual seat is maintained, the German commercial register has the right to file a procedure to opening the liquidation process which may finally lead to a deemed distribution (Sec. 52 SEImpl. Act) subject to taxation following general tax rules. 10d.1.2 Conclusion Sec. 52 SEImpl. Act is compliant with the SE-Regulation.	Sec. 12(1) RTA Article 64 SE-Regulation Sec. 52 SEImpl. Act

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
10d.2 Tax treatment of third country residents If a non-resident holds shares in a SE/SCE which is tax resident in Germany, and the SE/SCE transfers its registered seat to another Member State the following would apply. 10d.2.1 Concept 10d.2.1.1. Shares held in a permanent establishment in Germany Provided that the shares are held in a permanent establishment in Germany, a future disposal of the shares would be subject to taxation in Germany in the same way as prior to the transfer of the registered seat to another Member State. A limitation of the German taxation right (based on the application of a DTC) caused by the transfer of the registered seat to another Member State would be disregarded. 10d.2.1.2. Shares not held in a permanent establishment in Germany If the non-resident shareholder can claim protection under a DTC of his country of residence with Germany the taxation right for any capital gain realized upon the sale of the shares is granted to the state of his residence	Sec. 4(1) 4th sentence ITA Sec. 15(1a) ITA Sec. 17(5) ITA Sec. 49(1) no. 2 lit. e, bb ITA Article 10d Merger Directive

and not to Germany. In some rare cases this is different if the corporation qualifies as a real estate holding company. This result also applies if the corporation, i.e. the SE has moved its registered seat outside of Germany. In the absence of DTC protection the disposal of shares by non-residents in a corporation with its place of management or registered office in Germany is only subject to taxation in Germany in case of a substantial shareholding (at least 1 per cent or more of the registered capital at any time within a five-year period prior to the sale). A future disposal of the shares would be subject to taxation in Germany in the same way as prior to the transfer of the registered seat to another Member State. The taxation right would not be limited to the hidden reserves which were generated prior to the transfer of the registered office of the SE/SCE. No tax credit for foreign taxes paid on the disposal of the shares would be available. It is our understanding that Article 10d of the Merger Directive must be read in such a way that any capital gain which results from an increase in value after the transfer of the registered office to another Member State can only be taxed if this would also be allowed for shares in a company which did not move its registered office but did qualify as foreign resident company from its inception. <u>10d.2.2 Conclusion</u> In our view the taxation of hidden reserves generated after the transfer of the registered office is in the aforementioned scope incompliant with Article 10d of the Merger Directive.	

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 *'Leur-Bloem'* and C321/05 *'Kofoed'*. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 *'Cadbury'*. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> The RTA contains no general provision for the prevention of tax abuse. Special provisions to avoid tax abuse are stated in Sec. 15 (2) and Sec. 22 (1), (2) RTA (see under no. 11.4 below).	

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
11.2 General anti-abuse provision The tax administration would apply Sec. 42 GTC stating that the tax law cannot be circumvented by the abuse of rights. An abuse of rights is given, if the taxpayer chooses an inadequate legal structuring, resulting in a tax benefit which would not have occured in case of an adequate structuring.	Sec. 42 GTC

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' 11.3.1 Transformation in domestic law Sec. 42 AO has been amended as from January 1, 2008. If the taxable person can demonstrate that the structuring has been chosen for non-tax reasons taking into consideration the concrete facts and circumstances this will not be treated as tax abuse. According to the explanatory memorandum of the Tax Amendment Act 2008 the question of having an abusive structuring must be in case of an EU structure interpreted in the light of the concept of wholly artificial arrangements. The '*Cadbury Schweppes'* judgment also resulted in changes of the German CFC-rules. 11.3.2 Conclusion The concept of 'wholly artificial arrangements' has only insofar been implemented into national law as it forms a principle for interpretation. This is not compliant with the requirement stated in the '*Biehl II'* decision of the ECJ. According to '*Biehl II*', C 151/94, ref. 18, the incompatibility of provisions of national law with provisions of the Treaty, even those which are directly applicable, can be definitively eliminated only by means of binding domestic provisions having the same legal force as those which require to be amended.	Sec. 42(2) GTC

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationality or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
<u>11.4 Specific anti-abuse provisions</u> <u>11.4.1 Concepts</u> <u>11.4.1.1. Division/partial division</u> The transfer of assets at book value or any higher value below the fair market value is in case of a division or partial division not to be applied if the division creates the preconditions for disposal. This is to be assumed if shares in a company involved in the division accounting for more than 20 per cent of the shares in the company existing before the coming into effect of the division are disposed within 5 years from the effective transfer date for tax purposes. In the case of separate shareholder groups, the transfer of assets below fair market value shall also require that the holdings in the transferring company have existed for at least 5 years before the effective transfer date for tax purposes. According to the '*Leur-Bloom*' judgment of the ECJ a general rule automatically excluding certain categories of operations from a tax advantage would go further than required for preventing such tax evasion or such tax avoidance and would undermine the aim pursued by the Merger Directive. For this provision the two-year time limit according to Article 3(2) of the Parent-Subsidiary Directive has been exceeded. In addition, the provision does not allow the taxpayer to give evidence that in the specific situation a misuse is not given. Therefore, in our view Sec. 15(1) and (2) RTA are incompliant with the Merger Directive. Based on the intention of the legislator to set up uniform tax principles for all reorganizations covered by the RTA the aforementioned rules should be applicable for reorganizations under the Merger Directive as well as for domestic reorganizations. <u>11.4.1.1.1 Conclusion</u> Therefore, the compliance of the aforementioned rules with the Merger Directive is in case of domestic reorganizations at least doubtful. <u>11.4.1.2. Transfer of assets/exchange of shares</u> In so far as in the case of a contribution in kind below fair market value the transferor disposes of the received shares within a period of seven years from the transfer date, the gain resulting from the contribution is to be taxed retroactively in the fiscal year of the contribution as profit of the	Sec. 15(1),(2) RTA Sec. 22(1),(2) RTA Article 11 Merger Directive Article 43 and 48 EC (Ministry of Finance Circular of September 7, 2007) (C-28/95 '*Leur-Bloem*' [1997] ECR I-4161) (Explanatory memorandum SETI Act from 11.8.2006, BR-Drs. 542/06, S. 32)

transferor. Contribution gain shall be the amount by which the fair market value of the transferred business assets and liabilities, net of cost of the transfer of assets and liabilities, at the transfer date exceeds the value assessed by the receiving company for the transferred business assets and liabilities, reduced by one-seventh for each time year expired since the transfer date. In the seven years following the transfer date, the transferor must at the latest by May 31st annually give evidence to whom the received shares and the shares based on these shares are to be attributed upon expiration of the day corresponding to the relevant transfer date. Otherwise the shares shall be deemed to have been disposed. In so far as shares transferred below the fair market value within the context of a contribution in kind or an exchange of shares are disposed of by the receiving company within a period of seven years from the transfer date and the transferor is no person privileged by Sec. 8b(2) CITA, the gain resulting from the contribution is retroactively to be taxed in the fiscal year of the transaction as gain of the transfer or on the disposal of shares. Contribution gain shall be the amount by which the fair market value of the transferred business assets and liabilities, net of cost of the transfer of assets and liabilities, at the transfer date exceeds the value assessed by the receiving company for the transferred business assets and liabilities, reduced by one-seventh for each time year expired since the transfer date. In the seven years following the transfer date, the transferor must at the latest by May 31st annually give evidence to whom the transferred shares and the shares based on these shares are to be attributed upon expiration of the day corresponding to the relevant transfer date. Otherwise the shares shall be deemed to have been disposed. According to the '*Leur-Bloom*' ruling of the ECJ a general rule automatically excluding certain categories of operations from a tax advantage would go further than required for preventing such tax evasion or such tax avoidance and would undermine the aim pursued by the Merger Directive. For both provisions the two-year time limit according to Article 3(2) of the Parent-Subsidiary Directive has been exceeded. In addition, the provision does not allow the taxpayer to give evidence that in the specific situation an abuse is not given. 11.4.1.2.1 Conclusion Therefore, in our view Sec. 22(1) and (2) RTA are incompliant with the Merger Directive.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
<u>11.5 The concept of 'valid commercial reasons'</u> <u>11.5.1 General transformation</u> The concept of valid commercial reasons can be found in the new Sec. 42(2) 2nd sentence GTC as well as in Sec. 50d(3) ITA. According to Sec. 42(2) 2nd sentence GTC no tax misuse is given if the taxable person can demonstrate that the structuring was chosen for non-tax reasons taking into consideration the concrete facts and circumstances. As the explanatory memorandum of the Tax Amendment Act 2008 implementing this rule refers for EU structures to the concept of wholly artificial arrangements there is a clear reference to the European Community principles as articulated by the ECJ in a number of cases. The special anti-abuse provision in Sec. 50d(3) ITA is in our view incompliant with the concept of valid commercial reasons as highlighted by the ECJ in the case '*Cadbury Schweppes*' as it requires inter alia excessive valid business or commercial reasons. <u>11.5.2 Specific provisions</u> <u>11.5.2.1 Concept</u> The concept of valid commercial reasons is not considered in the RTA. The German anti-abuse legislation in the RTA is characterized by the above mentioned time limited retroactive taxation (see above under 11.4.1.2). To prevent fraudulent use this concept is extended by additional scenarios (see Sec. 22(1) 6th sentence RTA). This can be illustrated for reorganizations following tax privileged reorganization as follows. <u>11.5.2.2 Example</u> Company A tax resident in Member State A maintains a permanent establishment/branch of activities in Germany. The branch will be contributed to company B tax resident in Member State B at book value in exchange for shares (Sec. 20 RTA). Company A contributes the shares in company B to company C which is tax resident in the Member State C analogous to Sec. 21 RTA within a 7 year period following the contribution. According to the German RTA (Sec. 22(1) 6th sentence no. 2 RTA) the contribution of the branch to company B will not be taxed if company A values the shares in company C at the same value as the shares in company B, i.e. at book value. Company C is allowed to value the shares in company B at a value exceeding the book value. In the above example German commentators consider whether a taxable event in Germany is given, dependent on the valuation of a not directly connected transaction in another Member State (in the above case the	Sec. 42 GTC Sec. 50d (3) ITA Sec. 22(1) 6th sentence no. 2, 4 and 5 RTA Article 8(1) Merger Directive Article 11 Merger Directive (C-196/04 *'Cadbury Schweppes'* [2006] ECR I-0000)

valuation of the shares in C at the level of A in Member State A) as a violation of EC law. We share this view under the aspect of the required holding period of seven years and the concept of valid commercial reasons. If the transfer of the shares in company B follows valid commercial reasons it is not acceptable that the shares in company C must be valued for tax purposes at the level of company A in the (foreign) country A with the book value of the shares in company B. 11.5.2.3 Conclusion In our view this rule is incompliant with Article 8(1) and Article 11 Merger Directive.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof The initial burden of proof is with the taxpayer, which is in our view principally in line with EC law (see '*Cadbury Schweppes*', para. 70).	Sec. 22 RTA / Sec. 42 GTC (C-196/04 '*Cadbury Schweppes*' [2006] ECR I-0000)

GREECE

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
<u>**Overall state of implementation**</u> The 90/434 Directive has been implemented into the Greek legislation by virtue of Law 2578/1998, which was issued on 17-2-1998 (Volume A΄ 30/17-2-1998 of Government's Gazette). Law 2578/1998 did not have retroactive effect and it did not cover the years during which Greece was in breach of the European legislation. By virtue of such law, the content of the above Directive was transposed literally into Greek legislation, i.e. the wording used in the Greek law is almost identical to the one found in the Directive. In addition, on 21 December 2006 the Greek parliament passed Law 3517/2006 (Volume A΄ 271/21-12-2006 of Government Gazette), which transposed into Greek law Directive 2005/19 that amended the 1990 Directive and introduced a number of amendments to Law 2578/1998. However, given that the Greek corporate law (Law 2190/1920) does not provide for any regulatory framework for cross-border mergers, divisions, and partial divisions, transfers of assets and exchanges of shares, the practical implementation of the Merger Directive remains pending. In particular, the current corporate legal framework regulates such transactions effected only between Greek corporations. As a result, the tax provisions of Law 2578/1998 remain in practice inactive and are currently of theoretical interest only. Nevertheless, Greek case law has acknowledged in isolated cases (Ruling 58/2002 of Legal State Council) that Law 2578/1998 has introduced the legal framework permitting cross-border mergers. Furthermore, it is also interesting to note that the Greek administration and Greek tax authorities have not dealt with Directives 90/434 and 2005/19 and have not issued any relevant administrative guidelines/ rulings in connection thereto.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>**1.1 Involved companies**</u> Law 2578/1998 and Law 3517/2006 define the term 'company' as an entity listed in the Annex of the Directive and, as a result, relief given under Greek law in connection to mergers, divisions, partial divisions and share for share exchanges is restricted to those types of entities. Please note that from a Greek tax law perspective only Greek 'societe anonyms' companies (AE) and limited liability stock companies ('ΕΠΕ') are entitled	Article 1 and Annex A1(d) of Law 2578/1998

to take advantage of the procedures introduced by Merger Directive 1990/434 and Directive 2005/19. Parent companies are not included in the term ''companies involved''.	

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
1.2 Foreign Member State and third state merger Currently, it does not seem possible under Greek law to apply the benefits of the Merger Directive if the Merging companies were from a single (foreign) Member State or from a third (non-EU) State or States.	N/A.

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term 'securities' Tax law adopts the definitions introduced by domestic corporate law. Securities are defined as 'shares in the share capital of a stock company'. The term 'stock company' for the purposes of the Directive includes two types of stock company: (a) the societe anonyme (AE) and (b) the limited liability stock company (ΕΠΕ). As long as the type of non-resident company is included in the relevant Appendix of the Directive, it would be included in the scope of the Directive from a Greek perspective.	Article 2 of Law 2578/1998

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' Such possibility has been implemented, but there are no administrative guidelines. Based on the wording of Law 2578/1998, it can be argued that it applies on a per shareholder basis.	Article 2 (c) of Law 2578/1998

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger No.	N/A.

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares There are no administrative guidelines with the subject matter. By reference to the wording of the transposing legislation, the relief is granted in respect of the exchange that leads to the acquisition of a majority holding or when holding such a majority to the acquisition of a further holding.	Article 2 (στ) of Law 2578/1998

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
2.5 Consolidation of qualifying holding No further requirements should be met, provided that the transactions are carried out for valid commercial reasons and not for tax evasion or tax avoidance.	Articles 2 (στ) and 8 of Law 2578/1998

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
2.6 The term 'branch of activity' No administrative guidelines have been introduced. However, as per the definition adopted by the Greek administration (Circular 1103/1990 of the Greek Ministry of Finance), the term 'branch of activity' (or business sector) includes the total of tangibles and intangibles, such as movables and real estate, receivables, liabilities, clientele, goodwill, trademarks, etc, organized as an independent unit. In contrast with the transfer of assets on an itemized basis, the transfer of business sector is considered as the transfer of an economic entity which retains its identity and is taken as the total of organized resources for the exercise of economic activity (principal or secondary). Indicatively, under current Greek incentives' laws it is required that the business sector be constituted by a totality of assets and liabilities, qualifying and operating as an independent economic unit and having accounting autonomy (i.e. being monitored in separate accounts).	N/A.

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
3.1 Types of entities No.	N/A.

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
3.2 Transparent entities Greek tax law does not make any reference to tax transparent entities, since no tax transparent entities exist under Greek law. However, Law 2578/1998 as amended provides that a foreign company is considered as tax transparent if its profits are taxed in the hands of its shareholders or partners, according to the foreign legislation.	Article 3 para. 7 of Law 2578/1998

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
<u>3.3 Qualification of tax residency</u> Greek tax law basically adopts the legal seat criterion of a legal person in order to assess its tax residence. Having said this, according to Greek civil law, a company shall be deemed to have its real seat in Greece if Greece is the place of its effective management. Based on standard case-law of the Greek courts, the latter is a matter of fact; the place of incorporation stated in the Articles of Association is no more than an indication of the seat of the company. Evidence that a prima facie foreign company is effectively managed in Greece would attribute Greek-company and Greek tax residency status to the foreign company at hand. DTCs concluded by Greece adopt in general the tax residence tiebreaker criterion stipulated in Article 4 of the OECD Model Tax Treaty and abide by the respective remarks included in the OECD commentary.	Article 2 and 101 of Greek Income Tax Code (law 2238/1994) and Article 10 of Greek Civil Code.

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>3.4 Subject-to-tax clause</u> The 'subject-to-tax' clause has been transposed literally in Greek legislation and no further guidelines exist.	Article 1 para. 2(b) and Annex B of Law 2578/1998

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>3.5 Shareholder requirements</u> No such restriction has been introduced under Greek law.	N/A.

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>4.1 The concepts of 'real values' and 'value for tax purposes'</u> The concept of 'real value' corresponds to the fair market value of the assets and liabilities, while the concept of 'value for tax purposes' corresponds to the net book value.	Article 3 para. 1 of Law 2578/1998

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
<u>4.2 Specific guidance for divisions/partial divisions</u> No specific guidance has been issued (please see 4.1).	N/A.

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>4.3 The concepts of 'effectively connected' and 'permanent establishment'</u> There is no specific implementation or interpretative administrative guidelines in this respect. Based on the wording adopted by Law 2578/1998, the term 'effectively connected' should be regarded as meaning that such assets are used in a trade carried on by the permanent establishment at stake in order to generate profits. The term 'permanent establishment' is defined in Greek Income Tax Law and the definition adopted is quite similar to the one found in Article 5 of the OECD Model Tax Treaty. The definition in Greek tax law provides that: A foreign legal entity is deemed to have a permanent establishment in Greece when: (a) it maintains in Greece one or more shops, agencies, branches, offices, factories, warehouses or workshops, as well as installations for the handling or processing of natural resources; (b) it is involved in the industrial processing of raw materials or agricultural products using their own facilities or facilities of a third party in Greece who acts under their orders and on their behalf;	Article 100 para. 1 of Greek Income Tax Code (Law 2238/1994)

(c) it conducts operations or provides services in Greece through an agent authorized and empowered to negotiate and conclude contracts on behalf of the legal person, as well as when such operations are conducted or services are rendered without the agent provided that they involve the composition of a study or plan or generally involve the conduct of research programs or other activities of a technical or scientific nature; (d) it maintains a stock of merchandise for the purpose of fulfilling orders on their behalf; and/or (e) it participates in a partnership or a private limited liability company whose seat is registered in Greece There are not any special techniques for the allocation of an asset to a permanent establishment. An asset would be considered as effectively connected to a permanent establishment if it is (or should have been) recorded in the accounting books of the PE.	

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief No such specific limitation of relief is provided, as long as that the transactions are carried out for economically fair commercial reasons and not for tax evasion or tax avoidance.	Article 8 of Law 2578/1998

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment The transfer of assets and liabilities would not be subject to the rules introduced by Law 2578/1998 and Law 3517/2006 implementing Directives 1990/434 and 2005/19. Assets and liabilities are allocated to a permanent establishment, as long as they are depicted by means of relevant entries in its accounting books. As a result, assets and liabilities not effectively connected with a permanent establishment would be subject to the local capital gains taxation (i.e. 25% tax), unless relief could be invoked under a relevant double taxation treaty.	Article 1 para. 3 of Law 2578/1998

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company Even though no practical experience of the Merger Directive exists in Greece, the merger should be tax exempt in this case as well.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral N/A. No account of the ECJ case law has been taken.	

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities Greek tax law does not make any reference to tax transparent entities, since no tax transparent entities exist under Greek law. However, Law 2578/1998 as amended provides that a foreign company is considered as tax transparent if its profits are taxed in the hands of its shareholders or partners, according to the foreign legislation (please see 3.2).	Article 3 para. 7 of Law 2578/1998 and Article 2 para. 7 of Law 3517/2006

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief The Greek law expands the tax relief – apart from capital gains and income tax – also to real estate transfer tax. Specifically, under tax incentive L.1297/1972 the transfer by the absorbed company of its real estate to the absorbing company is exempt from real estate transfer tax on the condition that the property will be used for the needs of the absorbing company for a period of at least 5 years starting from the date of the merger's completion. Please note that during said 5 year period and provided that the principal activity of the absorbing company does not alter, the absorbing company is allowed: (a) to lease the real estate property contributed or (b) to sell such property provided that the proceeds from the sale shall be used within the next 2 years from such sale for the acquisition	Article 5 of Law 2578/1998

of real estate or other new fixed assets intended for the operational needs of the company or for the settlement of debts existing at the time of sale from bank loans and credits or from tax liabilities towards the State and social security contributions.	

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>5.1 The term 'provisions and reserves'</u> There is no specific definition of the term 'provisions and reserves' in the said laws transporting both Directives. Therefore, for the purpose of specifying such term within the framework of the Directive's implementation, it may be argued that one could find recourse to Greek tax incentive laws providing for Greek tax provisions and reserves. The term 'reserve' is generally found in Greek investment incentives' legislation as is currently in force and stands for the amount of cash grant recorded in a special account (special reserve account) of a company, which cannot be distributed prior of the lapse of a certain period of time from the completion of the investment and the commencement of operation. The penalty in case of distribution during this period is reclaiming of the subsidy (plus interest). If the reserve is capitalized or distributed within the above period of time, it is subject to corporate tax. The term 'provision' is defined in Article 42e para. 14 of law 2190/1902, according to which 'provisions for liabilities and charges' are intended to cover losses or debts the nature of which is clearly defined and which at the date of the balance sheet are likely to be incurred, but uncertain as to amount or as to the date on which they will arise.	Article 3 para. 4 of Law 2578/1998

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
<u>5.2 Exclusion of 'provisions and reserves' from permanent establishments</u> There is no specific rule excluding the provisions and reserves deriving from permanent establishments abroad since such provisions and reserves may not be utilized under the Greek tax law by Greek head offices.	N/A.

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
<u>5.3 Allocation method for provisions and reserves</u> No specific method of allocation exists.	N/A.

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
<u>5.4 Further conditions for carry-over of provisions and reserves</u> For the carry-over of provisions and reserves it is necessary that the provisions and reserves are transferred and recorded in special accounts of the receiving entity.	Article 3 para. 4 of Law 2578/1998

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
<u>6.1 The concept of carry-over of losses</u> The term 'loss' has not been specifically defined or interpreted for the purposes of applying the Directive; hence, the general rules of Greek tax law would be applicable. A loss is deemed to arise when the expenses or debits arising in respect of one of those types of income earned exceeds the related income or credits. The choices available to a company with respect to losses of a particular kind arising in a period are as follows: (a) use to offset against other types of income arising in the period; this applies to losses derived from all kinds of income; (b) carry forward for offset against future income arising within the following 5 years; this applies to losses derived from all kinds of income with the exception of income derived from real estate Please note that losses attributed to a permanent establishment located abroad can be offset against income derived abroad and not against income arising in Greece. Moreover, under Greek tax law there is no 'group relief' against profits arising in other group entities.	Article 4 para. 3 and 4 of Greek Income Tax Code (Law 2238/1994)

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment No special rules exist for the allocation of losses to permanent establishment. Losses are allocated to a permanent establishment, as long as they are depicted by means of relevant entries in its accounting books.	N/A.

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets No. The above rules are equally applicable.	N/A.

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses The carry over of losses is applicable to the extent that the domestic law grants such possibility to mergers of Greek companies effected under the provisions of Articles 1 - 5 of Greek Law 2166/1993 or Article 16 para. 5 of Law 2515/1997. It should be mentioned that currently, carry-over of losses is not possible for mergers of Greek companies effected in accordance with Law 2166/1993 or Article 16 para. 5 of Law 2515/1997.	Article 3 para. 5 of Law 2578/1998 Article 1 – 5 of Law 2166/1993 Article 16 para. 5 of Law 2515/1997 Law 2166/1993

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Amended holding threshold The holding threshold of 15% has been implemented in Greek law by virtue of Article 4 para. 6 of Law 2578/1998.	Article 4 para. 6 of Law 2578/1998

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses It has not been dealt in the Greek legislation. Although there are no administrative guidelines, presumably losses are lost for tax purposes.	N/A.

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder The Greek transposing legislation does not provide for the avoidance of economic double taxation.	Article 6 para. 1 of Law 2578/1998

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
8.2 Computation of the capital gain No guidance has been issued. Therefore, the general rules of Greek tax law should apply. Capital gains are treated under Greek law as business profits. No specific definition of capital gains exists under Greek law. Basically, the term includes all gains arising from alienation of tangible and intangible assets of an enterprise. Cash payments under Article 8 (9) of the Merger Directive are subject to taxation.	Article 6 para. 1-3 of Law 2578/1998

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
8.3 Further conditions for tax relief No further conditions for said tax relief exist.	N/A.

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>**9.1 Avoidance of economic double taxation at the level of the transferring company**</u> The Greek law has not made any specific reference to any provisions for the avoidance of the double taxation. No general rules provisions with respect to the avoidance of economic double taxation exist in Greece.	Article 3 para. 3 of Law 2578/1998

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>**9.2 Further conditions for tax relief**</u> No further conditions for tax relief are applicable.	N/A.

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>**9.3 Tax deferral**</u> N/A. No account of the ECJ case law has been taken.	N/A.

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>**10.1 Loss recapture for permanent establishments in third Member States**</u> Greece does not consider loss recapture as stated in Article 10(1) as it applies the derogation available in provision of Article 10 (2).	Article 3 para. 6 of Law 2578/1998

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> Greece does not consider loss recapture as stated in Article 10(1) as it applies the derogation available in provision of Article 10 (2).	Article 3 para. 6 of Law 2578/1998

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> As per the transposing Greek law provisions, the capital gain of the permanent establishment of a Greek merging company is subject to income tax. From the abovementioned income tax is deducted the total tax that would have been imposed in the Member State in which the permanent establishment is situated. There is neither a carry-back nor a carry-forward option for foreign tax credit, i.e. it is lost for tax purposes.	Article 3 para. 6 of Law 2578/1998

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
<u>10.4 Tax deferral</u> No.	N/A.

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
<u>10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies</u> Greek tax law does not make any reference to tax transparent entities, since no tax transparent entities exist under Greek law. However, Law 2578/1998 as amended provides that a foreign company is considered as tax transparent if its profits are taxed in the hands of its shareholders or partners, according to the foreign legislation. In this case, the profits or capital gains would be taxable in the hands of Greek resident members of the transparent entity. From the	Article 3 para. 7 of Law 2578/1998

abovementioned tax is deducted the total tax that would have burdened the foreign entity in case the provisions of the Greek transporting law did not apply.	

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit The tax basis for the notional tax credit is the positive difference between the fair market value of the transferred assets and liabilities and their net book value.	Article 3 para. 7 in combination with Article 3 para. 1 of Law 2578/1998

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit The notional tax credit is determined as amount of tax that would have been imposed against the foreign transparent entity if Law 2578/1998, as amended, had not been applicable.	Article 3 para. 7 of Law 2578/1998

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders According to the transposing law of the Directive, Greece does not apply the merger directive when the non-resident receiving or acquiring company is a deemed fiscally transparent one.	Article 6 par. 3 of Law 2578/1998 as amended

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company Greece has not transposed Article 10a(4) of the Merger Directive.	N/A.

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
<u>10b.1 Exit taxation</u> Yes, it would give rise to exit taxation under the provisions of Article 106 of Law 2238/1994. Law 2238/1994 is the Greek Income Tax Code. Such taxation should not be contrary to EU law under the '*Daily Mail*' case law.	Article 106 of Law 2238/1994

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
<u>10b.2 The term 'head office'</u> There is no definition of the term 'head office' in Greek legislation.	N/A.

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
<u>10b.3 Head office and tax residency</u> Given that Greece applies the siège réel doctrine, the transfer of the head office should coincide with the transfer of tax residency.	N/A.

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>10b.4 Assets and liabilities not effectively connected with a permanent establishment</u> There is no guidance as regards the tax treatment of such assets. Their taxation or not, would depend on the general tax rules and the application of the relevant Double Taxation Treaty provisions.	N/A.

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the '*N*' case?	Reference
10b.5 Tax deferral N/A. No account of the ECJ case law has been taken in Greece.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 The term 'comparable circumstances' There are no administrative guidelines for the definition of the above term.	N/A.

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Loss recapture for permanent establishments Losses attributable to permanent establishment in a third Member State may not be utilized in Greece.	Article 4 para. 4 of Greek Tax Income Code (Law 2238/1994)

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
10d.1 Deemed liquidation The transfer of registered office of an SE should not give rise to a deemed liquidation from a tax perspective unless no permanent establishment remains in Greece. In any case no taxation should exist.	N/A.

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
10d.2 Tax treatment of third country residents Please see above 10d.1	N/A.

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
11.1 Transposition of anti-abuse provisions By virtue of the provisions of Article 8 of Law 2578/1998, the exact wording of Article 11(1)(a) of the Directive was transposed into Greek law. There are no further administrative guidelines specifying and / or giving guidance on the parameters of anti abusive exercise of rights within the framework of the Directive.	Article 8 of Law 2578/1998

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
11.2 General anti-abuse provision There are no general anti-abuse measures.	

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the '*Cadbury*' judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' No account of the '*Cadbury*' judgment has been taken by the Greek tax authorities.	N/A.

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions N/A given that the Directive has never been implemented in practice in Greece.	N/A.

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' The concept of 'valid commercial reasons' has been redefined as economically fair reasons while the other two terms have been interpreted as such. There is no guidance on the concept of 'economically fair reason'.	Article 8 of Law 2578/1998

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof Law 2578/1998 does not make any reference as to which party has the initial burden of proof. According to Greek case law regarding other tax matters (e.g. transfer pricing), it is the tax authority the party that has such burden of proof.	N/A.

HUNGARY

Abbreviations

English	Hungarian	English	Hungarian
Act on CIT	Tao. törvény	Act LXXXI of 1996 on Corporate Tax and Dividend Tax	1996. évi LXXXI Törvény a Társasági Adóról és Osztalékadóról
Act on Accounting	Sztv.	Act C of 2000 on Accounting	2000. évi C Törvény a Számvitelről
Act on Solidarity Surtax		Act LIX of 2006 on the Introduction of Special Tax to Improve the Balance of Public Finances	2006. évi LIX. Törvény az Államháztartás egyensúlyát javító különadóról és járadékról
Act on Tax Procedure	Article	Act XCII of 2003 on Tax Procedure	2003. évi XCII. Törvény az Adózás Rendjéről

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.

Overall state of implementation

Corporate Income Tax

In Hungary, the provisions of the Merger Directive were first introduced by Act XLII of 2002, effective as of 1 January 2003. The provisions implementing the Merger Directive could only be applied by Hungarian companies for the first time when determining their corporate income tax liability for the 2003 tax year. Further amendments to the Hungarian Act on Corporate Income Tax ('CIT') for the purpose of implementing the Merger Directive were introduced by Act XCI of 2003 (effective as of 1 January 2004), Act XLV of 2004 (effective as of 8 October 2004), Act CXIX of 2005 (effective as of 1 January 2006), Act LXI of 2006 (effective as of 1January 2007).

Additionally, it should be noted that the benefits of the Merger Directive are not only available in Hungary to cross-border transactions, but also to purely domestic transactions. Hungarian legislation distinguishes between preferential transactions and general transactions. Preferential transformations are those transactions which may enjoy the benefits available under the Merger Directive, but also have to meet further conditions.

As regards subsequent preferential mergers, certain changes were introduced in the Hungarian legislation in this respect. Nevertheless, in practice, it is not clear how the Directive has to be interpreted in conjunction with Hungarian legislation in such cases.

Solidarity Surtax

The solidarity surtax for companies in Hungary was introduced as of 1 September 2006; nevertheless, the Act on Solidarity Surtax did not include any rules relating to preferential transformations, exchange of shares and transfer of assets. However, these rules were introduced into the Act on Solidarity Surtax by Act CXXXI of 2006 (effective as of 1 January 2007). The provisions contained in the Act on Solidarity Surtax on preferential transformations, exchange of shares and transfer of assets mirror the provisions in this respect included in the Act on CIT, i.e. either the wording of the provisions in both acts is almost identical or the Act on Solidarity Surtax directly refers to the relevant provision of the Act on CIT. Therefore, the provisions of the Act on Solidarity Surtax implementing the provisions of the Merger Directive should be interpreted in the light of the Act on CIT and of the Act on Accounting.

Administrative guidance and national case law

There is not much administrative guidance or national case law dealing with the interpretation of the provisions on preferential transformations, exchange of shares and transfer of assets, even if there are interpretative holes as regards the method of practical implementation and the exact wording of the implementing provisions. Up until now there has only been one administrative guideline published by the Hungarian Tax Authority which refers to the need for making transfer

pricing adjustments to the taxpayer's corporate income tax base whenever the transfer of assets between related parties is not carried out at fair market value.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies (corporations)</u> We note that 'preferential transformations' are those transactions which may enjoy the benefits of the Merger Directive, subject to the conditions stipulated in the Merger Directive. The expression 'in which companies from two or more Member States are involved' includes only the companies directly involved in the preferential transformation and does not refer to their individual shareholders or parent companies. (However, income realized in Hungary by foreign entities without a permanent establishment is not subject to Hungarian taxation.) The term 'companies involved' refers to the corporations taking part in the transaction and does not mention their parent companies. According to the Act on CIT a 'corporation means a business association, nonprofit company and, effective as of the operative date of the Act promulgating the treaty on the accession of the Republic of Hungary to the European Union, any corporation domiciled in a Member State according to the tax laws of that state (a) the corporation does not have a domicile in a non-Member State under the provisions of a valid international agreement on income tax and wealth tax to which the said non-Member State is a party, and (b) b) the corporation operates in a form governed in the Council Directive on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States or in the Council Directive on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, and is taxable under these directives without the possibility of having an option or being exempt.' The transferring and the receiving companies must be corporations established in accordance with the legislation of a Member State within the meaning of Article 48 EC Treaty. The registered office and place of management of the transferring company and the receiving company must both be located within the EU, although not necessarily within the same Member State.	Act on CIT, Section 4(32/A) Act on CIT, Section 2(2a) Act on Solidarity Surtax, Sections 10-12 and Section 7(3)

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
1.2 Foreign Member State and third state merger Hungarian legislation on preferential transformations applies as follows: As stated in 1.1, Hungarian legislation does not extend the tax benefits of preferential transformations, transfer of assets and exchange of shares to the foreign parent companies of the resident merging entities, but such transactions are not taxable anyway. Mergers between companies from a single Member State with domestic shareholders may benefit from a tax base adjustment available in the case of preferential transformations.	Act on CIT, Section 4 (32/A) Act on CIT, Section 2(2a) Act on Solidarity Surtax, Sections 10-12 and Section 7(3) Act on CIT, Section 7(1)gy)

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term 'securities' The term 'securities' as such is not defined in the Act on CIT. In case of a merger or a division / partial division, the Hungarian legislation does not refer to the term 'securities' of the predecessor or the successor company but uses the term 'shares', 'quotas' and 'ownership rights' instead. Nevertheless, Section 4(23/C) of the Act on CIT, the provision which defines the exchange of shares, refers to the term 'securities' of the receiving company and 'securities' representing the issued capital of the former company. Similarly, the Act on Accounting (which, based on the law, needs to be observed when interpreting the Act on CIT) does not include a definition of securities either. Instead, the Act on Accounting defines 'share certificate' as *'all (…) securities, (…) which signify a right (…), in which the issuer acknowledges that a certain amount of money, or non-financial assets whose value is determined in money, has been placed at its disposal and that it commits itself to provide predetermined financial and other rights to/for the holder of such securities. This, in particular, includes stocks, partnership shares, proprietary shares, share notes, contribution notes, and investment notes issued by unlimited term investment funds, venture capital notes and venture capital shares.'*	Act on Accounting, Section 3 (6) 3 Act on CIT, Section 4 (23/C)

This definition seems to imply that both terms, 'securities' and 'shares', are used interchangeably under the Hungarian legislation which implemented the Merger Directive.	

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' The possibility to allow a 10% cash payment for reorganization at book value was implemented in the Hungarian legislation in line with the Merger Directive. Based on Hungarian legislation, the 10% cash payment for reorganization at book value applies on an overall basis, allowing a cash buy-out of minority shareholders.	Act on CIT, Section 4 (23/A), (23/B) and (23/C)

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger The Act on CIT uses a different wording than the one used in the Merger Directive for defining mergers, i.e. Hungarian legislation does not distinguish between the three types of merger described in the Merger Directive. Even so, the provision of the Act on CIT covers the scope of Article 2(a) of the Merger Directive. However, no further types of merger have been implemented into Hungarian legislation.	Act on CIT, Section 4(23/A)

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares Hungarian legislation follows the provisions of the Merger Directive in this respect. Under an exchange of shares, provided the acquiring company can obtain the majority of voting rights in the acquired company, or, if it	Act on CIT, Section 4 (23/C)

already held a majority of the voting rights before the transaction took place, it is entitled to increase its shares in order to consolidate its majority while still benefiting from the preferential tax treatment.	

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>2.5 Consolidation of qualifying holding</u> Hungarian legislation does not impose any conditions for benefiting from the preferential tax treatment available to exchange of shares when a company consolidates an existing majority holding.	Act on CIT, Section 4 (23/C)

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 *'Andersen og Jensen'*. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>2.6 The term 'branch of activity'</u> 'Branch of activity' is defined in the Hungarian legislation as 'all the assets and liabilities (including accrued expenses and deferred income) of a division of a company that, from an organizational point of view, constitutes an autonomous unit capable of functioning with its own assets and means'. In this respect, the Hungarian Tax Authority has not issued any guidance clarifying the concept 'branch of activity' and specifying which assets and liabilities are deemed to belong to the branch of activity.	Act on CIT, Section 4 (23/B)

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> For the purpose of defining 'company of a Member State', the provision dealing with preferential transformations (included in Section 4(23/A) of the Act on CIT) states that the term company or corporation has to be interpreted in the light of the definition of 'corporation' included in Section 4(32/A) of the Act on CIT. Pursuant to this provision, *'corporation' means a business association, and nonprofit company, and, effective as of the operative date of the Act promulgating the treaty on the accession of the Republic of Hungary to European Union, any corporation domiciled in a Member State according to the tax laws of that State*	Act on CIT, Section 4 (32/A)

(a) that does not have a domicile in a non-Member State under the provisions of a valid international agreement on income tax and wealth tax to which the said non-Member State is a party, and (b) that operates in a form governed in the Council Directive on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares, concerning companies of different Member States or in the Council Directive on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, and is taxable under these directives without the possibility of having an option or being exempt'. The above definition clearly follows the definition of 'company of a Member State' provided by the Merger Directive, i.e. in the Annex.	

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>3.2 Transparent entities</u> The Hungarian legislation does not regard any of the entities listed in the Annex as being transparent.	

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
<u>3.3 Qualification of tax residency</u> <u>3.3.1 Domestic legislation</u> Section 2(2) of the Act on CIT states that 'of domestic persons, the following shall be deemed resident taxpayers: a) business associations (including non-profit business associations), and European Company (SE) (including European holding companies) and European cooperative societies'. This provision lists further domestic entities which are considered to be resident for Hungarian tax purposes, but have not included them since they are excluded from the application of the Merger Directive.) In other words, if these entities are incorporated in Hungary, they are considered to be tax residents in Hungary. Further, pursuant to Section 2(3) of the Act on CIT, 'any foreign person whose place of management is located in Hungary shall be deemed a resident taxpayer'. Section 4(35) of the Act on CIT states that 'the place of management means the place where management governs the operations of the company'.	Act on CIT, Section 2 (2) and (3)

3.3.2 Double tax conventions The DTCs concluded by Hungary are based on the OECD Model Convention. Therefore, the tiebreaker criterion followed by Hungary is the place of effective management criterion.	

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject-to-tax clause The Hungarian Act on CIT introduced the subject-to-tax clause in its definition of corporation (see question 3.1) by stipulating that a corporation is 'any corporation domiciled in a Member State according to the tax laws of that state'. This provision of the Act on CIT clarifies that this clause needs to be interpreted in the light of the Merger Directive (i.e. the company needs to 'operate in a form governed in the Council Directive on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States'. No administrative guidance has been issued in order to clarify the subject-to-tax clause.	Act on CIT, Section 4 (32/A)

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
3.5 Shareholder requirements The nationality or the residence of the company's shareholders is irrelevant when it comes to applying to them the benefits of the Merger Directive.	

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
4.1 The concepts of 'real values' and 'value for tax purposes' The Act on Accounting determines real value as 'fair value', meaning 'the amount for which an asset can be exchanged (sold or purchased) or for which a debt can be settled between properly informed parties with intent to enter into a business deal under a transaction (contract) concluded under customary market conditions.' The Hungarian Act on CIT uses the term 'real value' to mean the fair	Act on Accounting, Article 3 (9) 12. Act on CIT, Article 4 (23/A)

market value of the assets and liabilities which is the value to be paid when selling the single asset at market price. The 'value for tax purposes' has been interpreted as the tax book value of the assets in the books of the transferring company at the time of the merger or division.	

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions No specific guidance has been issued for divisions or partial divisions.	

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' The definition of 'permanent establishment' in the Act on CIT follows the definition set out in the OECD Model Tax Convention. Accordingly, Section 4 (33) of the Act on CIT stipulates that a 'permanent establishment' is a *'permanent business establishment, equipment, and accessories that are used by the taxpayer in whole or in part for business activities irrespective of the legal title, whereby the term shall include, in particular, the place of management, representative offices established with a registered office in Hungary, offices, factories, plants, workshops, mines, crude oil or natural gas wells, and other facilities used to explore or exploit natural resources.'* Construction or assembly sites are also considered to constitute permanent establishments. In this respect, it is also important to determine the place where the profits or losses are deemed to be generated. Therefore, the Act on CIT also defines what is considered to be the 'place of gainful activity' and clarifies which activities are attributable to a branch. In this respect, the 'place of gainful activity' means, *'in respect of income from business operations, the place of business where the gainful activity is performed; if, however, the business operation is not pursued in a branch, it shall be the location where the operator of the enterprise is registered as a resident, in respect of dividends, the place where the person paying (providing) the dividend is a resident, or if paid (provided) by a resident business establishment of a foreign enterprise or by a domestic branch of a nonresident entrepreneur.'* The Act on CIT also prescribes how the corporate income tax base of foreign companies has to be determined (in those cases where no double tax treaty applies). Accordingly, foreign companies have to calculate their corporate income tax base, together for all its domestic business establishments, exclusive of branch offices and separately for each of its Hungarian branch offices, in line with the provisions of the Act on CIT	Act on CIT, Section 4(33) Act on CIT, Section 4(22) Act on CIT, Section 14

which include the tax base adjusting items. The sales revenue, income, costs and expenses of a business establishment have to be recorded as if it were a separate entity, independent from the foreign company. Consequently, even if Hungarian legislation remains silent as regards the concept of 'effectively connected', this provision stipulates that separate records have to be kept for branch offices. This also means that the assets and liabilities need to be allocated to the branch office if attributable to such branch offices. No administrative guidance has been issued in respect of the above.	

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief The Act on CIT seeks to recapture depreciation on the assets transferred if the transformation does not qualify as a preferential transformation. Nevertheless, since the provisions of the Merger Directive implemented into Hungarian legislation are those referred to as preferential transformations, for preferential transformations, the Hungarian legislation does not limit the scope of tax relief set out in the Merger Directive. The Hungarian Tax Authority has not published any official guidelines limiting the scope of relief by seeking to recapture depreciation on the assets.	

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment As stated in 4.3, Hungarian legislation does not specify which assets or liabilities are effectively connected to the permanent establishment. Moreover, Hungarian legislation does not include a provision which would determine the tax treatment of assets and liabilities that are not considered to be effectively connected with a permanent establishment. Therefore, based on the general rules, assets and liabilities not effectively connected with a permanent establishment would be taxable.	Act on CIT, Section 16

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company The Hungarian legislation seems to imply that the merger is profit tax exempt at the level of the receiving company even if the profit is allotted to shares of the receiving company in the transferring company.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral Case C-470/04 'N' has not been taken into account for Hungarian tax purposes. Based on the Act on CIT 'if the taxpayer is no longer subject to this Act for any reason, except for termination due to transformation, or if its registered office is transferred to another country, it shall be considered as termination without succession. This provision shall not apply when a SE or a European cooperative society transfers its registered office to another country in connection with the activities it pursues as a non-resident entrepreneur. Furthermore, this provision shall not apply to any non-resident entrepreneur whose activities are taken over by a SE or a European cooperative society.' In the case of a termination without succession, certain corporate income tax base increasing items should be applied, as described in Act on CIT, which may result in a positive tax base for the company migrating abroad. Furthermore, as regards those assets and liabilities not effectively connected to a permanent establishment (please see 4.5).	Act on CIT, Section 16(7) Act on CIT, Section16(1) c)

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities Hungarian law does not recognize the concept of fiscally transparent entities; therefore, it is unclear how Hungarian law would treat such entities established under foreign law. We are aware that in some specific cases (not related to the interpretation of the Merger Directive) for Hungarian tax purposes, the Hungarian authorities treated some fiscally transparent entities as transparent based on the qualification of non-Hungarian tax laws. However, no public guideline is available, and each case should be	

investigated in a case-by-case basis since the authorities also have very limited experience in this respect.	

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief Several formal requirements have to be met by the companies involved in order to benefit from the preferential tax treatment for mergers, divisions and partial divisions (e.g. closing the books of the legal predecessor company, filing tax returns, filing documents with the Court of Registry, informing the creditors and the contractors of the legal predecessor about the merger and merging the books of the companies). In the event of preferential transformation, the conditions for tax relief are the following: The predecessor has to notify the Tax Authority in its closing tax return that it will not adjust its CIT base. The successor will determine its CIT base, as if the merger had not been carried out. In other words, it will depreciate the assets based on their original value as shown in the predecessor's books before the revaluation. The successor is obliged to keep separate records concerning the assets and liabilities taken over from the legal predecessor. These records should contain the historical cost, the tax and accounting book value of the assets and liabilities recorded in the predecessor's closing books as well as the CIT base adjustments accounted for by the successor following the merger.	Act on Accounting Section 137-138,

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
5.1 The term 'provisions and reserves' The term 'provisions and reserves' is not defined in the Hungarian Act on CIT. However, according to Section 1(5) of the Act on CIT, this piece of legislation shall be interpreted in observation and in harmony with the provisions of the Act on Accounting. In other words, the terms defined in the Act on Accounting are equally applicable when interpreting the Act on CIT. Similarly to the Act on CIT, the term 'provisions and reserves' as such is also not defined in the Act on Accounting. Only the term 'provisions' has been defined in Section 41 of Act on Accounting; nevertheless, throughout this Section, the term 'reserves' is used in conjunction with the term 'provisions'. Therefore, it can be concluded that even if only the term 'provisions' has been defined, indeed it refers to both 'provisions and reserves'.	Act on CIT, Section 1(5) Act on Accounting, Section 41(1)-(3)

Section 41 of the Act on Accounting defines provisions as follows: '(1) Provisions shall be formed to the debit of pre-tax profit or loss - to the extent necessary - to cover payment liabilities towards third persons which originate from past and current transactions and contracts [...] and which are likely or sure to be incurred by the balance sheet date; however, the amounts of such liabilities are not established by the balance sheet preparation date and the company has not provided the required cover for such in any other form. (2) Provisions may be formed to the debit of pre-tax profit or loss - to the extent necessary to establish the actual profit or loss - to cover major and recurrent liabilities with the potential to occur in the future which are likely or sure to be incurred by the balance sheet date; however, the amounts and the actual date of such liabilities are not established by the balance sheet preparation date, and cannot be shown under accrued expenses and deferred income. (3) Provisions according to subsection (2) may not be formed for expenses regularly and continuously incurred in normal business activities.' Further, no administrative guidance has been issued by the Hungarian Tax Authority relating to the term 'provisions and reserves'.	

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
<u>5.2 Exclusion of 'provisions and reserves' from permanent establishments</u> The Hungarian tax legislation remains silent as regards those provisions and reserves which should be attributable to a foreign permanent establishment or business division. Nevertheless, Section 16(11) of the Act on CIT prescribes that 'after transformation, the successor shall determine its tax base taking into consideration the assets and liabilities received from the predecessor (including provisions and reserves or accrued income), by adjusting the pre-tax profit, as if the transformation had not taken place'. The wording of this provision, i.e. the expression 'as if the transformation had not taken place', is vague and does not clarify how the provisions and reserves from a permanent establishment can be distinguished from those of other permanent establishments or of the company as a whole. Nevertheless, this provision seems to imply that the carry over of provisions and reserves should be tax exempt.	Section 16(11) of the Act on CIT

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
<u>5.3 Allocation method for provisions and reserves</u> The Hungarian legislation does not regulate the methods to be applied to allocate provisions and reserves in the case of a division, partial division and transfer of asset. Please see 5.2.	

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
<u>5.4 Further conditions for carry-over of provisions and reserves</u> Since the Hungarian legislation does not contain any provision similar to Article 5 of the Merger Directive, the carry-over of provisions and reserves seems not to be linked to any other conditions.	

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
<u>6.1 The concept of carry-over of losses</u> The term 'loss' was not specifically defined for the purpose of implementing the Merger Directive; the general interpretation under the Hungarian CIT will be applicable. Accordingly, 'loss' means the negative corporate tax base of a company or a branch determined in accordance with the provisions of CIT. Based on the Act on CIT, the tax losses incurred may be carried forward indefinitely. Nevertheless, after the fourth tax year of the establishment, i.e. the registration of the company with the Court of Registry, (in the case of transformations also including the legal predecessor's tax years), a permit from the Hungarian tax authorities is needed for carrying tax losses forward if the pre-tax profit (in a particular year) is negative and if one of the following criteria is met: the total revenues are less than 50% of the costs and expenses; or the tax base was also negative in the previous two tax years. The application of the tax losses has to be established based on regulations effective in the year in which the losses were generated. Therefore, it is possible that certain tax losses generated before 2004 can only be carried forward for five years as a result of the limits set forth by earlier rules. Losses carried forward can be offset against the company's future profit. No carry-back of losses is possible.	Act on CIT, Section 17(1) Act on CIT, Section 17(8)

In the case of transformations (e.g. mergers) the legal successor may utilize losses brought forward by the legal predecessor without any administrative procedure.	

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment Incomes and expenses are allocable to a PE if they are derived from (or occur in connection with) the activity of the PE. Should a PE realize losses, it can carry them forward, in a similar way to the provisions applicable to a company. This interpretation is supported by Article 17 of the CIT concerning the loss carry forward, which provides that 'taxpayers' can carry forward losses as outlined in point 6.1. Since the definition of 'taxpayer' also includes PE's of foreign companies, the above rules are also applicable to them. In the case of a cross-border merger, when a Hungarian entity merges into a foreign one and the Hungarian company ceases to exist, due to the remaining business activity and assets in Hungary, the surviving foreign company will most likely have a PE in Hungary (which will also be taxable for corporate income tax purposes in Hungary). Therefore, one may argue that the losses incurred by the Hungarian company (which ceased to exist) can be utilized by the foreign company; more specifically by the Hungarian PE of the foreign company. However, to date, no guidance has been issued on this matter. With regard to the rules of national mergers, please see 6.1.	Act on CIT, Section 17(1) Act on CIT, Section 2(4) Act on CIT, Section 17(7)

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets Special provisions apply to the transfer of assets. Under CIT, the receiving company can utilize the losses incurred by a separate division (to whom the assets belong) of the transferring company while the transferring company can no longer use those losses. With respect to divisions and partial divisions, the losses carried forward should be split in the ratio of the balance sheets of the entities involved.	Act on CIT, Section 17(7) Act on CIT, Section 6(8c)

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses N/A.	

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Amended holding threshold There is no restriction on the holding threshold under Hungarian legislation.	Act on CIT, Section 7(1gy)

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses Generally, losses realized in connection with the cancellation of shares should decrease the company's profit for accounting as well as taxation purposes (i.e. it should be tax deductible). Since Hungarian tax law does not provide for specific provision to the treatment of losses realized on the cancellation of a holding, in our view this should imply that such losses are also tax deductible.	

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder In case of a merger/division/partial division the income deriving from the allotment of shares is not subject to corporate income tax at the time of the allotment. The relevant law provides that '*the shareholder, in case of a preferential transformation, may deduct from its tax base the accrued income that exceeds the acquisition value of the shares in the transferring company, which have been disposed of in the course of the merger or*	Act on CIT, Section 7(1gy) Act on CIT, Section 8(1r) Act on CIT, Section 8(1t) Act on CIT, Section

division.' However, if later on the shares are cancelled from the books, the above decreasing item (as deferred income) increases the pre-tax profit of the shareholder of the receiving company for the actual tax year (i.e. the taxation of the income is deferred until the shares acquired are disposed of). The amount of capital gain realized during the tax year, as earned on shares transferred under an exchange of shares by the member (shareholder) of the acquired company, can remain non-taxable, provided that the taxpayer opts for this treatment. In this case, the taxpayer must keep separate records of all shares acquired as part of the exchange of shares. The value attributed to the shares received by the acquiring company is determined by its shareholders; however, this value should not be higher than market value. Accordingly, the value attributable to the shares can be the book value, i.e. the value that the shares had before the transaction. The value that is used for book purposes is also applicable for tax purposes. If the shareholder of the acquired company and the acquiring company are considered as related parties for transfer pricing purposes, the transfer pricing rules apply for the exchange of shares. Pursuant to Section 18, (6) of the Act on CIT, should the shares not be transferred at market value, the difference between the value of transfer and the market value would be taxable. Therefore, the difference between the value of transfer and the market value is taxed based on the Hungarian transfer pricing rules regardless of the fact that the difference could have been differed for tax purposes as outlined above. Thus, the Hungarian transfer pricing rules are unlikely to be fully coherent with the Directive.	7(1h) Act on CIT, Section 6(8d) Act on CIT, Section 18

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>**8.2 Computation of the capital gain**</u> Under the general rules, cash payment should be deemed as part of the consideration received by the shareholder of the transferring/acquired company and is included in the computation of the capital gain.	Act on CIT Section 4(23a)

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>**8.3 Further conditions for tax relief**</u> No further conditions are prescribed.	

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>9.1 Avoidance of economic double taxation at the level of the transferring company</u> Based on the Act on CIT, transferring companies 'have the option to decrease their pretax profit by the portion of the income realized in connection with the transfer of a business unit that is in excess of the book value of the transferred assets, or shall increase the pretax profit by the portion of the book value of the transferred assets that is in excess of the income realized.' When the assets are transferred at fair market value, the tax on the gain on the assets is deferred until the sale of the shares received in exchange.	Act on CIT, Section 16(12)

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>9.2 Further conditions for tax relief</u> Based on the Act on CIT, the tax relief granted in Hungary upon the transfer of assets is not subject to any of the aforementioned requirements (i.e. holding period requirements, continuity of business requirements, nationality requirements) but rather to formal requirements. Accordingly, Section 16(13) of the Act on CIT stipulates that 'the tax relief may be applied on condition that the written agreement, drawn up on the preferential transfer of assets, contains an itemized list of the transferred assets and liabilities (including deferred expenses or accrued income), indicating their original value and book value recorded by the transferring company for the day of transfer, and that the agreement contains a clause stipulating the commitment for the application of the provisions contained in Subsection (14), and that the transferring company notifies the tax authority of its selection in the tax return filed for the tax year in which the preferential transfer of assets took place, with an original copy or a notarized duplicate of the agreement attached.' Further requirements are set out in Section 16(13) of the Act on CIT: 'the receiving company shall keep separate records on the assets and liabilities received, indicating their original value and the book value with and without adjustments by the transferring company for the day of transfer, their adjusted recorded value as well as the sums it has claimed after the transfer to adjust the pretax profit on the basis of the assets and liabilities in question.'	Act on CIT, Section 16(13)-(14)

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
9.3 Tax deferral Case C-470/04'N has not been taken into account for Hungarian tax purposes. Based on the Act on CIT 'if the taxpayer is no longer subject to this Act for any reason, except for termination due to transformation, or if its registered office is transferred to another country, it shall be considered as termination without succession. This provision shall not apply when a SE or a European cooperative society transfers its registered office to another country in connection with the activities it pursues as a non-resident entrepreneur. Furthermore, this provision shall not apply to any non-resident entrepreneur whose activities are taken over by a SE or a European cooperative society.' In the case of a termination without succession, certain corporate income tax base increasing items should be applied, as described in Act on CIT, which may result in a positive tax base for the company migrating abroad.	Act on CIT, Section 16(7)

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
10.1 Loss recapture for permanent establishments in third Member States Hungarian legislation is silent with respect to loss recapture for permanent establishments, however, it is reasonable to assume that there is no loss recapture in such situation.	

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
10.2 Permanent establishment in the Member State of the receiving company There is no specific Hungarian regulation for the branch conversion.	

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
10.3 Concept of worldwide taxation/tax credit system Hungary follows worldwide taxation principle. The Hungarian tax treatment of the tax paid in other countries should be determined on the basis of the relevant double taxation treaties and the supporting rules of the Act on CIT, as well as Act on Solidarity Surtax. Under most double taxation treaties concluded by Hungary, the exemption method is applicable. Under domestic rules, the credit method is applicable provided that there is no double taxation treaty in force. However, the application of the credit method in a specific situation is not clear since no guideline has been published and, as the exemption method is widely used under the treaties, there is no experience in this respect.	Act on CIT, Section 28 Act on Solidarity Surtax, Section 6

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
10.4 Tax deferral No specific account has been taken of ECJ case law.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies Hungarian law does not recognize the concept of fiscally transparent entities; therefore, it is unclear how Hungarian law would treat such entities established under foreign law (please see 3.2). We are aware that in some specific cases (not related to the interpretation of the Merger Directive) for Hungarian tax purposes, the Hungarian authorities have accepted interpretations where they treated some fiscally transparent entities as transparent based on the qualification of non-Hungarian tax laws. However, no public guideline is available, and each case should be investigated in a case-by-case basis since the authorities also have very limited experience in this respect.	

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit N/A.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit N/A.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders N/A.	

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company N/A.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
<u>10b.1 Exit taxation</u> Pursuant to Hungarian legislation, the transfer of the registered office would qualify as a liquidation of the company's activity in Hungary for corporate income tax purposes; therefore, final corporate income tax returns have to be submitted to the Hungarian Tax Authority. However, in the case of SEs and SCEs, this provision is not applicable, (i.e. the transfer of the registered office of an SE or SCE would not give rise to exit taxation under Hungarian legislation) for the business that the SE or SCE continues in Hungary through its Hungarian permanent establishment. However, please note that a Hungarian case (C-210/06 '*Cartesio*') was referred to the ECJ by a Hungarian Court and is still pending. Similarly to the '*Daily Mail*' case,' *Cartesio*' (resident for corporate income tax purposes in Hungary) wanted to transfer its head office to Italy; however, it required doing so by submitting its final corporate income tax returns. Given the importance of the case, the Grand Chamber looks to be the most likely body to decide on the case. The Advocate General's opinion was published on 22 May 2008. In its opinion, Advocate General Maduro supported Cartesio to transfer its head office without going into liquidation.)	Act on CIT, Section 16(7)

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
<u>10b.2 The term 'head office'</u> The term 'head office' has been translated into Hungarian legislation as 'place of management'. It means the place 'where the management governs the operations of the company'.	Act on CIT, Section 4(35)

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
<u>10b.3 Head office and tax residency</u> Pursuant to the Act on CIT, the Hungarian tax residency for corporate income tax purposes is determined by a) incorporation or b) the place of the head office/place of management. Accordingly, 'any foreign person whose place of management is located in Hungary shall be deemed a resident taxpayer'.	Act on CIT, Section 2(3)

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>10b.4 Assets and liabilities not effectively connected with a permanent establishment</u> As noted above, the transfer of the registered office would generally qualify as a liquidation of the company's activity in Hungary for corporate income tax purposes; therefore, final corporate income tax returns would have to be submitted to the Hungarian Tax Authority. However, in the case of SEs and SCEs, this provision is not applicable, (i.e. the transfer of the registered office of an SE or SCE would not give rise to exit taxation under Hungarian legislation) provided that the SE or the SCE continues its activities in Hungary through its Hungarian permanent establishment. Should assets and liabilities not effectively connected with the permanent establishment, any gain on such assets is taxable as the preferential treatment for SEs and SCEs is not applicable. The question, whether the various exit taxation schemes of the Member States are contrary to the EC law, is widely disputed and the ECJ's case law is not straightforward in this respect either. Once any development in the interpretation of the EC law in this respect appears, this question may be reinvestigated.	Act on CIT, Section 16(7)

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
<u>10b.5 Tax deferral</u> No specific account has been taken of ECJ case law.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 The term 'comparable circumstances' The term 'comparable circumstances' has not been specifically defined for the purpose of the Directive in Hungarian tax laws, nor have guidelines been issued in this respect.	

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Loss recapture for permanent establishments See answer under point 10.1.	

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
10d.1 Deemed liquidation The Hungarian tax laws do no rule on this matter; the transfer of registered office of an SE/SCE should not generally result in any addition taxation on the shareholder level.	

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
10d.2 Tax treatment of third country residents There are no specific provisions in respect of third country residents; thus, the transfer of registered office of an SE/SCE should not generally result in any additional taxation on the shareholder level.	

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>**11.1 Transposition of anti-abuse provisions**</u> No special transposition of anti-abuse provisions has been performed for the purpose of the implementation of the Directive; however, the general anti-evasion or anti-avoidance tax rules are applicable.	Act on Tax procedures, Section 2(1)

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
<u>**11.2 General anti-abuse provision**</u> General anti-abuse provisions are also applicable for the transactions of the Merger Directive. The Act on Tax procedures also sets out a similar principle of anti-avoidance: 'all rights in tax-related matters shall be exercised within their meaning and intent. In the application of tax laws, contracts and other transactions contrived with the intent to evade the provisions of tax laws shall not be construed as exercised within their specific intent'. The principle of substance over form is also laid down in Hungarian legislation. According to the Act on CIT, 'any rule, tax allowance (tax relief, tax incentive) which affects tax liability or the amount of taxes, and results in the reduction of such, may be used and/or applied to the extent that the essence of the transaction to which it pertains or other similar action manifests the purpose of the rule or tax allowance. (…) If the essence of the transaction suggests that the sole purpose of the transaction is to obtain a tax advantage in favor of any or all parties, the costs and expenditures charged on the basis of such transaction shall not qualify as costs and expenditures incurred in the interest of the enterprise, and no tax allowance may be claimed'. Based on our view, the anti-abuse provisions described above are in accordance with the EC Law.	Act on Tax procedures, Sec. 2 (1) Act on CIT, Section 1(2)

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' Hungarian legislation has not been amended to reflect the 'Cadbury' judgment. Furthermore, the term 'wholly artificial arrangement' is not interpreted by either the Hungarian legislation or any guidelines. Thus, the general anti-abuse provisions are applicable.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions N/A.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' No guidelines have been issued in this respect, therefore the general anti-abuse rules are applicable.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof As a general principle, the burden of proof is always with the party who has the interest in the question. Pursuant to CIT, 'Any rule, tax allowance (tax relief, tax incentive) which affects tax liability or the amount of taxes, and results in the reduction of such, may be used and/or applied to the extent that the essence of the transaction to which it pertains or other similar action manifests the purpose of the rule or tax allowance. Applicability or enforceability must be demonstrated by the party in whose interest it stands.' In the case of a tax audit, the Act on Tax procedures provides that 'The tax authority shall clarify the facts and prove its findings at the conclusion of the inspection, unless the burden of proof resides with the taxpayer.'	Act on CIT, Section 1(2) Act on Tax Procedures, Section 97(4)

IRELAND

Abbreviations

English	English
TCA 97	Taxes Consolidation Act 1997
FA 2006	Finance Act 2006
Revenue	Irish Revenue Commissioners
SDCA 99	Stamp Duties Consolidation Act 1999

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.

Overall state of implementation

The original 1990 Mergers Directive (referred to from hereon as the 'Directive', a term that will be applied to both the original legislation and the amended legislation as appropriate) was implemented through new provisions included in Finance Act 1992 which took effect from 1 January 1992. The scope of these rules, which are now contained in Part 21 TCA 1997 was limited to:

(a) the transfer of an Irish trade, or part of a trade, between two companies (not necessarily resident in two different Member States);

(b) the transfer of the whole or part of a trade carried on through a non-Irish branch in return for securities in the receiving company; and

(c) the transfer of an asset used for the purpose of an Irish trade to a company which holds all of the securities representing its capital.

The rationale for limiting the implementation to these situations involving transfers of assets was that the Irish Revenue did not consider that mergers, divisions and (later) partial divisions were possible under Irish company law as it existed at the time. However, discretion was given to Revenue to extend relief on a 'just and reasonable' basis to any other transactions 'of a type specified in the Directive' upon application in writing to the Revenue. While there is no evidence to suggest the Revenue would refuse to give relief for transactions covered by the Directive, the discretionary nature of this measure could be viewed as an inadequate means of implementing the Directive especially in light of the fact that on 27 May 2008, Ireland transposed into Irish law Directive 2005/56/EC on cross-border mergers (10th Company Law Directive).

Furthermore, specific legislation was not brought into account for share for share exchanges on the basis that Ireland already had legislation in place that governed the taxation of paper for paper exchanges and that this legislation was already compliant with the Directive.

In response to Regulation 2157/01 introducing the Societas Europea (SE) and the amendments in Directive 2005/19/EC of 17 February 2005, Ireland introduced legislation in Finance Act 2006 amending the original 1992 legislation with effect from 1 January 2006. These amendments primarily facilitate the creation of an SE and do not extend the 1992 provisions to other Mergers, Divisions or Part-divisions.

Method of Implementation

Irish Tax law is made up of a number of different statutory acts and instruments, which as far as Corporation Tax, Income Tax and Capital Gains Tax are concerned, are usually incorporated into Taxes Consolidation Act 1997.

Specific Areas of Irish Tax Law

The specific areas of Irish tax legislation that implement the Directive are contained in the following areas (references to 'pre-1992' etc. indicate when the legislation or its pre-consolidation equivalent was introduced):

(a) taxes Consolidation Act 1997;

(b) share for *share* exchanges (pre-1992) – sections 586, 587;

(c) company *reconstruction* or amalgamations involving transfers of assets where the transferring company receives no consideration for the transfer (pre-1992) - section 615;

(d) capital gains and capital allowances arising on transfers of assets (1992) – sections 630 – 633, 635 and 636;

(e) credit for deferred capital gains tax arising on transfers of trades of non-Irish branches to non-Irish companies (1992) – section 634;

(f) discretionary relief for other transactions of a type specified in the Directive (1992) – section 637;

(g) formation of SE or SCE by merger (2006) – sections 633A – 633C;

(h) residence of SE or SCE and transfers of head offices thereof (2006) – section 23B.

The rules implementing the Mergers Directive are not at a single location in the tax legislation but are instead scattered throughout TCA97.

Irish Revenue Guidance

The Irish Revenue issues guidance to taxpayers through a number of sources

(a) TCA97 Notes for Guidance – these provide guidance to taxpayers on how Revenue interprets the legislative provisions contained in TCA 97.

(b) Finance Act Guidance Notes – these provide a Revenue explanation of every legislative provision contained in each annual Finance Act.

(c) Tax Briefings – these are issued three to four times a year and provide the Revenue's view on specific technical topics.

(d) Ebriefs – these are electronic press releases issued on an ad-hoc basis when points of note arise that require comment by Revenue.

(e) Technical notes or guidelines – these are published from time to time on specific topics as needs arise.

Revenue Guidance

The guidance to date has been limited to the notes provided in connection with the 2006 Finance Act (revised Directive's amendments) and those on the consolidated legislation contained in TCA97.

Practical guidance is thin on the ground. The main reason for this is that, to date, there has been relatively little in the way of merger activity in Ireland. This might be partly explained by the fact that there was a general consensus held by many bodies, including Revenue that mergers were not permitted under Irish company law. The Revenue states in the current guidance notes on TCA97 that '*because it is generally not possible under existing EU or domestic company law for cross-border mergers and divisions of the type envisaged in the Directive to take place, relief is not specifically provided in respect of such transactions. However, Part 21 gives the Revenue Commissioners general authority to grant the reliefs specifically provided by the Directive in respect of any parts of the Directive to which effect is not given by specific measures*'.

Interestingly enough, no distinction has been made in the commentary between partial divisions and divisions. Partial divisions are widely defined in the Directive and would seem to cover many types of reconstructions for which relieving provisions already exist.

Parliamentary scrutiny of Mergers Directive proposal.

On 24 March 2004 Revenue and Department of Finance officials appeared before an Irish parliamentary committee (the Joint Committee on Finance and Public Service) to discuss the then proposed revisions to the Mergers Directive. The Revenue official indicated to the committee that generally Irish companies entered into 'reconstructions' or 'amalgamations' by way of share exchanges and that Irish law already provided for this. The official was unclear as to whether or not Irish law inhibited companies from merging but expressed the view that it probably limited the ways in which mergers could be carried out in Ireland.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> <u>1.1.1 Definition of company</u> The definition of 'company' is inconsistent between the various areas of legislation that implement the Directive. This can perhaps be attributed to the fact that in some instances the pre-existing Irish legislation was considered to sufficiently provide for the Directive's provisions and it was only in respect of the supplemental 1992 amendments that specific references to the Directive were introduced.	TCA 97 s586, s587, s615, s631, s632, s617
(a) Mergers, Divisions and Partial Divisions Ireland has not enacted specific legislation to cater for all mergers, divisions and partial divisions envisaged by the Directive on the basis that the Revenue view is that such transactions are not generally permissible and if necessary, discretionary relief can be given.	S.633A, S.633B, S.633C
However, the formation of an SE or SCE by merger is specifically catered for. In practice mergers, divisions and partial divisions are often affected by means of a combination of transfers of assets and an exchange of shares.	S.631, S.632

(b) Transfers of assets The 1992 amendments concerning transfers of assets define a 'company' as a company from a Member State within the meaning of Article 3 of the Directive (as amended). While the Directive obliges the reliefs to be granted in the case of transactions which involve companies from two or more Member States, the reliefs are extended to transfers between any two companies resident in the European Union. These two companies could be resident in the same Member State (including Ireland). The Directive provisions are not always required due to two other provisions that permit the transfers of assets. Firstly, where there is a scheme of 'reconstruction' or 'amalgamation' involving the transfer of the whole or part of a company's business to another company a deferral of tax on any capital gains arising is available if the transferring company receives no part of the consideration for the transfer (other than the receiving company taking over some or all of the liabilities of the business). Since 2002, this relief has been available to companies resident in a 'relevant Member State' as defined. For this purpose a 'relevant Member State' includes Member States of the European Communities plus EEA States with which Ireland has entered into double taxation agreements, i.e. Norway and Iceland. A 'company' appears not to be specifically defined for the purposes of this provision. The general definition of a 'company' for TCA97 purposes refers to a company being any 'body corporate' subject to certain exceptions for bodies established under specific Irish statutes (e.g. local authorities) and for European Economic Interest Groupings. Due to the widening of the scope of this provision to encompass companies resident in EU Member States there is less need to utilize the Directive's provisions. Secondly, transfers of assets, other than trading stock, within groups also attract chargeable gains tax deferrals. This relief also applies to group companies resident in 'relevant Member States' as outlined above. However, for this purpose a specific definition of 'company' is used which includes companies 'formed under the law of a country or territory outside the State'. In both of the above instances it is a precondition for obtaining relief that the assets remain chargeable assets following the transfer, e.g. because the assets are used by an Irish trading branch post transfer. In both instances there is no requirement that the transferring company and receiving company be resident in different Member States. (c) Share for share exchanges There is no definition of 'company' for share for share exchanges so the general definition of a company employed for capital gains purposes should be used. This defines a company as any body corporate with the exception of European Economic Interest Groupings. This would appear to be compliant with the Directive as it goes beyond the minimum relief that must be given. There is no territorial restriction within this area of legislation that would block the application of share for share relief. This goes beyond the	S.615 S.616 (definitions) S.617 S.586, S.587

minimum requirements of the Directive and hence appears to be in compliance with it. 1.1.2 Companies Involved The legislation enacting the Directive only covers the companies directly involved in the transfer of assets. These pre-existing provisions dealing with asset transfers and share for share exchanges do not refer to shareholders or parent companies.	

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
1.2 Foreign Member State and third state merger Irish legislation enacting the Directive does not interpret 'companies involved' as including parent companies. However, it is unclear, in the absence of specific provisions facilitating mergers, divisions and partial divisions to what extent discretionary relief would be available from the Irish Revenue if existing reliefs, e.g. for share exchanges, were found to be insufficient. As noted at 1.1 above, the benefits of the Directive vis-à-vis transfers of assets can apply to transfers between companies from a single Member State (whether foreign or Irish). Irish domestic law does not provide for relief for transfers of assets between non-Member States (third States). However, a Revenue concession exists that permits the transfer of assets to group companies resident in third States in situations where the transfer is part of the transfer of an Irish trade and the assets remain chargeable to Irish corporation tax. Certain conditions apply to put the concessional relief on the same footing as the statutory relief. As noted at 1.1 above a deferral of tax on chargeable gains may be available in transactions involving companies resident in Iceland and Norway.	S.637 S.617

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
<u>2.1 The term 'securities'</u> <u>2.1.1 Transfers of assets</u> The 1992 amendments dealing with transfers of assets define 'securities' as meaning shares (including stock) or debentures. No specific definition of shares or debentures is provided in the tax legislation so reference may be made to relevant company law. <u>2.1.2 Company law – shares</u> Shares are defined in company law as a 'share in the share capital of a company'. No further guidance is provided as to the meaning of this term. <u>2.1.3 Company law – debentures</u> Debentures are defined as including 'debenture stock, bonds and any other securities of a company'. No further guidance on the subject has issued by the Revenue. Some guidance can be obtained from UK case law (which is of persuasive influence on Irish Courts) where a debenture was taken to mean a document '… which either creates a debt or acknowledges it'. The provisions applicable to intra-group transfers of assets are not contingent on the issue of shares or securities. <u>2.1.4 Share for share exchanges</u> Prior to 4 December 2002 the 'share for share' relief for amalgamations and reconstructions applied to situations where companies issued shares or debentures (hence it is often referred to as 'paper for paper' relief). For that purpose shares were defined as including stock, debentures and where the company had no share capital (e.g. companies limited by guarantee) to '*any interests in the company possessed by members of the company*'. Post 4 December 2002 the 'share for share' relief does not generally apply where a company issues debentures, loan stock or other similar securities to a person in exchange for shares of another company unless the company issuing the debentures, loan stock or other similar securities and the person to whom they are issued are members of the same group throughout the period commencing one year before and one year after the day the debentures, loan stock or other similar securities are issued. This change was introduced for anti-avoidance reasons primarily to prevent the deferral/ non-taxation of gains on sales of domestic companies. It is unclear if the narrower definition of 'shares' that now applies accords with the meaning of 'securities' in the Directive.	S.630 (definitions) Companies Act 1963 Section 2 For example, Lemon v Austin Friars Investment Trust Ltd, UK Court of Appeal 1925 S.617 S.586, S.587

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' Irish tax legislation only facilitates mergers, divisions and partial divisions by way of transfers of assets and liabilities. 2.2.1 Transfers of assets The 1992 provision implementing the Directive's requirements on the transfer of assets only applies where a company transfers the whole or part of a trade carried on by it in Ireland to another company for a consideration which consists solely of the issue to the transferring company of securities in the receiving company. If this provision alone was required to carry out a merger, division or partial division it would appear not to be compliant with the Directive. The alternative relief for company reconstructions and amalgamations requires that the transferring company receive no part of the consideration for the transfer otherwise than by the assumption of the whole or part of the liabilities of the business. The terms 'reconstruction' and 'amalgamation' are not defined in the tax code. In the UK case of re *South African Supply and Cold Storage [1904] chd 268* the judge Buckley J stated that 'Neither of these words has any definite legal meaning. Each is a commercial and not a legal term and even as a commercial term, bears no exact definite meaning. In each case one has to decide whether the transaction is such that, in the meaning of commercial men, it is one which is comprehended in the term 'reconstruction' or 'amalgamation'.' An amalgamation is essentially the blending of two concerns into one so that in substance they are owned by the same person. Resort must be had to case law for guidance. In this instance any cash payment to the transferring company would preclude the relief from applying. While the legislation itself does not preclude any cash payments to shareholders in the transferring company it is important for the transaction to be regarded as a scheme of reconstruction or amalgamation that the shares be issued pro-rata to existing shareholders. In that regard the Irish courts have recently approved UK case law on the meaning of a reconstruction whereby post transaction, 'substantially the business and the persons interested must be the same'. This would appear to preclude cash payments to minority shareholders although the matter is not free from doubt in light of the fact that the stamp duty and capital duty (abolished) codes anticipate the possible payment of cash in 'reconstructions or amalgamations' (up to 10% of the consideration in the case of stamp duty).	S.631 S.615 Patrick W. Keane & Company Ltd v The Revenue Commissioners, [2007] IEHC 466 S.80, S.119 SDCA 1999 S. 586, S. 584 S.587 S.633C

2.2.2 Share exchanges In order to qualify for the relief under the legislation covering share for share exchanges, the transaction must consist of a paper for paper transaction. The relief applies where the company issuing shares or debentures has or will have control of the other company or the shares are issued as part of a general offer seeking control of the company. A similar relief also applies where there is a scheme or reconstruction or amalgamation involving the issue of shares or debentures to existing shareholders or debenture holders in proportion to their holdings. Where the company issuing shares has or is seeking to obtain control of the target company and shares are issued, the single company reorganisation rules are applied. The Revenue guidance confirms that where the consideration is made up of shares or debentures, and cash, that the cash element is treated as a capital distribution in respect of the shares in the hands of the shareholder of the acquired company The transaction is split into two elements; a share for share element that, provided it qualifies for relief as a share for share exchange in its own right, is covered by the legislation; and a cash sale which is subject to Irish tax in the normal way. The base cost of the share upon which any such gain would be calculated is allocated between the two transactions using normal part disposal rules. No guidance has been issued concerning the impact of cash payments made to existing shareholders. If a branch of activity is transferred to a new company the shareholders in which represent 90% of the shareholders in the existing company (the other 10% shareholders having received cash) it is unclear, following the case law referred to above, if this could be regarded as a reconstruction. In practice reconstructions are often carried out prior to a subsequent disposal of shares with caution usually being exercised to ensure there is no link between the reconstruction and a subsequent sale. 2.2.3 Mergers creating an SE or SCE The creation of an SE or SCE by mergers under Articles 2(1) and 17(2)(a) or (b) of the SE Regulation or Article 2 of the SCE Regulation is deemed to be a reconstruction if certain conditions are met. Therefore, the payment of cash within the limits envisaged by the Directive would not seem to preclude the paper for paper relief from applying to such mergers.	

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger As noted at 1.1 Ireland has not enacted specific legislation to facilitate the cross-border mergers facilitated by the Directive with the exception of a merger that facilitates the creation of an SE or SCE.	N/A.

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares The 'paper for paper' rules generally apply only where the company issuing the shares already has control or will, as a consequence of the exchange, have control. However, where the company issues the shares as a result of a general offer to all members of the target company or any class of them on conditions, which it had been satisfied, would have resulted in the company gaining control of the target company the paper for paper relief may apply. This might apply for example where the issuing company made unconditional a general offer which was previously conditional on it acquiring control of the other company. Thus, the relief can apply to failed take-over bids.	S.586(2)

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
2.5 Consolidation of qualifying holding The relief is subject to the transaction being carried out for bona fide commercial purposes and not part of a scheme or arrangement where the main purpose or one of the main purposes is avoidance of liability to tax.	S586(3)

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
2.6 The term 'branch of activity' A distinction must be made between the Irish/UK concepts of 'Branch' and 'Branch of Activity' and some consideration given to the concept of a trade. A non-resident company is liable to Irish corporation tax only if it carries on a trade in Ireland through a branch or agency. The liability applies to trading profits of the branch or agency, other income from property or rights used by the branch of agency and chargeable gains on the disposal of Irish assets used or held for the purposes of the branch or	S. 4(1)

agency. (a) Branch A branch is a familiar concept in Ireland with many non-Irish organizations having a taxable presence in Ireland through a branch without the need to be incorporated in Ireland. Legislation describes a branch or agency as 'any factorship, agency, receivership, branch or management'. The term 'branch' is not necessarily interchangeable with the term 'permanent establishment' that is used in double taxation agreements. (b) Branch of Activity The concept of 'Branch of Activity' is a less well defined, used and understood concept compared to 'branch', although undeniably, covers a far wider ambit. The concept of a 'business' mirrors the wording in '*Andersen og Jensen*' although this term is, itself not defined in Irish legislation.	S.83
There has been a body of UK case law around what the term 'business' means. In American Leaf Blending v Director General of Inland Revenue in which it was stated that '*in the case of a company incorporated for the purpose of making profits to its shareholders, any gainful use to which it puts any of its assets prima facie amounts to the carrying on of a business*'. This includes trading activities but would also include investment activities. This extension is reflected in legislation whereby an investment company is defined as '*any company whose business consists wholly or mainly of making of investments*'. (c) Concept of a trade Many aspects of Irish legislation, in particular the 1992 amendments implementing the Directive's provisions on the transfer of assets, refer to the concept of a trade. The legislation defines a trade as including, '*every trade, manufacture, adventure or concern in the nature of trade*'. As a definition this is inadequate. As the Revenue guidance notes point out, it is necessary to refer to the extensive body of case law (primarily from the UK) so as to obtain a full picture of what is or is not a trade. In this regard reference is frequently made to the UK report of the Royal Commission on the Taxation of Profits and Income which identified a number of 'badges of trade', i.e. factors to consider when deciding whether or not a particular activity constitutes trading. In view of the fact that a lower rate of corporation tax applies to 'trading income' the Revenue is prepared to give opinions on whether or not particular activities constitute 'trading' and some of these decisions have been published on the Revenue's website. Revenue has also produced some general guidance outlining how Revenue approaches the subject of whether or not a taxpayer is trading. Whether a company is trading or not is a question of fact, to be decided based on a review of the circumstances of each case. The Revenue has indicated that trading 'presupposes activity' and that the company must have the people with the necessary skills and authority to carry on the business activities. In evaluating whether a company is trading the Revenue evaluate; the nature of the trade particularly if the activity might appear to be of an investment or passive nature, the activities and functions carried out at senior level by management and the number of	www.revenue.ie/doc/trade.doc S.637 S.615 S.633

skilled people at management and other levels. If it is accepted that the concept of a trade is narrower than a business or branch of activity then there would appear to be a discrepancy between the implementing measures and the Directive. However, a non-resident company is only liable to Irish corporation tax if it carries on a trade in Ireland through a branch or agency. A non-resident company, not carrying on a trade in Ireland through a branch or agency, could be liable to Irish income tax on certain Irish source income, subject to the application of a relevant double taxation agreement. A non-resident company carrying on such a business activity theoretically could also be liable to Capital Gains Tax on the disposal of certain specified assets, in particular Irish land (except development land for which specific provision for a tax deferral has been made). In this instance, an application might need to be made to the Revenue seeking discretionary relief if the transaction is of a type that should be covered by the Directive, for example a bona fide reconstruction or transfer of assets to another company in consideration for shares. The domestic capital gains tax deferral for transfers of assets under reconstructions and amalgamations applies to the transfer of the whole or part of a company's business rather than simply to the transfer of a trade. However, as the assets being transferred must remain chargeable assets, this effectively means that the assets must be used either by an Irish resident company or for the purpose of an Irish trade carried on by a non-resident company. While there is no reason to suggest that the Revenue would refuse to grant relief in cases clearly covered by the Directive, the discretionary nature of the relief is a less than ideal way of implementing the Directive.	

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> See the analysis at 1.1.	S.4(1), S.5(1), S.616, S.630

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>3.2 Transparent entities</u> The Revenue has not issued any list of foreign entities which it regards as being transparent. It is understood that the preparation of such a list is under consideration. However, the Irish Revenue has issued opinions to taxpayers in response to specific requests for clarification on the application of particular elements of Irish tax law to specific foreign entities. Although these opinions are not published some information on	

these opinions may be available under the Irish Freedom of Information Act. From experience, many of the factors outlined in 3.2 of the UK response are likely to be considered relevant by the Irish authorities also.	

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency	
3.3.1 Irish Law	S.23A
Companies can be tax resident in Ireland either (a) by incorporation in Ireland, or (b) if they are incorporated outside Ireland, if 'central management and control' is located in Ireland.	
Central management and control is a matter of judgment which depends on the particular facts of each case. However, the case law (primarily from the UK) has established that the most important factor when determining where a company is managed and controlled is the answer to the question of where the meetings of directors who control the company take place.	S.23B S.23A
Where a company is regarded for the purpose of any double taxation agreement as resident outside Ireland and not in Ireland it is to be so treated for domestic law purposes also.	
An SE or an SCE which has its registered office in Ireland is regarded as resident in Ireland unless it is not resident by virtue of a double taxation agreement.	
A 'relevant company' that is incorporated in Ireland is not resident in Ireland if it carries on a trade in Ireland or is related to a company which carries on a trade in Ireland. A relevant company is a company which is (a) under the direct or indirect control of a person resident in an EU Member State or a territory with the government of which a tax treaty has been entered into (without being under the direct or indirect control of a person or persons not so resident), or (b) which is, or is related to, a company, the principal class of the shares of which is substantially and regularly traded on one or more recognized stock exchanges in an EU Member State or territory with the government of which a tax treaty has been entered into.	
3.2.2 Double Tax Treaties	
Where a company could be regarded as being tax resident in both Ireland and another country, then, where a double taxation agreement is in place	

between Ireland and that other tax authority, the most common tie breaker is to determine where the place of effective management is located.	

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject-to-tax clause 3.4.1 Transfers of assets The 1992 provisions implementing the Directive's provisions on the transfer of assets apply the Directive's definition of 'company from a Member State'. Both the intra-group transfer provisions and the relief for transfers of assets on a 'reconstruction' or 'amalgamation' apply only where the transferring company and the receiving company are Irish resident and/or the assets are chargeable assets, immediately before or after the transfer. In effect this means that a transferring or receiving company must be liable to Irish corporation tax, one of the taxes listed in Article 3(c) of the Directive. 3.4.2 Share for share exchanges There is no specific requirement that, for a share for share exchange to qualify for the relief, either of the companies must be subject to tax. No administrative guidance has been issued on the 'subject to tax' point.	S.631, S.632, S.630 (definitions)

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
3.5 Shareholder requirements The benefits of the Directive are not restricted due to the identity of the owner of the company.	N/A.

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>4.1 The concepts of 'real values' and 'value for tax purposes'</u> <u>4.1.1 General Points</u> Before responding to this point, it is interesting to note that, in Irish legislation, like the UK, the term 'capital gains' has a specific meaning inasmuch as it refers specifically to the taxation of gains and losses on the disposal of certain assets. However, it has been assumed that for the purposes of this review, the term 'Capital Gains' refers to tax on the transfer of all assets within a company or branch included as part of a merger, division or partial division. It should also be noted that the Irish authorities, in implementing the Directive, have taken advantage of the derogation in Articles 10(2) (permanent establishment in a third Member State) and Article 10a (transparent entities). Hence the analysis below refers to mergers, divisions and partial divisions between opaque companies where there remains a presence in Ireland after the transaction through a branch continuing to be located in Ireland. <u>4.1.2 Real Values and Values for Tax purposes</u> Capital gains are calculated by deducting from the sales proceeds the cost of an asset and incidental costs of disposal. The base cost of the asset may be subject to an indexation factor if the asset was acquired prior to 2003. Transactions between connected parties or not made at 'arm's length' are deemed to take place at market value unless there is a specific relief to the contrary (for example for intra-group transactions). Within each of the following sections, the concepts of 'real value' and 'value for tax purposes' have not been directly defined. Instead the rules have sought to apply the Directive by defining the gain or loss that arises on such a transfer. It can be argued that by using this approach, the concepts of 'real value' and 'value for tax purposes' have been implicitly defined as, in the absence of the Directive gains or losses would be calculated with reference to these terms. Irish legislation does not specify how to calculate 'real values'. The concept applies to each individual transaction as being what a third party purchaser would buy the assets at if it were taking part in an arms length transaction under the same or similar circumstances to the one that actually took place. <u>4.1.3 Transfers of Assets</u> As noted in 1.1 Ireland has not implemented specific rules for Merger, Divisions or Partial Divisions.	S.615, S.617, S631, S.632, S.633, S.633A S.631(2), S.400

All the measures providing for the deferral of taxation on chargeable gains on transfers of assets operate in a similar manner. Where the provisions apply, the transfer or assets from transferring company to receiving company is deemed to take place at a value that would generate neither a gain nor a loss on transfer. The value of the deemed transfer is calculated by reference to the cost of the relevant asset (the 'base cost') without any reference to indexation (an allowance to reflect the time value of money that applied up to 31 December 2002 under general capital gains principles). It would appear that this is compliant with the Directive. 4.1.4 Capital allowances Tax depreciation (capital allowances) is available in respect of capital expenditure incurred on certain assets, primarily plant or machinery and industrial buildings (as defined). The rates of depreciation vary depending on the nature of the asset and when it was acquired. Where plant or machinery is disposed of for a sum in excess of its tax written down value there will generally be a recapture of some or all of the capital allowances granted (a 'balancing charge'). If the sum received for the asset is less than its tax written down value a balancing allowance could arise. Industrial buildings balancing charges and allowances can arise where an industrial building is disposed of during its tax life. The tax life will vary based on the nature of the asset and when it was acquired. The transfer of assets qualifying for capital allowances will be deemed to be carried out at a value that does not give rise to any balancing allowance or charge. This relief may be available under the 1992 provisions implementing the Directive or under other domestic legislation that applies where there is a reconstruction without a change in ownership. 4.1.5 Other items Only disposals of assets can result in chargeable gains or allowable capital losses. The disposal of capital liabilities is a tax 'nothing' with no tax consequences.	

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions No specific guidance has been issued in respect of divisions or partial divisions.	N/A.

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' 4.3.1 Effectively connected There is no specific definition of 'effectively connected' within Irish legislation. No guidance has been issued by Revenue on this aspect. 4.3.2 Permanent Establishment The term 'permanent establishment' is not defined in Irish legislation except for the purposes of implementing the Interest and Royalties Directive 2003/49/EC. The term 'permanent establishment' is defined in double tax treaties that Ireland has entered into. While the definitions in the agreements include branches they also include other establishments such as offices, mines, factories and construction sites. Ireland interprets this part of the Directive by linking it to the transfer of assets used for the purpose of the narrower concept of a trade carried on by the receiving company in the State and the assets remaining chargeable assets. In order to constitute chargeable assets the assets must be used in or for the purposes of a trade carried on by a non-resident company through a branch or agency. The Irish High Court decision in '*Murphy v Dataproducts*' (Dublin) Ltd (1988) provides some guidance as to when assets are used by or for a branch, a key requirement to establish Irish taxing rights. In that case an Irish incorporated company resident in the Netherlands controlled a Swiss bank account. While the *money's withdrawn* were used by the company only for the Irish branch this was differentiated from 'use by the Irish branch'. The management of the Irish branch had no power to make any decision in relation to the account, the account was established by resolutions in the Netherlands and the money therein was available for any intra-vires purpose of the company.	S.631, S.632, S.615, S.617 S.25, S.29

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief As noted above, there is no specific legislation addressing mergers, divisions or partial divisions. In practice partial divisions may be effected using a reconstruction relief. This relief has no clawback provision presumably on the basis that the successor activities will remain within the charge to Irish tax.	

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment The relief is only available where the assets continue to be used for the purpose of a trade carried on by the receiving company in Ireland. Otherwise it will be subject to the normal rules on transfers of assets between companies. In general terms the transfer will be deemed to take place at the market value of the item being transferred on the date of the transfer, with profits and losses calculated accordingly.	S.615, S.617

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company Under Irish law, 'merger profits' do not arise. If the transaction is one that qualifies for relief the receiving company will likely be treated as inheriting the tax attributes of the assets being transferred. For example, the only specific references to Mergers in the Irish implementing measures are the provisions applying to the formation of an SE or SCE by merger. Where chargeable assets are left in Ireland following a merger to form an SE or SCE the transfer is treated as having been made at no gain/ no loss.	S.633A

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral There have been no specific amendments to the Irish tax code subsequent to the decision of the ECJ in the 'N' case. However, the migration of an Irish company's tax residence to an EU Member State would not necessarily trigger an exit charge. See 9.3 for more details.	N/A.

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
<u>4.8 Criteria to determine tax transparent entities</u> See 3.2.above. No guidance has been published to date as to the treatment of particular entities.	N/A.

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
<u>4.9 Further conditions for tax relief</u> As indicated at 1.1 Ireland has not implemented specific measures referring to mergers, divisions or partial divisions. Relief for these types of transactions, if not already available under other domestic provisions, may be available on application to the Revenue. Relief may be given on a 'just and reasonable' basis. The legislation providing for this discretionary relief does not contain any conditions other than the transaction must be of a type specified in the Directive for which specific relief (e.g. for a transfer of assets) has not already been provided for. All relief under the Directive, i.e. as respect a transfer or disposal of assets of the formation of an SE or SCE by merger, is only available if the transaction is effected for bona fide commercial reasons and does not form part of any arrangement or scheme of which the main purpose or one of the main purposes is avoidance of a liability to income tax, corporation tax or capital gains tax. A similar 'bona fide' test is contained in the paper for paper relief provisions.	S. 635

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>5.1 The term 'provisions and reserves'</u> There is no specific definition of the term in Irish tax legislation. <u>5.1.1 General Point</u> Under general Irish tax law, assets and liabilities of a business or trade (as applicable) can be transferred from one company to another under legislation specifically covering such transfers. However, no such law covers transfers of provisions, reserves or losses. The general approach is that such items belong to the legal entity in which they arise and, unless	S.400

specific rules state otherwise, they cannot be transferred from entity to entity. Therefore, in the situation where a branch is transferred between two legal entities, regardless of the method by which this happens, brought forward losses remain in the transferring company.. By way of exception, where the transferring company held more than 75% of the share capital of the receiving company after the transfer took place, any losses that are attached to a trade being transferred are retained by the receiving company for use against the future profits of that trade.	

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments These concepts do not arise in Ireland so there is no need to distinguish between provisions and reserves derived from various permanent establishments.	N/A.

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves See 5.2 above.	N/A.

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves There are no specific rules to cover this situation. None are required.	N/A.

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry-over of losses 6.1.1 Meaning of 'loss' The concept of 'loss' has not been specifically defined for the purpose of implementing the Directive. Therefore first principles must be used to determine the meaning of a loss. In general terms, in Ireland profits and losses are streamed with respect to the nature of the activity that generated them and a loss is deemed to arise when the expenses or debits arising in respect of one of those types of income exceeds the related income or credits. For any given classification of loss, the company or permanent establishment has a number of choices with respect to how it can apply those losses against profits arising in that entity either in that period or in other periods, or against profits arising in other companies provided that they qualify under Ireland's group relief rules. A corporation tax group for loss relief purposes consists of a parent company and its 75% (direct or indirect) subsidiaries. A company resident anywhere in the EEA (except Liechtenstein) may surrender losses in respect of its Irish trading branch to other group companies that are within the charge to Irish corporation tax. Group relief is also available to consortium members where a loss making company is owned by a consortium. Ireland taxes most types of trading income at a rate of 12.5% while non-trading income is subject to corporation tax at 25%. Certain activities, e.g. petroleum trades or dealing in development land are liable to corporation tax at 25%. For this reason there are restrictions in place to prevent losses from a 12.5% activity being used to shelter profits liable at 25% on a euro for euro basis. Instead relief is given for such losses by way of a tax credit equal to 12.5% of the value of the losses (or 10% if the company qualifies for manufacturing relief, i.e. the 10% effective rate on manufacturing activities which exists until 2010). 6.1.2 Options available in respect of losses With the exception of capital gains and capital losses, the choices available to a permanent establishment (in an Irish context – a trading branch) with respect to losses of a specific character arising in a particular period are as follows: If the branch is carrying on a 12.5% trade (normally so): (a) offset against other trading income or foreign dividends taxable at 12.5% arising in the period;	S.396A S.396A S.420A S.396B S.396B S.420B S396(1) S.396(2) S.396(2) S.420 S.396(1) S.400

(b) carry back one year against 12.5% income arising in the previous period; (c) group relief against 12.5% income arising in other 'group' entities; (d) use to offset against relevant corporation tax in the period on a 'value basis'; (e) carry back against relevant corporation tax for the previous period on a 'value basis'; (f) group relief against relevant corporation tax payable by other 'group' entities on a value basis; (g) carry forward indefinitely for offset against future income of the same trade. If the branch is carrying on a 25% trade (certain specified activities) (h) use to offset against total profits (income and gains) arising in the period; (i) carry back one year against total profits (income and gains) arising in the previous period; (j) group relief against total profits (income and gains) arising in other 'group' entities; (k) carry forward indefinitely for offset against future income of the same trade. However, losses are not transferred to the receiving company on the transfer of a trade (or part of a trade) from one company to another except where the transferring company owned 75% of the ordinary share capital of the receiving company, or where the same shareholder owns 75% of the shares of both the transferring and receiving companies, either directly or indirectly at some point in the two years after the transfer.	

What method is applied to allocate losses to the permanent establishment?	Reference
<u>6.2 Allocation of losses to the permanent establishment</u> No specific rules are outlined for the allocation of losses to the permanent establishment (Irish branch). In a domestic context reference is made to 'any necessary apportionment … of receipts or expenses'. Thus presumably the profits and losses of the trading activities of the Irish branch would be calculated as if it was a separate enterprise trading on its own account.	S.400(12)

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets No specific reference is made in Irish legislation to divisions, partial divisions or transfer of assets in the context of preservation of losses under the Directive. The rules in 6.1.2 apply to any succession to a trade or part of a trade.	N/A.

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses As noted above, loss transfers are not permitted on transfers of trades from one legal entity to another (irrespective of the method used) unless the transferring company owns 75% of the equity of the receiving company, or the same shareholder owns 75% of the shares of both the transferring and receiving companies (direct or indirect) at some point in the two years following the transaction. Ireland does not discriminate between transactions in a wholly domestic context and cross-border transactions as the same rules apply equally to both situations.	S.400

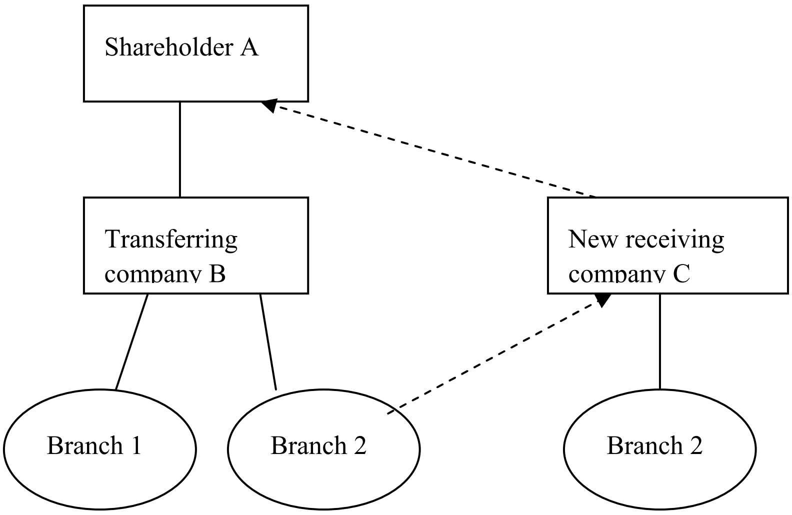
Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Amended holding threshold The Irish tax code does not refer to share cancellations (except in the context of paper for paper relief, i.e. exchanges of securities) or to the derogation permitted above for the reasons explained in the introduction to this report. Where a receiving company holds shares in a transferring company that is being dissolved (so there is no exchange of shares) an application would need to be made to Revenue seeking (discretionary) relief from any gain arising on the disposal (i.e. cancellation) of the shares. Given that Ireland has now implemented the 10th Company Law Directive specific provision for the cancellation of shares outside the context of exchanges of securities would now seem to be required if the discretionary alternative is considered inadequate.	S.587, S.633C

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses As noted above, in the context of mergers, there is no specific Irish legislation directed at cancellations of holdings.	S.587(2), S.633C(2) (applies S.587 to SE/ SCE mergers)

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder 8.1.1 Share for Share exchanges Where a shareholder exchanges their shares in one company for shares in another, and the conditions for relief under the paper for paper exchange rules are met, then the newly received shares are treated as having the same tax attributes as the shares previously held. Economic double taxation on the shares transferred to the acquiring company may be avoided on the assumption that the shares transferred will be deemed to be received by the acquiring company at their market value. If the exchange takes place between two group companies, this may not be the case if the decisions in the UK cases of '*Westcott v Woolcombers Ltd*' [1987] STC 600 and '*NAP Holdings UK Ltd v Whittles*' [1994] STC 979, determining that the intra-group transfer provisions took priority, are applied by the Irish Courts. Unlike the UK, Ireland did not introduce specific legislation to take account of this decision. A group for corporation tax on chargeable gains purposes consists of a principal company, its effective 75% subsidiaries and any 75% subsidiaries of those subsidiaries. To be a member of a group a company must be resident in an EEA Member State (except Liechtenstein). Economic double taxation may also be avoided if the disposal of the acquired company would qualify for the exemption available for disposals of certain trading companies. However, this exemption is not available if the shares in the acquired company derive the greater part of their value from land or mineral rights in Ireland. The exemption applies to disposals of shares in a company resident in the EU or in a territory with which Ireland has entered into a double taxation agreement provided at least 5% of the company's ordinary share capital, profits available for distribution to equity holders and assets available on a winding up to equity holders, has been held for a period of 12 months in	S.587 S.616 S.626B

the 3 years prior to the disposal. The trading requirement can be met by the acquired company carrying on a trade or by virtue of the business of the acquiring company, its acquired company and any other '5 per cent' investee companies, taken as a whole, consisting wholly or mainly of the carrying on of a trade or trades.	
8.1.2 Partial Divisions	S.615
	
Securities issued under a partial division may qualify under the paper for paper relief provisions and be treated as if they formed part of the original shareholding in the transferring company. Where the whole or part of a business is transferred (for example a branch) to a new company in exchange for the issue of shares to the shareholder in the transferring company this 'partial division' may be regarded as a reconstruction. Where the reconstruction relief applies, the receiving company will inherit the same tax basis that the transferring company had and will be treated as acquiring the assets at the same time as the transferring company. In this instance there is no market value step up for the receiving company. Whether or not this results in economic double taxation depends on a number of factors. As noted above under Irish law many disposals of shares by companies (not individuals) are exempt under Ireland's substantial shareholding exemption. Where the exemption is available no tax would be due on the subsequent disposal of shares in the receiving company by a corporate shareholder. However, the subsequent disposal of underlying branch assets would generally be subject to tax in full. Any economic double taxation arising in this example would not appear to arise out as a result of the reconstruction but rather it already existed under the original structure. The receipt of shares in the receiving company by shareholders in the transferring company in consideration for the transfer of part of the	

transferring company's business may technically constitute an income distribution under Irish law. There is a Revenue practice not to seek to apply this charge in commercially driven reconstructions. It would seem that the Directive would require this 'concession' to be applied to transactions covered by the Directive, in particular 'partial divisions', which are widely defined. 8.1.3 Mergers and Divisions As noted in 1.1 no specific provision is made in the Irish tax code for mergers and divisions exception in connection with the formation of an SE or SCE by merger. The comments at 8.1.2 would apply.	

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
8.2 Computation of the capital gain 8.2.1. Share for share exchanges Cash receipts are treated as though a disposal of the securities in question had taken place under normal capital gains rules (see section 2.2. above) 8.2.2 Mergers, divisions and partial divisions The only specific reference to mergers in the Irish tax code relates to a merger of two or more companies to form an SE or SCE. The rules for share for share exchanges apply. In order for the 'reconstruction' or 'amalgamation' relief on the transfer of assets to apply to partial divisions the transferring company must receive no consideration other than the receiving company taking over the whole or part of the liabilities of the business being transferred. As noted in 2.2 the Revenue has not indicated if it would allow relief to be given in respect of transactions where some cash (e.g. equal to or less than 10% of the value of the assets being transferred) is given to shareholders of the transferring company.	S.587 S.615

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
8.3 Further conditions for tax relief The share for share provisions contain a requirement that the transaction must have been for bona fide commercial reasons and did not have tax avoidance as a main purpose or one of the main purposes.	

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>9.1 Avoidance of economic double taxation at the level of the transferring company</u> Where a company transfers a trade or part thereof to a receiving company in exchange for the issue of shares, the receiving company effectively stands in the shoes of the transferring company. Any subsequent disposal by the receiving company of the trading branch assets may result in chargeable gains depending on the nature of these assets. Economic double taxation at the level of the transferring company may be avoided if the shares issued by the receiving company are considered to be received by the transferring company at the market value of the assets exchanged. Furthermore, as noted at 8.1.1 above under Irish law many gains arising on disposals of shares <u>by companies</u> (not individuals) are exempt under Ireland's substantial shareholding exemption. Where the exemption is available no tax would be due on the subsequent disposal of the receiving company shares by the transferring company. The provisions implementing the Directive provide that where a transferring company receives shares in consideration for the transfer of assets and it disposes of those shares within 6 years of the date of transfer the aggregate of the chargeable gains deferred is deducted from the allowable base cost in computing the gain on the disposal of the shares. This 6-year clawback period is not provided for in the Directive. However, this legislation predates the introduction of the exemption referred to above and would seem to have no practical impact where that relief is available.	S.631(3), S.617 S.626B S.631(4)

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>9.2 Further conditions for tax relief</u> The transaction must have been for bona fide commercial purposes and not have a tax avoidance motive.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>9.3 Tax deferral</u> See 4.7. Irish law has not been amended to take account of the 'N' case. The tax deferral for intra-group asset transfers is subject to a claw-back mechanism that deems a transferee company leaving a corporate group with the asset that it received under the intra-group transfer provisions as having at the time of its acquisition sold the asset for its market value and reacquired it. The provision applies (subject to exceptions) where the transferee leaves the group within 10 years of its acquisition of the asset. However, this claw-back provision does not apply to companies leaving groups as a result of bona fide commercial mergers. Furthermore as EU resident companies can be members of an Irish group, EU resident companies can be interposed into corporate structures without jeopardizing the deferral of any gains under the group relief provisions. The Irish corporate tax system contains an exit charge that can apply where companies cease to be resident in Ireland. It does not apply to companies that are 90% owned by certain foreign companies (e.g. companies controlled by residents of treaty partner States, effectively including all Member States except Malta). Also the exit charge does not apply to any assets which immediately after the transfer are situated in Ireland and are used or held for the purposes of a branch or agency carried on in Ireland by the company.	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Loss recapture for permanent establishments in third Member States</u> Ireland does not provide for loss recapture as envisaged in Article 10(1) as it applies the derogation available in Article 10(2) in respect of the transfer.	S.634, S.633B

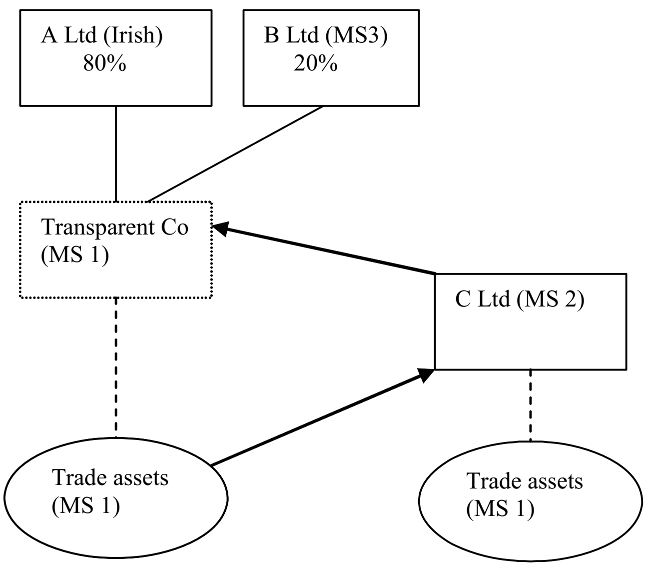
Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
10.2 Permanent establishment in the Member State of the receiving company Ireland avails of the derogation in Article 10(2).	N/A.

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
10.3 Concept of worldwide taxation/tax credit system Ireland has availed of the derogation in Article 10(2) and may tax unrealized capital gains. The specific rules for giving credit for tax that would have been payable except for the Directive are contained in Section 634 TCA97 and apply where: (a) a company resident in Ireland transfers the whole or part of a trade which immediately before the transfer was carried on in a Member State (other than Ireland) though a branch or agency to a company not resident in Ireland; (b) the transfer included the whole of the assets of the transferring company used for the purposes of the trade or the part of the trade (or the whole of those assets excluding cash); and (c) the consideration for the transfer consists wholly or partly of the issue to the transferring company of securities in the receiving company. The provision also applies where there is a formation of an SE or SCE by way of a merger without leaving assets in Ireland. In this instance the conditions are: (a) an SE is formed by the merger of 2 or more companies in accordance with Articles 2(1) and 17(2)(a) or (b) of the SE Regulation, or (b) an SCE is formed by a merger in accordance with Article 2 of the SCE Regulation, and (a) each merging company is resident for the purposes of tax in a Member State,	S.634 S.633B

(b) the merging companies are not all resident for the purposes of tax in the same Member State, (c) the merger is effected by the transfer by an Irish resident company to another EU resident company all assets and liabilities of a trade which the Irish resident company carried on in another Member State through a branch or agency, and (d) the aggregate of the chargeable gains accruing on the transfer exceeds the aggregate of any allowable losses accruing. The relief is best illustrated by an example. An Irish company has a French permanent establishment. It wishes to merge with an Italian company to form an Italian SE. Section 633B TCA97 applies. The aggregate chargeable gains on the disposal of the French PE will be liable to Irish corporation tax. However, Ireland will take account of any French tax that would have been imposed by the French authorities were it not for the application of the Directive and/or French domestic law providing for a deferral. In order to benefit from a credit for this notional tax, a certificate from the French tax authorities (the Member State in which the trade was carried on) is required. This certificate must state (a) whether gains accruing to the Irish company would have been chargeable to French tax but for the provisions of French law and/or the Directive deferring the charge to tax; and (b) if so, the amount of tax that would have been payable on the assumption that any losses arising on the transfer could be offset against any gains arising and all deductions and reliefs available were claimed.	

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
<u>10.4 Tax deferral</u> No amendments to S. 634 TCA97 were made to take account of ECJ case law. Ireland has followed the wording of the Directive closely in implementing the provisions of the Article 10(2) derogation. Therefore, the points raised by the N case with respect to how a Member State can seek to restrict the freedom of establishment of a person by imposing a form of exit taxation upon them are not addressed.	N/A.

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies Ireland has chosen to adopt Article 10a. This was achieved by adapting in 2006 the tax credit provisions of S.634 TCA97 as they apply to transfers of assets as follows: (a) where a non-resident company transfers the whole or part of a trade to another company and the consideration consists solely of the issue to the transferring company of securities in the receiving company, and (b) for the purpose of computing the income or gains of any person who is chargeable to Irish tax, income or gains of the transferring company are treated as being income or chargeable gains of that person and not of the transferring company, (c) then, in computing the liability of the person liable to Irish tax in respect of the transfer, an appropriate part of the tax specified in a certificate given by the tax authorities of the Member State in which the trade was carried is to be credited against any Irish tax due. The required certificate from a tax authority of a Member State is the same certificate referred to above at 10.3. The position may best be illustrated by example.  In this instance, Ireland regards Transparent Co as fiscally transparent while MS 1 does not. If the trade assets were transferred to C Ltd in return for the issue of shares to Transparent Co how might Ireland treat	S.634

the transaction? Ireland would regard A Ltd as having disposed of the trade assets in MS1 to C Ltd and absent any relieving provisions would assess A Ltd to Corporation Tax on 80% of any chargeable gain arising. However, the transaction is covered by the Mergers Directive and MS1 should apply a local equivalent of Section 615 TCA97 or Section 631 TCA97 to ensure that no gain arises at the time of the disposal of the trade assets to MS2. Section 634 TCA97 (as amended) will then operate to ensure that Ireland grants the appropriate credit to A Ltd, this being 80% of the tax that would have been payable in MS1 had the benefit of the Merger Directive (or indeed a domestic equivalent) not applied. As B is carrying on a trade in Ireland through a branch or agency, B will be liable to Irish corporation tax on its share of the gain. However, as B is within the charge to Irish tax, the same relief that is available to A will also be available to B. If the trade assets had been located in MS2, section 634 would operate so as to provide a tax credit based on a certificate issued by MS2 and not MS1. If MS1 had imposed a charge in that instance it would have been obliged to have itself taken account of a certificate issued by MS2 so the reference in section 634 to the Member State in which the trade is located seems reasonable. The amendment to section 634 introduced by the 2006 Finance Act refers only to a transfer of a trade or part of a trade. Presumably exchanges of shares etc. are covered adequately by the provisions of section 587, but if not, the ability to make a claim under section 637 TCA97 (transactions referred to in the Directive but not covered in Part 21 TCA97) should be noted. No specific reference has been made to Mergers, Divisions, Partial Divisions or Exchange of Shares involving transparent entities.	

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit S. 634 TCA97 focuses exclusively on transparent transferring companies and makes no reference to transparent acquired companies.	S.634

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit No specific reference is made in Irish tax legislation to transparent acquired companies.	N/A.

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders No specific references are made in Irish tax legislation to the provisions of either Article 10a(3) or 10a(4).	N/A.

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company This element of the Article does not appear to have been transcribed into Irish law.	N/A.

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation Under pre-existing Irish legislation, this relief already existed. S.627 TCA97 states that, in the event of an Irish resident company (including an SE) ceasing to be tax resident in Ireland, then an exit charge arises on a deemed disposal of all of the assets of the company at market	S.627

value. However, as noted at 9.3 above, an exception to the general rule exists where those assets continue to be used in a trade carried on through a branch or agency in Ireland after the company has ceased to be Irish tax resident. Therefore provided the SE continues to operate an Irish trade through a branch or agency after the movement of its tax residence (see below how that coincides with movements of its head office) then there should be no immediate exit tax in respect of any assets used in carrying on a trade in Ireland through a branch or agency. This provides the relief required in this Article.	

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' The term 'head office' has not been used in the national legislation implementing Article 10b.	S.23B

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency See 3.3 for the criteria used to determine tax residence of a company. The transfer of a registered office may not be sufficient to trigger a change in corporate tax residence. While the transfer of a registered office might result in a transfer of management and control the two events will usually not happen contemporaneously. The transfer of management and control may take a little bit longer than the relatively straightforward transfer of a registered office. An SE or SCE with its registered office in Ireland is regarded as tax resident in Ireland subject to the application of any other rule that disapplies tax residence, for example, the application of a double taxation agreement tiebreaker clause. An SE or SCE which transfers its registered office out of Ireland does not cease to be tax resident in Ireland by virtue only of that transfer. Reference will need to be made to applicable tax treaties (if available – for example Ireland has not yet entered into a double taxation agreement with Malta).	S.23B, S.23A

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>10b.4 Assets and liabilities not effectively connected with a permanent establishment</u> On the assumption that the transfer of the registered office also results in a transfer of tax residence, the exit charge provisions may apply to assets unconnected with a branch or agency retained in Ireland. However as indicated at 9.3 the cessation of tax residence does not automatically trigger an immediate exit charge as factors such as the ownership of the company will also need to be considered.	S.627

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
<u>10b.5 Tax deferral</u> No specific account has been taken of ECJ case law. See 9.3 above.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
<u>10c.1 The term 'comparable circumstances'</u> The term 'comparable circumstances' has not been specifically defined for the purpose of implementing the Directive. However, the concept is incorporated in Irish legislation by the wording of the rules in respect of the use of losses carried forward. S.396(1) TCA97 states that where a company carrying on a trade incurs a loss the company can claim to deduct those losses against trading income from the same trade in succeeding accounting periods. The carry-forward rule applies equally to Irish resident companies and to non-resident companies carrying on a trade through a branch or agency in Ireland. Therefore, provided the SE is still within the charge to Irish tax, losses are preserved in Ireland in the event that it becomes non-Irish resident, provided: (a) it carries on the trade in Ireland through a branch or agency; and (b) losses are not deemed to be extinguished under rules that operate in the event of a change in the nature or conduct of a business	S.396(1) S.401

within three years, either before of after, a change in ownership of the SE. This rule is a general rule under Irish law and not specifically designed to implement the Directive.	

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Loss recapture for permanent establishments No provision is made for the recapture of losses attributable to permanent establishments in third Member States. If these losses are considered to have arisen from a single worldwide trade carried on by the SE prior to the transfer of its registered office, the losses would appear to be available for carry forward against the future income of that same trade even though only the Irish branch remains liable to Irish corporation tax.	S.396(1)

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
10d.1 Deemed liquidation Provided there are no changes to the share capital of the SE, the change of registered office of the SE would not, of itself, trigger any deemed liquidation or distribution of assets within it.	

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
10d.2 Tax treatment of third country residents See 10d.1 above.	N/A.

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> Article 11a has been implemented by, in each instance where relief is available under the implementing legislation in respect of the Directive, making the relief dependent upon the related transaction being carried out for bona fide commercial purposes and not for one where tax avoidance was the main purpose or one of the main purposes. A similar anti-abuse provision is contained in general paper for paper provisions. In Ireland, like the UK, there is a fundamental difference between 'avoidance' and 'evasion'. Whereas 'avoidance' implies that the taxpayer has taken advantage of an aspect of the legislation to reduce their tax burden, 'evasion' implies that the taxpayer has used illegal or fraudulent means to reduce their tax burden. The doctrine of 'wholly artificial'; as described in '*Cadbury*' has not been specifically transcribed into Irish law governing the Directive.	

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
<u>11.2 General anti-abuse provision</u> Article 11(1)(a) has been incorporated into Irish law. Ireland also has a General anti-avoidance rule (GAAR). See 11.3.	Section 811, 811A

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the '*Cadbury*' judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
<u>11.3 The concept of 'wholly artificial arrangement'</u> Ireland has made no attempt to amend its legislation post 'Cadbury'.	S.811, S811A

Ireland has a general anti-avoidance rule that permits the Revenue to reclassify what is regarded as tax avoidance transactions so as to remove the tax advantages obtained. A tax avoidance transaction arises where the Revenue forms the view that a transaction gives rise to a tax advantage (widely defined) and the transaction was not undertaken or arranged primarily for purposes other than to give rise to the tax advantage. A transaction is not a tax avoidance transaction if the Revenue is satisfied that the transaction was undertaken with a view to the realization of business profits and not undertaken or arranged primarily to give rise to a tax advantage. Any transaction undertaken or arranged for the purpose of obtaining the benefit of any relief, allowance or other abatement provided for in the tax code will not be a tax avoidance transaction provided the transaction would not result in a misuse or abuse of the relieving provision.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
<u>11.4 Specific anti-abuse provisions</u> As noted at 9.1 the 1992 provisions implementing the Directive's requirements on the transfer of assets provide that where a company receives shares in consideration for the transfer of assets and it disposes of the shares within 6 years of the date of transfer the aggregate of the chargeable gains deferred is deducted from the allowable base cost in computing the gain on the disposal of the shares. If the transferring company is non-resident this may not represent a tax cost unless the shares are unquoted shares deriving their value of the greater part of their value from land in Ireland. It may also not represent a tax cost if the disposal of the shares would qualify for the corporate tax exemption for gains on the disposal of certain shares.	S.631(4) S.626B

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
<u>11.5 The concept of 'valid commercial reasons'</u> The concept of 'valid commercial reasons' has been implemented by way of the 'bona fide commercial reasons' test outlined at 11.1.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof The provisions implementing the Directive are stated not to apply unless it is shown that the relevant transaction is effected for bona fide commercial reasons. This puts the onus of proof on the taxpayer.	

ITALY

Abbreviations

English	Italian	English	Italian
Decree	Decreto	Legislative Decree No. 544 of December 30, 1992	Decreto Legislativo N. 544 del 30 Dicembre 1992
Delegation Law	Legge Delega	Law No. 142 of February 19, 1992	Legge Delega N. 142 del 19 Febbraio 1992
ITC	TUIR	Italian Tax Code	Testo Unico delle Imposte sui Redditi
CIT	IRES	Corporate Income Tax	Imposta sui Redditi delle Società
IT	IRE	Income Tax	Imposta sui Redditi
RTPA	IRAP	Regional Tax on Productive Activities	Imposta Regionale sulle Attività Produttive
MD	DFT	Merger Directive	Direttiva sulle Fusioni Transfrontaliere
IMD	DIFT	Italian Merger Directive	Direttiva Italiana sulle Fusioni Transfrontaliere
ICC	CC	Italian Civil Code	Codice Civile
SE	SE	European Company	Società Europea
SCE	SCE	European Cooperative Society	Società Cooperativa Europea
EU	UE	European Union	Unione Europea
DTC	TCDI	Double Tax Treaties	Trattati Contro le Doppie Imposizioni
OECD	OCSE	Organization for Economic Co-operation and Development	Organizzazione per la Co-operazione e lo Sviluppo Economico
OIC	OIC	Italian Accounting Organization	Organismo Italiano di Contabilità
PE	SO	Permanent Establishment	Stabile Organizzazione

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
<u>Overall state of implementation</u> The original 1990 Mergers Directive was implemented in Italy through the Legislative Decree No. 544 of December 30, 1992. Such Legislative Decree was implemented by the Italian Government on the basis of Article 34 of Law No. 142 of February 19, 1992. The Delegation Law provided for the implementation of a tax regime applicable to intra-Community corporate reorganizations since the domestic tax regime applicable to corporate reorganizations was already in place at that time. Subsequently, the 1995 Budget Law has modified such domestic tax regime by harmonizing the latter with the tax regime applicable to intra-Community corporate reorganizations. Subsequently, the above mentioned tax rules were inserted in the ITC through the Legislative Decree No. 344 of December 12, 2003. The new Articles introduced in the ITC were substantially similar to the original Decree: only minor wording changes were made. The 2006 European Council amendments to the Directive were introduced in the ITC through the Legislative Decree No. 199 of November 6, 2007. The amendments were retroactively applicable to all intra-Community reorganizations which had taken place from January 1, 2007. Please note that the Italian intra-Community reorganization rules are applicable also to SEs and SCEs without any specific amendment been made since the Technical Explanation to the Decree No. 199 stated that 'SEs were already included in the tax regime applicable to intra-Community reorganizations since they were already subject to the same tax provisions applicable to Italian companies'. The Merger Directive has not had a vast application in Italy, but for the share for share exchange, due to a lack of a legal background for international mergers and divisions. Please note that effective January 1, 2008, companies resulting from mergers, divisions and contribution of assets can align the tax values of the transferred assets (including goodwill) to their book value by paying a substitute tax ranging between 12% and 16%. From a transferor perspective, the reorganization shall remain tax neutral. Such election can be made also with respect to the differences between book and tax values as at December 31, 2007 related to prior years reorganizations.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> The term 'in which companies from two or more Member States are involved' has been interpreted as comprising only the companies directly involved in the transaction and not the parent companies. However, a	Article 178, 179, 180 and 181 of the ITC

derogation to such principle is set forth in rules governing the exchange of shares. Accordingly, the requirements set forth in the Directive should be satisfied only in relation to the following entities: (a) Mergers: the merged companies and the company resulting from the merger. (b) Divisions/partial divisions: the dissolving company and the companies resulting from the division. (c) Transfer of assets: the transferring company and the receiving company. (d) Exchange of shares: based on the literal interpretation of the tax law, the exchange of shares follows under the provision of the Italian Merger Directive only if at least one of the shareholders involved is resident in Italy or the exchanged shares are held by a qualifying EU company through an Italian permanent establishment. (e) Such provision may violate the principles of the Merger Directive. Different positions have been taken by authors in relation to such requirement. Some authors have interpreted the above mentioned provision as restricting the application of the Italian Merger Directive in a manner not in line with the purpose of the Merger Directive. Some others have interpreted such provision as a mere clarification that the Italian Merger Directive does apply in cases where only one of the shareholders involved is resident in Italy or even when the exchanged shares are held by a qualifying EU company through an Italian permanent establishment. The companies involved in the transaction should satisfy the following requirements set forth in the ITC: (a) Take one of the forms listed in the Annex A to the Decree. For Italian purposes the term companies includes joint stock companies, partnerships limited by shares, limited liability companies. In addition Italy, with respect to the Italian subjects, has also included cooperative companies, mutual insurance companies and any other private or public company carrying out business activities. (b) Subject to one of the taxes indicated in Annex B to the Decree, with no possibility of an option or of being exempt. (c) According to the tax laws of Member State are considered to be resident in that State and are considered, under a DTC, tax resident within the European Community.	

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
1.2 Foreign Member State and third state merger Italian Legislation enacting the Merger Directive does not interpret 'companies involved' in this scenario as including parent companies., (a) Mergers between companies resident in Italy and owned by foreign companies are not covered by the Italian Merger Directive; they do follow under the scope of the domestic tax legislation. (b) Mergers between companies from a single Member State with Italian shareholders do not fall under the Italian Merger Directive, but they should not create any taxable event in Italy as no capital gain arises at the Italian shareholders level from the merger itself.	

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term 'securities' The term 'securities' has been interpreted as referring to shares or quotas of companies (no reference is made to other types of securities); the definitions of shares and quotas are set forth in the Italian Civil Code.	Articles 2346 and 2468 of the ICC

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' The 10% cash payment related to the intra-Community reorganizations has been allowed under the ITC. The term 'cash payments' should be interpreted in the light of the provisions set forth in the ICC, which provides that the cash payment cannot exceed 10% of the nominal value of the shares/quotas assigned. Please note that the 10% limit set forth in the	Paragraph 2, Article 2501*ter* of the Italian Civil Code

ICC is applicable only to mergers between share companies. As far as Italian Tax Law is concerned in case of intra-Community reorganization, the 10% cash payment applies as follows: (a) Mergers/divisions and partial divisions: 10% of the nominal value of the participation received. Based on our interpretation, it should apply on a per shareholder basis, however no specific comments in this respect have been found both in the doctrine and in Italian Tax Authorities interpretations. (b) Exchange of shares: 10% of the nominal of the shares or quotas attributed to the participants. Based on our interpretation, it should apply on a per shareholder basis, however no specific comments in this respect have been found both in the doctrine and in Italian Tax Authorities interpretations.	

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
<u>2.3 Further types of merger</u> The ITC does not specifically define the term 'merger'. As a consequence, reference should be made to the ICC and to the Directive 2005/56/CE which do not contemplate other types of mergers. The ICC comprises the same forms of mergers covered by the Merger Directive. No other types of mergers are covered. Companies under liquidation that have already started distributing their assets may not participate in a merger.	Article 2501 of the ICC

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
<u>2.4 Qualifying exchange of shares</u> The wording of the ITC had lead to different interpretations of the term 'consolidate' ('*integrare*'); in the absence of an official interpretation of the Italian Tax Authority, the doctrine had expressed its opinion that the above term covered both the exchange of shares leading to the obtaining of a majority of the voting rights, and any further exchanges that might consolidate that majority.	Article 178(1)(e) of the ITC Legislative Decree No. 199 of November 6, 2007 Ruling 190/E of December 13, 2000 Ruling 159/E of

Effective January 1, 2007, these doubts have been clarified in the new wording of the law. With respect to the definition of majority holding the law has also been modified in order to take into account paragraph 15 of the Preamble of the 2005 amending Directive. Accordingly, the definition of exchange of shares contained in the Merger Directive as implemented in Italy covers not only an exchange of shares leading to the obtaining of a majority of the voting rights either by law or according to the statute or voting rules, but also any further exchange that may consolidate that majority. As a final remark, Italian Tax Administrations, following the EC observations, have replaced a previous interpretation requiring that the book value of the participation received by the contributing company was equal to the book value of the participation. Accordingly, such requirement is no longer to be met to benefit from the Italian Merger Directive.	July 25, 2003

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
2.5 Consolidation of qualifying holding The relief is not subject to any further conditions set by the ITC in addition to the conditions set forth in the Merger Directive (please see 2.4). However, the Italian Tax Authority has taken the position that the exchange of shares should be carried out for valid business reasons and without any intention of avoiding taxes. As a consequence, the exchange of shares should be subject to the general anti-avoidance provision set forth in Article 37bis of Presidential Decree No. 600 of September 29, 1973.	Ruling 55/E of April 17, 1996 Ruling No. 106/E of July 7, 2000 Article 37bis of Presidential Decree No. 600 of September 29, 1973

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
2.6 The term 'branch of activity' The term 'branch of activity' has been implemented in the ITC by using the term '*azienda*' (i.e. business) and '*ramo d'azienda*' (i.e., business going concern or independent part of a business). The former term is defined in Article 2555 of the ICC. The latter term has been interpreted by the Italian Tax Authorities as 'a collection of assets that together enable to carry out a business activity, i.e. a collection of assets able to satisfy the technical needs of a production activity'.	Ministerial Circular No. 321530 of October 25, 1965.

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
3.1 Types of entities Please refer to the answer under 1.1.	

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
3.2 Transparent entities Italian Tax Legislation regards foreign entities as non-transparent for the purpose of the application of the CIT.	Article 73(1)(d) and (2) of the ITC Article 89(3) of the ITC

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency Italian Tax Law defines as resident in Italy entities that for the majority of the fiscal year have in Italy either their main seat, or the administrative seat, or carry on in Italy their main/core and substantial business activity. The main seat of the company is provided for by its statute. The main/core business activity is instead to be found based on a substantial approach. Many Supreme Court and Tax Courts decisions and Italian Tax Authorities interpretations have been issued in this respect. Italian tax treaties mainly follow the OECD Model Convention. However, Italy has expressed an observation to paragraph 24 of the OECD Commentary stating that 'the place where the main/core and substantial activity of the entity is carried on is also to be taken into account when determining the place of effective management'.	Articles 5(3)(d) and 73(3) of the ITC

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>3.4 Subject-to-tax clause</u> Article 3(c) has been introduced in the ITC by making reference to fulfillment of the subject to tax (Annex B) clause without the possibility of benefiting of an optional tax regime; no reference is made to the possibility of being exempt. However, Italian Tax Law has implemented the Parent-Subsidiary and the Interest and Royalties Directives by making reference to the fulfillment of the subject to tax (Annex B) clause without the possibility of benefiting of an optional regime or of being exempt. The Italian Doctrine has considered such difference as a lack in the implementation of the Merger Directive not to be interpreted as widening the application of the same. As a consequence, the subject to tax clause in the Italian Merger Directive should be interpreted in the light of the wording of the Italian Parent-Subsidiary and Interest and Royalties Directives.	Articles 26*quater* and 37*bis* of the Presidential Decree No. 600 of September 29, 1973

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>3.5 Shareholder requirements</u> 3.5.1 Mergers/divisions and partial divisions: The ownership of a company by EU or EEA nationals or residents is not relevant for Italian Tax Law purposes in order to apply the Merger Directive. Therefore the shareholders involved in the transaction might be resident also outside the EU/EEA territory or may even have a legal form different from what stated by the Merger Directive (i.e., they might also be individuals). 3.5.2 Exchange of shares: ITC requires that at least one of the participants that make the share exchange is either a resident in Italy or an Italian PE to which such shareholding is attributed. In this respect please see 1.1.	Article 178(1)(e) of the ITC

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>**4.1 The concepts of 'real values' and 'value for tax purposes'**</u> No specific reference to the 'real value' concept is made in the ITC. However, in general, reference should be made to the fair market value. According to the Italian Tax Authorities, in relation to the fair market value reference should be made to the value that would be applied in case of transactions between independent enterprises. The ITC does not contain any specific provision defining the 'value for tax purposes' concept resembling that in the Merger Directive. However, the same concept can be construed by considering several ITC provisions. Accordingly, in principle the value for tax purposes is equal to the cost of acquisition plus capitalized expenses less depreciation.	Article 9(3) and (4) of the ITC Articles 179(1) and (6), 172(1) and (8) of the ITC

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
<u>**4.2 Specific guidance for divisions/partial divisions**</u> <u>4.2.1 Concept</u> The valuation of assets in case of divisions and partial divisions follows the same rules as applicable to mergers. In case of a division, the Merger Directive requires the transfer of all of the assets and liabilities of the transferring company to two or more existing or new companies. Under the ITC it is required for a division that the assets transferred must each be branches of activities ('*ramo d'azienda*'). It should be noted that there is a discrepancy between the rules governing the domestic divisions and intra-community divisions whereby the domestic provisions do not require that the assets transferred must each be branches of activities. <u>4.2.2 Conclusion</u> In our view a differentiation between the partial division - which requires that at least one branch of activity must be retained by the transferring company and at least one branch of activity must be transferred to the acquiring company - and a division is not justified. As a matter of fact considering that, Article 2(f) of the Merger Directive states that the receiving company must either receive (all) assets and liabilities or one or more branches of activity, also the division under the Merger Directive requires the transfer of branches of activities to the acquiring companies involved.	Article 178(1)(b), 179(6) and 173 of the ITC

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' Italian Tax Legislation does not provide for a specific definition of 'effectively connected'. As of January 1, 2004, ITC contains a definition of 'permanent establishment' which substantially resemble the definition given in the OECD Model Convention. The main difference is that 'building sites, construction or installation projects and related supervisory activities are set forth in a separate paragraph. As a final remark, no 'force of attraction' of the permanent establishment is included in the Italian Tax Law. Therefore, assets should not be effectively connected with a permanent establishment when they are not used in the conduct of the business of the permanent establishment and/or their production or trade is not the purpose of the business of the permanent establishment. In addition there are no specific law requirements with respect to its 'the balance sheet and the profit and loss account', which may be drawn up under any method and any form, provided that they comply with normal accounting principles'. Nevertheless, ITC provides detailed provisions regulating positive and negative items of the income of a tax resident entity and the criteria of evaluation of the assets and liabilities forming part of the working capital of such entity. Please note that according to Italian Tax Law, there is a formal segregation requirement for accounting and tax purposes of assets/liabilities/reserves of the foreign permanent establishment of Italian companies although they are integrated in the Statutory financial Statements of the Italian Company.	Article 15(4) of Presidential Decree No. 600 of September 29, 1973 Article 162 of the ITC

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief No limitation has been set forth in the Italian Tax Law.	

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment Upon realization of intra-community reorganizations assets and liabilities not effectively connected with the permanent establishment in Italy are considered as realized; consequently, the difference between their fair market value and tax value is considered capital gain subject to tax according to ITC.	Articles 166(1) and 86 of the ITC

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company According to ITC, merger profit is tax exempt even if the profit can be allotted to shares of the receiving company in the transferring company.	Law 549 of December 28, 1995

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral No specific account has been taken.	

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities N/A.	

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
<u>4.9 Further conditions for tax relief</u> No further conditions have been set forth in Italian Tax Legislation. It should be noted, however, that from a tax compliance perspective, Italian tax law requires that the difference between the book value of the assets and liabilities transferred entered in the balance sheet of the transferee and their tax value must be indicated in a 'recapitulative statement' to be attached to the tax return.	

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>5.1 The term 'provisions and reserves'</u> No specific definition is given under Italian Tax Law. In principle, reference should be made to the Italian Civil Code and to the Italian Accounting Standard Principles since Italian Tax Law states that the Statutory Financial Statements are the starting point for applying Tax principles ('*principio di derivazione*').	Section IX, Book V of the Italian Civil Code OIC 4

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
<u>5.2 Exclusion of 'provisions and reserves' from permanent establishments</u> In case of mergers, divisions (no specific reference is made to partial divisions) and transfer of assets, the ITC states that tax-free provisions and reserves of the Italian resident transferring company, which are not derived from permanent establishment abroad, may be carried over in a tax exemption regime by the Italian permanent establishment of the non resident receiving company. Provision and reserves totally or partially tax free are taxable in Italy only if they are not recorded in the accounting of transferee's Italian permanent establishment. Should the merger surplus be distributed or the capital be reduced, the related reserved will be taxable.	Article 180 of the ITC

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
<u>**5.3 Allocation method for provisions and reserves**</u> No specific regulations are provided for by the ITC in case of intra-Community divisions, partial divisions or transfer of assets. However, the regulations provided for domestic divisions should be applicable to intra-Community divisions: in such a case provisions and reserves are to be allocated in proportion to the net equity transferred to the beneficiaries, unless they specifically relate to single assets or liabilities transferred; in the latter case they follow the asset/liability they relate to. With respect to domestic transfer of assets, the provisions and reserves must be transferred with the assets in relation to which they have been created.	Article 173(4) and (9), and Article 180 of the ITC Article 176(5) of the ITC

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
<u>**5.4 Further conditions for carry-over of provisions and reserves**</u> No other conditions are set forth in Italian Law than the Italian Accounting Principles aimed at carrying out the transaction from an Italian accounting point of view.	

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
<u>**6.1 The concept of carry-over of losses**</u> Article 181 of the ITC is substantially similar to above mentioned Article of the Merger Directive. The concept of 'loss' for the purpose of implementing Article 6 of the Merger Directive is not different from the concept used for Italian tax purposes. In fact, such tax losses are subject to the same anti-avoidance provision as are set forth for domestic mergers (i.e., net equity threshold and economic/vitality test). Tax losses are determined on the basis of the tax adjustments provided for by the ITC provisions to the accounting net income/loss.	Articles 181 and 172(7) of the ITC

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment Article 181 states that tax losses of the Italian transferring company may be carried over to the foreign receiving company to the extent they relate to the assets and liabilities effectively connected with the post-reorganization Italian permanent establishment. Should the tax losses be not effectively connected with the Italian permanent establishment, the above described tax loss carry-over will not be granted. The post-reorganization Italian permanent establishment takes over the tax losses belonging to the Italian transferring company in proportion to the net equity transferred to the permanent establishment. Such tax losses will be available to offset, in the tax return, future taxable income of the post-reorganization Italian permanent establishment. Please note that according to the ITC, losses may be carried forward for five years with the exception of the losses generated in the first three years of activity. The tax losses carry forward period is not refreshed neither through domestic reorganization nor through intra-Community reorganizations.	Articles 84 and 181 of the ITC

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets 6.3.1 Divisions/partial divisions: The rules outlined above also apply to divisions but not to partial division since Article 181 specifically refers only to mergers and divisions, without mentioning partial divisions. It is our opinion that the take over of tax losses should be extended to intra-Community partial divisions since it is allowed for domestic partial divisions, however as to date no specific comments have been made by the doctrine or by the tax authorities in this respect. 6.3.2 Transfer of assets: Because losses cannot be taken over in a domestic transfer of assets, there is no carry over loss rule existing which must be extended to cross border transfer of assets under the Merger Directive.	Articles 172(7), 173(10) and 181 of the ITC.

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
<u>6.4 Further conditions for carry over of losses</u> No further conditions for carry over of tax losses which were not set out in Article 6 of the Merger Directive has been implemented, but for an anti-abuse requirement, which applies also to domestic divisions. In particular, losses carry forward upon merger and division is allowed up to the limit of the net equity of company and if in the profit and loss account preceding the change of ownership, the same company has had revenues from the ordinary activity and costs for employees higher than 40% of the average of the previous two fiscal years. As far as partial divisions, transfer of assets and exchange of shares, the general anti-abuse provisions should apply (please see 10c.1).	Article 181 of the ITC

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
<u>7.1 Amended holding threshold</u> No holding threshold has been implemented in the ITC. Accordingly, no threshold holding requirement is set forth for benefiting from the above mentioned provision.	Article 179(4) of the ITC

Article 7(1) covers <u>gains</u> accruing on the cancellation of a holding. It does not cover <u>losses</u> that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
<u>7.2 Treatment of losses</u> Italian Tax Law has not implemented Article 7(1) as regards the holding threshold and has not dealt with losses at all.	

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
<u>8.1 Avoidance of economic double taxation at the level of the shareholder</u> According to the ITC, no capital gain is realized in case the shareholders attribute to the securities received a tax value equal to the tax value that the exchanged securities had before the reorganization. Accordingly, economic double taxation may arise and no specific Italian legislation has been implemented in order to avoid it.	Article 179 of the ITC

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>8.2 Computation of the capital gain</u> The capital gain on cash payments is computed according to national provisions applicable to domestic capital gains. Accordingly, in principle capital gains may be 95% exempted when realized by companies, and 60% exempt when realized by individuals if participation exemption regime requirements are met. Should such conditions not be met, capital gains will be fully taxable at the relevant CIT rates.	Articles 47(7), 58, 68, 87 and 179 of the ITC

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>8.3 Further conditions for tax relief</u> In principle, the restrictions to benefit from the relief are the following: (a) the reorganization must be carried out for valid business reasons and without any intention of avoiding taxes; (b) the Italian companies/assets forming part of the reorganization shall remain subject to tax in Italy through a permanent establishment in Italy; (c) tax losses carry forward is allowed if the net equity requirements and the economic/vitality test are satisfied.	Articles 172, 174, 178 and 179 of the ITC Article 37bis of the Presidential Decree No. 600 of September 29, 1973

Please note that the Italian domestic anti-abuse provision applies also to intra-community reorganization transactions. Therefore, such transactions and the relative benefits should be analyzed in the light of it.	

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>**9.1 Avoidance of economic double taxation at the level of the transferring company**</u> No specific Italian legislation has been implemented in order to avoid economic double taxation.	

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>**9.2 Further conditions for tax relief**</u> Pursuant to the general anti-abuse provisions, the relief may be denied if the transfer of assets is not carried out for valid business reasons and with the intention of avoiding taxes. Moreover, the above mentioned (please see 8.3) 'permanent establishment provision' has been implemented under Italian Tax Law in order to benefit from the tax relief.	Article 37bis of the Presidential Decree No. 600 of September 29, 1973

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>**9.3 Tax deferral**</u> No specific account has been taken in relation to the judgment in Case C-470/04. ITC states that assets transferred as a result of a merger or division are deemed to be realized and taxed at the fair market value if they are not effectively connected to a permanent establishment in Italy. Roll-over is not granted, and therefore tax deferral not realized, in case the assets transferred to the permanent establishment are subsequently taken out of it.	Article 179(6)

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>**10.1 Loss recapture for permanent establishments in third Member States**</u> Italy does not consider loss recapture as it is stated in Article 10(1) of the Merger Directive: Italy in fact applies the derogation principle available under Article 10(2) in respect of the transfer.	Article 179(3) and (5) of the ITC

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>**10.2 Permanent establishment in the Member State of the receiving company**</u> Italy does not consider loss recapture as it is stated in Article 10(1) of the Merger Directive: Italy in fact applies the derogation principle available under Article 10(2) in respect of the transfer.	Article 179(5) of the ITC

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>**10.3 Concept of worldwide taxation/tax credit system**</u> Italian Tax Law provides for a notional credit system similar to the system set forth in Article 10(2) of the Merger Directive. Accordingly, if the Italian transferring company has a permanent establishment in another Member State, the capital gain on the transfer of the permanent establishment is taxed in Italy at its fair market value. However, a notional credit is granted for an amount equal to the tax that would have been levied by the state where the permanent establishment is located if the relief under the Merger Directive was not granted.	Article 9 and Article 179(5) of the ITC

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
10.4 Tax deferral Roll-over is not granted, and therefore tax deferral not realized, in case the assets transferred to the permanent establishment are subsequently taken out of it.	Article 166(1) and Article 179(5) of the ITC

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies Italian Tax Law has not implemented Article 10a. As far as the entities involved in the intra-Community reorganization satisfy the above mentioned requirements, they are considered entitled to benefit from the Merger Directive as implemented by the Italian Tax Law. Moreover, Italian Tax Legislation regards foreign entities as non-transparent for the purpose of the application of the CIT.	

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit N/A.	Article 179(3) of the ITC

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit N/A.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
<u>10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders</u> N/A.	

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
<u>10a.5 Comparison with a resident fiscally transparent company</u> N/A.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
<u>10b.1 Exit taxation</u> In principle, the SE was already included in the Italian Tax provisions concerning the application of CIT to transfer of the register office. However, such inclusion has been directly set forth in Article 73(1)(a) of the ITC through the Legislative Decree No. 199 of November 6, 2007. As a consequence, the transfer of the registered office of an SE does not give rise to capital gain if the assets of the transferring company are included in an Italian permanent establishment of the SE. Should this not be the case, a taxable capital gain would arise based on the fair market value of the assets not allocated to the PE. Moreover, loosing the fiscal residence does not represent a taxable event in the hands of the shareholders of the transferred company.	Article 73(1),(a) of the ITC Legislative Decree No. 199 of November 6, 2007 Article 166(1) and (4) of the ITC

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' Italian tax law does not contain a specific definition of head office.	

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency Please refer to the answer under question 3.3.	

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
10b.4 Assets and liabilities not effectively connected with a permanent establishment The assets and liabilities not connected to a permanent establishment in Italy after the transfer of the register office are subject to tax on the capital gain determined as difference between their fair market value and their tax value. Such capital gain is taxed according to Article 166 of the ITC. In case of permanent establishments abroad of companies transferring the registered office from Italy, the ITC provides for the taxation of the capital gains arising as difference between the fair market value and the tax value of the assets attributable to the foreign permanent establishments.	Article 166 of the ITC

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
10b.5 Tax deferral N/A.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
<u>10c.1 The term 'comparable circumstances'</u> The term 'comparable circumstances' has not been specifically defined for the purpose of implementing the Merger Directive. However, the concept is incorporated in the ITC by the wording of the rules in respect of the use of losses carried forward. In principle, to the extent a SE or SCE are still within the charge to IRES (i.e., assets and liabilities connected to a permanent establishment), losses are preserved in Italy in the event that they become non-Italian resident if: (a) they carry on a trade or business in Italy through a PE; (b) do not satisfy both the following anti-abuse requirements set forth in the domestic legislation in relation to the loss carry forward: Change of ownership requirement: the majority or voting rights is transferred; Change of business requirement: the business purpose is changed in the year of change of ownership or in the following two fiscal years. The above test does not apply if both the following conditions are met: (a) in the two years before the change of ownership, the company transferred has never had less than ten employees; and (b) in the profit and loss account preceding the change of ownership, the company transferred has had revenues from the ordinary activity and costs for employees higher than 40% of the average of the previous two fiscal years.	Articles 166(2)*bis* and 84(3) of the ITC

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
<u>10c.2 Loss recapture for permanent establishments</u> No loss recapture is provided for in the ITC.	

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>10d.1 Deemed liquidation</u> The transfer of the registered office of an SE/SCE should give rise to capital gain if the assets of the transferring company are not included in an Italian permanent establishment. Accordingly, only in such a case the transfer of the registered office would give rise to CIT taxation. Losing the fiscal residence does not give rise to taxes in the hands of the shareholders of the transferred company.	Article 166(1) of the ITC

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>10d.2 Tax treatment of third country residents</u> Losing the fiscal residence does not give rise to taxes in the hands of the shareholders of the transferred company irrespective of their residence status.	Article 166(4) of the ITC

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> The ITC does not contain a specific anti-avoidance provision applicable to intra-community restructuring transactions. However, the general domestic anti-avoidance provisions are applicable also to intra-community restructurings. With respect to share-for-share exchange transactions the Italian Tax Authorities have taken the position that the exchange of shares should be carried out for valid business reasons and without any intention of avoiding taxes. This confirms the opinion that the exchange of shares should be subject to the general anti-avoidance provision set forth in Article 37bis of Presidential Decree No. 600 of September 29, 1973.	Ruling 55/E of April 17, 1996 Ruling No. 106/E of July 7, 2000 Article 37bis of Presidential Decree No. 600 of September 29, 1973

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
<u>**11.2 General anti-abuse provision**</u> According to Article 37bis of Presidential Decree No. 600 of September 29, 1973, Italian Tax Authorities may disallow transactions, which do not have valid business reasons, if aimed at avoiding tax provision or at unduly reducing the tax burden. Such provision is applicable to the following transactions: (a) changes of legal structure, mergers, demergers, voluntary liquidations and net equity reserves (different from accumulated earnings and profits) distributions to the shareholders; (b) business/going concern contributions or other transactions related to the transfer of a business/going concern; (c) sale of receivables; (d) sale of tax credits; (e) intra-community reorganizations as ruled in the ITC, and transfers of tax residence abroad by companies; (f) transactions, as well as valuations and appraisals affecting the Statutory Financial Statements, regarding securities; (g) sale of assets and services within companies which applied for the Italian Tax Consolidation regime; (h) payment of interests and royalties to directly or indirectly controlled companies resident outside the European Community; (i) specific dealings with companies resident in countries not listed in the so-called 'white list'. The above described anti-abuse provisions may not apply on a case by case basis and subject to the filing of an advance ruling.	

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the '*Cadbury*' judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
<u>**11.3 The concept of 'wholly artificial arrangement'**</u> No steps have been taken in this respect. However, the domestic anti-avoidance provision seems to be in line with the '*Cadbury*' Judgment.	Article 37bis of Presidential Decree No. 600 of September 29, 1973

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions No other requirements are imposed by the Italian domestic provisions.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' Italian Tax Law has not defined the 'valid commercial reasons'. Some guidance can be found only in rulings to specific cases scrutinized under the anti-abuse provision. However, no specific principles have been issued by Italian Tax Authorities. From the rulings referred to it is possible to understand the way of reasoning of the Italian Tax Authority which is based on a factual analysis on a case by case basis.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof In principle, the Italian Tax Authorities has the burden of proof.	Article 37bis(5) of Presidential Decree No. 600 of September 29, 1973

LATVIA

Abbreviations

English	Latvian	English	Latvian
CITA	-	Corporate Income Tax Act	Likums ‘Par uzņēmumu ienākuma nodokli’
TDA	-	Taxes and Duties Act	Likums ‘Par nodokļiem un nodevām’
CL	KL	Commercial Law	Komerclikums
APL	APL	Administrative Procedure Law	Administratīvā procesa likums
AAL	-	Annual Accounts Law	Gada pārskatu likums
SE	SE	European Company	Eiropas komercsabiedrība
SEA	-	European Companies Act	Eiropas komercsabiedrību likums
SCE	SCE	European Cooperative Company	Eiropas kooperatīvā sabiedrība
SCEA	-	European Cooperative Companies Act	Eiropas kooperatīvo sabiedrību likums
Reg. No 556	MK not. Nr. 556	Regulation No 556 ‘Procedures for the Application of Provisions of the Corporate Income Tax Act’ adopted by the Cabinet of Ministers on 4 July 2006	2006. gada 4. jūlija Ministru kabineta noteikumi Nr. 556 ‘Likuma ‘Par uzņēmumu ienākuma nodokli’ normu piemērošanas noteikumi’
Reg. No 587	MK not. Nr. 587	Regulation No 587 ‘Procedures for Determining Taxable Income and Paying of Tax of Permanent Establishments of Non-residents’ adopted by the Cabinet of Ministers on 27 December 2002	2002. gada 27. decembra Ministru kabineta noteikumi Nr. 587 ‘Nerezidentu pastāvīgo pārstāvniecību apliekamā ienākuma noteikšanas un nodokļu maksāšanas kārtība’

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.

<u>Overall state of implementation</u>

The Merger Directive has been implemented by the following amendment acts:

(a) Amendments in the Corporate Income Tax Act adopted by the 'Saeima' on 19 June 2003 (official newspaper 'Latvijas Vēstnesis' No 101 dated July 8, 2003). The amendment act came info effect on July 23, 2003.

With this amendment act, the Merger Directive was implemented by adding the following sections and paragraphs to the CITA:

- Section 6^2 'Special Provisions for Taxpayers Involved in a Reorganization';
- Section 6^3 'Special Provisions for Shareholders of a Company Involved in a Reorganization';
- eight paragraphs to Section 1 'Terms Used in the Law' defining terms 'transfer of assets', 'exchange of shares', 'merger', 'division', 'recognized cash payment', 'company', 'shareholder', 'security';
- Paragraph 5^1 to Section 8^1 'Tax Relief on Acquisition of Buses Used for Passenger Traffic' implementing tax relief in relation to reserves;
- Paragraph 11^1 to Section 14 'Losses Carry-Forward' implementing tax relief for losses carry-forward.

(b) Amendments in the Corporate Income Tax Act adopted by the 'Saeima' on 20 October 2005 (official newspaper 'Latvijas Vēstnesis' No 179 dated November 9, 2005). The amendment act came into effect on January 1, 2006. The amendment act has been adopted to implement the provisions of the Council Directive 2005/19/EC by adding the following sections and paragraphs to the CITA:

- Paragraph 22 to Section 1 'Terms Used in the Law' defining term 'transfer of the registered office';
- Paragraph 14 and 15 to Section 6 'Adjustment of Taxable Income' implementing tax relief for SE and SCE in relation to provisions and reserves;
- Paragraph 3^1 to Section 13 'Write-off of Value of Depreciated Fixed Assets and Intangible Investments' implementing tax relief for SE and SCE in relation to assets;
- Paragraph 1^2 to Section 14 'Losses Carry-Forward' implementing tax relief for SE and SCE in relation to losses carry-forward;
- Section 26^1 'Prevention of Tax Evasion' implementing rules for prevention of tax evasion in case of transfer of the registered office of SE or SCE.

The Regulation No 556 'Procedures for the Application of Provisions of the Corporate Income Tax Act' adopted by the Cabinet of Ministers on 4 July 2006 provides further explanations regarding

Paragraph 2 of Section 66[2] 'Special Provisions for Taxpayers Involved in a Reorganization'. The Amendments in the Commercial Law implementing Directive 2005/56/EC are not adopted by the 'Saeima'. On 28 February 2008 the draft law is approved by the 'Saeima' on second reading and shall be adopted on third (final) reading. The SE-Regulation (No. 2157/2001) has been supplemented with the European Companies Act adopted by the 'Saeima' on 10 March 2005 (official newspaper '*Latvijas Vēstnesis*' No 49 dated March 24, 2005). The amendment act came info effect on April 7, 2005. The SCE-Regulation (No. 1435/2003) has been supplemented with the European Cooperative Companies Act adopted by the 'Saeima' on 26 October 2006 (official newspaper '*Latvijas Vēstnesis*' No 180 dated November 9, 2006). The amendment act came info effect on November 23, 2006.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> <u>1.1.1. Definition of Company</u> The legislation enacting the Directive has defined the term 'company' as a capital company, which is a resident of the Republic of Latvia, as well as a company – resident of other Member States of the European Union, which at the same time conforms to the following criteria: (a) is referred to in the Annex 1 of CITA (complies with Annex of Directive); (b) in accordance with the tax laws of the Member States of the European Union is recognised for tax purposes as a resident of the relevant Member State of the European Union and, under the terms of an agreement for the prevention of double taxation, which has been entered into with a third state, for tax purposes is not considered to be a resident of a state which is not a Member State of the European Union; and (c) is a taxpayer, which pays one of the taxes referred to in Annex 2 of CITA if it is not exempt from the relevant tax or it does not have the possibility to choose a tax exemption. The above-mentioned criteria conform to Article 3 of the Merger Directive. <u>1.1.2. Companies Involved</u> The expression 'in which companies from two or more Member States are involved' has been interpreted as comprising only the companies directly involved in the transaction and not the parent companies.	Sec. 1 (19) CITA Sec. 6[2] (3) CITA

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
1.2 Foreign Member State and third state merger If the merging companies were from a third State or States, the benefits of the Merger Directive under the Latvian laws would not apply. If the merging companies were from a single foreign Member State, the benefits of the Merger Directive would apply only if the assets and liabilities of the transferring company after the transfer thereof would be applicable to the permanent establishment of the receiving company in Latvia.	Sec. 6^2 (3) CITA

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term 'securities' Securities are defined in the CITA as stocks, shares, capital shares or other documents, which create a right to receive dividends.	Sec. 1 (21) CITA

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' Cash payments are defined in the CITA as cash which, in addition to the value of issued or transferred stock, is paid by the acquiring company, receiving company, acquired company or divided company and which does not exceed 10% of the nominal value of the issued or transferred stock. The CL applies the cash payment on an overall basis. However, the CITA by implementing the Merger Directive does not give clear guidance regarding the application of the cash payment.	Sec. 1 (18) CITA Sec. 376 CL

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger No other forms of merger are contemplated.	Sec. 1 (16) CITA

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares According to the CITA, exchange of shares is defined as a process whereby a company (acquiring company) acquires a holding in the capital of another company (acquired company) in exchange for the securities issued by the acquiring company or the transfer thereof to the shareholders of the acquired company and – depending upon the circumstances – for a recognised cash payment receiving the securities of the acquired company, on the condition that the acquiring company has a majority of votes in the acquired company. Based on the above-mentioned definition, the relief will be granted only in respect of the exchange that finally leads to the acquisition of a majority holding. Each successive exchange of shares that does not per se achieve the necessary majority of votes is not a qualifying exchange of shares.	Sec. 1 (15) CITA

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
2.5 Consolidation of qualifying holding The CITA provides for the following additional conditions to qualify for tax relief for shareholders: (a) shareholders shall be residents of Latvia or (b) non-resident that has a permanent establishment in Latvia that is the holder of the transferred shares and the shares received in the result of exchange of shares. If the acquiring company already owns a majority holding any further exchanges of shares would be treated as a qualifying exchange of shares.	Sec. 1 (15) CITA Sec. 6^3 (3) CITA

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>2.6 The term 'branch of activity'</u> According to the CITA, the branch of activity shall include all such assets and liabilities of the company, which from an organisational point of view constitute an independent economic activity. There is no further explanatory guidance provided by the Latvian tax authorities regarding the term 'branch of activity'. We are of the opinion that the term must be interpreted in the light of the Merger Directive taking into account also the clarification provided by Case C-43/00 '*Andersen og Jensen*'.	Sec. 1 (14) CITA

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> The CITA applies the Merger Directive only to types of entities listed in the Annex of the Merger Directive.	Sec. 1 (19) CITA

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>3.2 Transparent entities</u> The term 'transparent entity' is not defined in the Latvian legislation and there is no general legislative or administrative guidance. Although the Latvian tax system treats certain entities as transparent for tax purposes, there is no general definition and no criteria to determine the tax transparent entity according to the Latvian tax legislation. Therefore, in respect of foreign entities it is difficult to determine whether the entity would be regarded as transparent according to the Latvian legislation.	N/A.

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency 3.3.1 Tax residency under domestic law According to the TDA, for the purposes of tax legislation, a taxpayer who is not a natural person shall be considered a resident if he was established and registered or if he should have been established and registered in accordance with the laws of the Republic of Latvia. Accordingly, the main criterion for the determination of tax residency under the domestic laws is the place of incorporation. However, there are certain types of economic activities that according to the Latvian laws may be undertaken only by persons registered with the Commercial Register of the Register of Enterprises. In case the person has undertaken such economic activity in Latvia without the appropriate registration, it will be considered to be a tax resident irrespective of the registration fact. 3.3.2 Tax residency under Double tax conventions The double tax conventions concluded by the Republic of Latvia generally do not provide one tiebreaker criterion for the tax residency of corporations. There are two main criteria – place of effective management and place of incorporation. However, the double tax conventions provide for any other criteria of similar nature to be used as tiebreaker criterion for tax residence qualification. There is no hierarchy between the different criteria mentioned. According to the majority of double tax conventions, where by reason of tax residency on grounds of place of management, place of incorporation or any other criterion of a similar nature person other than an individual is resident of both contracting states, the competent authorities shall endeavour to settle the question by mutual agreement. In absence of such agreement, for the purposes of the double tax convention, the person shall not be entitled to claim any benefits provided by the convention.	Sec. 14 (4) TDA Article 4 (3) of various Latvian double tax conventions

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject-to-tax clause The subject to-tax-clause is implemented in the national legislation by defining that only the companies – residents in other Member States of the European Union – that are subject to one of the mentioned taxes, without the possibility of an option or of being exempt, may benefit from the provisions of the Merger Directive as implemented in the CITA.	Sec. 1 (19) CITA

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
3.5 Shareholder requirements The ownership of a company by EU or EEA nationals is not relevant for application of the benefits of the Merger Directive as implemented in the CITA.	Sec. 1 (19) CITA

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
4.1 The concepts of 'real values' and 'value for tax purposes' 4.1.1 Interpretation 4.1.1.1 Real value According to the AAL, the real value is the amount in respect of which it is possible to exchange assets or fulfil obligations in a transaction between well informed, interested and financially independent persons. 4.1.1.2 Value for tax purposes 'Value for tax purposes' has been interpreted as the net book value of the assets in the books of the transferring company at the time of the merger, division or transfer of assets. 4.1.2 Implementation In case of merger, division or transfer of branch of activity, the results of the revaluation of the transferred assets and liabilities shall not be taken into account for the determination of the taxable income. In calculating the depreciation of fixed assets in accordance with the provisions of the CITA, the results of the revaluation of fixed assets shall not be taken into account in determination of the residual value of fixed assets, which the receiving company has received in relation to merger, division or transfer of branch of activity, i.e. the net tax value of the transferred fixed assets of the transferring company becomes the initial net tax value of the fixed assets of the receiving company. The above-mentioned provisions are subject to the one of following requirements: (a) in case of the transfer of branch of activity existing in Latvia or in another Member State of the European Union, both the transferring, merging or dividing company and the receiving	Preamble AAL Sec. 6^2 (1) (2) (3) CITA Clause 70 Reg. No 556

company shall be Latvian residents; (b) in case of merger, division or transfer of branch of activity existing in Latvia, the transferring, merging or dividing company shall be a resident of a Member State of the European Union and the receiving company shall be a Latvian resident and the assets and liabilities after the transfer thereof shall not be applicable to the permanent establishment of the receiving company outside of Latvia; (c) the receiving company shall be a resident of a Member State of the European Union and the transferring, merging or dividing company shall be a resident of Latvia or of a Member State of the European Union and the asset and liability obligations after the transfer thereof shall be applicable to the permanent establishment of the receiving company in Latvia.	

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions No specific guidance has been issued in respect of divisions and partial divisions. See 4.1.2.	Sec. 6^2 (1) (2) (3) CITA

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' 4.3.1 Concept of 'permanent establishment' According to the TDA, it shall be considered that a non-resident has a permanent establishment in Latvia if all of the following conditions simultaneously are complied with: (a) the non-resident uses a specific place for activities in Latvia; (b) the place for activities is permanently used or is established for the purpose of being used permanently; and (c) the place for activities is used for the performance of economic activities. The permanent establishment of a non-resident company in Latvia shall be considered a separate domestic taxpayer for the application of all Latvian	Sec. 14 (6) (7) (9) TDA Sec. 6^2 (3) CITA

tax laws. A permanent establishment of a non-resident company in Latvia shall pay taxes in accordance with the laws of the Republic of Latvia for income obtained in the Republic of Latvia, its territorial waters and air space, for income obtained in foreign states which pertains to this permanent establishment, as well as other taxes in accordance with specific tax laws. 4.3.2 Concept 'effectively connected' There is no specific definition of 'effectively connected' within Latvian laws. According to the provisions of the CITA, the transferred assets and liabilities shall be attributable to the permanent establishment of the receiving company in Latvia. The concept is implemented in order to assure that the right of Latvia to tax the gain on the disposal of the transferred assets with the receiving company is not excluded or limited as well as the profits generated from the transferred assets will be taxable in Latvia.	

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief The relief shall not be applied if the securities of the receiving company which have been received by the transferring, merging or dividing company are not in their ownership at least three years after the transfer thereof, unless the transferring, merging or dividing company justifiably prove that the alienation of such securities has not been performed for the purpose of reducing its taxable income and not to pay the taxes payable in Latvia or to reduce the amount thereof. In our view the minimum ownership period of three years subject to prove of non tax avoidance purpose is not contrary to Article 11 of the Merger Directive because the relief is not withdrawn, if the taxpayer proves that the transaction has not been performed for the tax avoidance purposes. The CITA provides for a recapture of depreciation in case of alienation of new production technology equipment within a period of five tax periods from the acquisition or establishment of such fixed asset which is also applicable in the case of reorganisation. In such case the taxable income shall be increased by the amount of the fixed asset depreciation value calculated in accordance with the provisions of the CITA, regarding which in the previous five tax periods taxable income was reduced, and shall be reduced by the amount of such fixed asset depreciation value referred to in the annual accounts of the company. This provision shall not be applied if the referred fixed asset is lost as a result of a natural disaster or by other forced execution and is replaced in conformity with the provisions of the CITA. The CITA does not provide further explanations regarding the application of the above-mentioned provisions for the depreciation recapture. The State Revenue Service of the Republic of Latvia treats the mentioned	Sec. 6^2 (4) CITA Sec. 13 (1^4) CITA

provisions as applicable also to the transfer of assets during the reorganisation process. As result, the application of the depreciation recapture for new production technology equipment in case of reorganisation is incompliant with Article 4 of the Merger Directive.	

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
<u>4.5 Assets and liabilities not effectively connected with a permanent establishment</u> According to the CITA, the relief is available only in respect of transferred assets and liabilities that are considered to be effectively connected with a permanent establishment of the receiving company in Latvia. In respect of assets that are not effectively connected with the permanent establishment, the transfer of assets would be regarded as disposal of the assets and the results of revaluation of assets would be taken into account for tax purposes. However, there is no clear guidance provided in the Latvian tax laws regarding the required valuation of assets and liabilities not effectively connected with the permanent establishment in Latvia in case of reorganisation.	Sec. 6^2 (3) CITA

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
<u>4.6 Tax treatment of shares of the receiving company</u> A merger is profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company.	Sec. 6^3 (1) CITA

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>4.7 Tax deferral</u> There have been no specific amendments in respect of the legislation implementing the Merger Directive as the result of Case Law. Case C-470/04 *'N'* has not been commented by the Latvian tax authorities. The Latvian legislation has no special rules regarding 'exit tax' in case of loss of the status of national taxpayer neither for individuals, nor for companies.	N/A.

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
<u>4.8 Criteria to determine tax transparent entities</u> There are no criteria defined in the Latvian legislation regarding tax transparent entities (see 3.2). No specific rules regarding fiscally transparent entities (Article 4 (2) of the Merger Directive) have been implemented in the Latvian laws.	N/A.

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
<u>4.9 Further conditions for tax relief</u> The relief shall not be applied if the securities of the receiving company which have been received by the transferring, merging or dividing company are not in their ownership at least three years after the transfer thereof, unless the transferring, merging or dividing company justifiably prove that the alienation of such securities has not been performed for the purpose of reducing its taxable income and not to pay the taxes payable in Latvia or to reduce the amount thereof (see also 4.4, first paragraph).	Sec. 6^2 (4) CITA

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>5.1 The term 'provisions and reserves'</u> The term 'provisions' is defined in Sec. 19 (1) of AAL and in Clause 4 of the Latvian Accounting Standards No 8. Provisions are liabilities intended to cover specific forms of obligations, which relate to the accounting year or previous years and which are foreseeable or known during the preparation of the annual accounts period, but for which the size or the date of the creation and covering of the concrete obligation is not clearly known. The Latvian laws do not contain one general definition for the term 'reserves'. According to the AAL and the Latvian Accounting Standards, there are the following types of reserves: revaluation reserves, legal reserves and other reserves.	Sec. 10, 19 (1), 29, 55^3 AAL Latvian Accounting Standards No 1, No 8

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments No specific rules regarding 'provisions and reserves derived from permanent establishment abroad' have been implemented in the Latvian legislation. There is no administrative or other guidance issued regarding provisions and reserves, including the allocation of provisions or reserves to the company as a whole or its permanent establishments.	N/A.

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves There is no guidance issued in respect to allocation of provisions and reserves in the case of a division, a partial division, or a transfer of assets.	N/A.

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves The CITA does not provide for any specific conditions regarding the allocation of provisions and reserves. The relief shall not be applied if the securities of the receiving company which have been received by the transferring, merging or dividing company are not in their ownership at least three years after the transfer thereof, unless the transferring, merging or dividing company justifiably prove that the alienation of such securities has not been performed for the purpose of reducing its taxable income and not to pay the taxes payable in Latvia or to reduce the amount thereof (see also 4.4, first paragraph).	Sec. 6^2 (4) CITA

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
<u>6.1 The concept of carry over of losses</u> According to the CITA, generally the tax losses may be carried forward for a period of next five tax periods (five years). Tax losses may not be carried back. According to Sec. 14 (11^1) CITA implementing Article 6 of the Merger Directive, the receiving company is entitled to take over the losses of the transferring company incurred in the previous tax periods that are related to the transferred branch of activity, and to cover such losses in accordance with the provisions of the CITA in the tax period in which the transfer took place and in the subsequent tax periods. The carry over of losses is subject to the same conditions as stated for the carry over of balance sheet values of the transferred assets (See 4.1.2). Moreover, Sec. 14 (11) CITA provides: if a company is reorganized by merging with another company, and the first and second company prior to reorganisation, but the second company after reorganisation is controlled by one and the same person or group of persons, the second company after reorganisation is entitled to carry over the previous tax period losses of the first company or co-operative society and to cover them in the tax period and in following tax periods according to the procedures specified in the CITA. In our view the above mentioned provisions are in contradiction, because Sec. 14 (11^1) CITA allows to carry over the losses irrespective of the control of the companies, however, Sec. 14 (11) CITA adopted before the implementation of the Merger Directive provides that in case of the merger the transferring company is entitled to carry over the losses only if the control requirement is complied with. According to the latest explanations of the above provisions of the CITA provided by the tax authorities, in case of the merger it is allowed to carry over the losses only if the control requirement is complied with. However, the control is not required to carry over the losses in case of the transfer of assets. Accordingly, more favourable tax regime is provided for the transfer of assets in comparison with the merger.	Sec. 14 (1) (11) (11^1) CITA

What method is applied to allocate losses to the permanent establishment?	Reference
<u>6.2 Allocation of losses to the permanent establishment</u> The taxable income of a permanent establishment of a non-resident shall be determined by assuming that the permanent establishment is a capital company – a resident of Latvia that carries out the same or similar activity in the same or similar conditions as the permanent establishment and	Sec. 14 (1) (11) (11^1) CITA Clause 4 of Reg. No 587

operates independently of the non-resident, the permanent establishment of which it is, and of any other persons (residents or non-residents). Subject to the conditions stated above (see 6.1), the losses of the transferring company may be covered with the taxable income of the receiving company's permanent establishment in Latvia.	

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
<u>**6.3 Specific legislation for divisions/partial divisions/transfer of assets**</u> The general rules that are outlined above (see 6.1, first paragraph) apply also for divisions, partial divisions and transfer of assets. The tax regime applicable for the transfer of assets is described in 6.1. If in the course of reorganisation a company is divided and the dividing company at the time of reorganisation has losses which it is entitled to cover, the right to cover the losses of this company in the case of division, observing the below-mentioned provisions, shall be carried over by the newly-founded companies, but in the case of partial division – the dividing company after reorganisation and the newly-founded company have both the right to offset previous losses. The losses of the dividing company shall be divided between the companies according to the following proportion - the value of the assets of the dividing company after reorganisation against the value of the assets of the dividing company prior to reorganisation.	Sec. 14 (1) (11^1) (12) (13) CITA

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
<u>**6.4 Further conditions for carry over of losses**</u> The relief will not be applied if the securities of the receiving company which have been received by the transferring, merging or dividing company are not in their ownership at least three years after the transfer thereof, unless the transferring, merging or dividing company justifiably prove that the alienation of such securities has not been performed for the purpose of reducing its taxable income and not to pay the taxes payable in Latvia or to reduce the amount thereof. These conditions apply also in case of the transfer of branch of activity existing in Latvia or in another Member State of the European Union in case, if both the transferring, merging or dividing company and the receiving company are Latvian residents.	Sec. 6^2 (3) (4) CITA Sec. 14 (1) (11^1) CITA

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Amended holding threshold The restriction in respect to the holding threshold (15%) has not been implemented in the Latvian laws.	N/A.

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses According to Sec. 6^3 (1) of CITA, a profit (or loss) resulting from the revaluation of the transferred shares shall not be taken into account with respect to the receiving company subject to the following conditions: the receiving company shall be either the resident of Latvia or the non-resident that has a permanent establishment in Latvia that is the holder of the transferred shares and the shares received in the result of exchange of shares. No further legislative or administrative guidance is issued relating the losses realized on the cancellation of holding.	Sec. 6^3 (1) (3) CITA

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder According to the provisions of the CITA implementing Article 8 of the Merger Directive, in case of merger, division or exchange of shares the results of the revaluation of the transferred shares shall not be taken into account with respect to the receiving company. The shares received in the result of exchange of shares shall be valued by the shareholder on the basis of their acquisition value, which the shares had at the moment of the exchange of shares in accordance with final financial report, and this value shall be increased by the amount of the recognised cash payment. The above-mentioned conditions are applicable to the following shareholders:	Sec. 6^3 CITA

(a) residents of Latvia; (b) non-resident that has a permanent establishment in Latvia that is the holder of the transferred shares and the shares received in the result of exchange of shares. However, according to the Latvian tax legislation, non-resident shareholders without a permanent establishment in Latvia are not taxed on the capital gain derived from their holding in a Latvian acquired company. According to the clarifications provided by our tax authorities the Sec. 6^3 CITA shall be interpreted as any revaluation made with regard to the shares will be disregarded for tax purposes in the moment of merger, i.e. shall not be taxable at the moment of transfer. Furthermore, the company receiving the shares shall account the shares at book value, i.e., acquisition value of shares before the reorganization. Thus, the tax relief is granted until further realization of capital gain.	

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>**8.2 Computation of the capital gain**</u> If the shareholder receives recognised cash payment, the results of the revaluation of the transferred shares shall be applied to the cash payment and included in the taxable income of the shareholder. There is no further guidance issued by the tax authorities on the computation of the capital gain according to Article 8 (9) of the Merger Directive.	Sec. 6^3 (1) CITA

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>**8.3 Further conditions for tax relief**</u> The tax relief is applicable only to the following shareholders: (a) residents of Latvia; (b) non-resident that has a permanent establishment in Latvia that is the holder of the transferred shares and the shares received in the result of exchange of shares.	Sec. 6^3 (3) CITA

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
9.1 Avoidance of economic double taxation at the level of the transferring company The Latvian tax legislation does not provide for the value to be attributed to the shares received by the transferring company. According to the CITA, the results of the revaluation of the assets and liabilities of the transferring company due to the transfer of assets shall not be taken into account for the determination of the taxable income of the transferring company. Accordingly, the transfer of assets does not give rise to the taxation at the level of the transferring company, subject to the condition that the receiving company in relation to the received assets and liabilities remains subject to the Latvian tax.	Sec. 6^2, 6^3 CITA

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
9.2 Further conditions for tax relief The relief will not be applied if the securities of the receiving company which have been received by the transferring company are not in its ownership at least three years after the transfer thereof, unless the transferring company justifiably proves that the alienation of such securities has not been performed for the purpose of reducing its taxable income and not to pay the taxes payable in Latvia or to reduce the amount thereof (see also 4.4, first paragraph).	Sec. 6^2 (4) CITA

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
9.3 Tax deferral There have been no specific amendments in respect of the legislation implementing the Merger Directive as the result of Case Law. Case C-470/04'N has not been commented by the Latvian tax authorities.	N/A.

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Loss recapture for permanent establishments in third Member States</u> The provisions of Article 10 of the Merger Directive have not been implemented in the Latvian legislation. Accordingly, the Latvian legislation does not provide for loss recapture as envisaged by Article 10 (1) of the Merger Directive.	N/A.

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> The provisions of Article 10 of the Merger Directive have not been implemented in the Latvian legislation. In order to make a conversion of a permanent establishment of a foreign company into a resident subsidiary, the following steps shall be undertaken: (a) a foreign company shall transfer the assets and liabilities allocated to its Latvian permanent establishment to a company located in Latvia; (b) the company in Latvia shall transfer those assets and liabilities to its subsidiary. In case a foreign company transfers the assets and liabilities (the branch of activity) allocated to its Latvian permanent establishment to a receiving company located in Latvia in exchange for the securities of the receiving company: (a) the results of the revaluation of the assets and liabilities of the transferring company due to the transfer of assets shall not be taken into account for the determination of the taxable income of the transferring company in Latvia; (b) the results of the revaluation of fixed assets shall not be taken into account in determination of the residual value of fixed assets for tax purposes, i.e. the net tax value of the transferred fixed assets of the transferring company becomes the initial net tax value of these fixed assets for the receiving company;	N/A.

(c) under the general rules for carry over of losses, the receiving company is entitled to take over the losses of the transferring company incurred in the previous tax periods that are related to the transferred branch of activity. In order to converse a permanent establishment into a resident subsidiary, the receiving company may undertake a partial division and transfer the received branch of activity to a new company (the subsidiary). The above described tax regime for the transfer of assets will be applicable also for the partial division.	

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> Latvia follows the concept of worldwide taxation of the residents and generally applies tax credit system. However, some double tax treaties provide for the exemption method. The tax credit is available only on actually paid taxes in the foreign country. The provisions of Article 10(2) of the Merger Directive have not been implemented in the Latvian legislation. The application of tax credit in the described situation is unclear therefore the lack of a notional tax credit might be contrary to the Directive.	Sec.3 (1) CITA Sec. 16 (1) CITA

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
<u>10.4 Tax deferral</u> No influence has been made on the Latvian legislation implementing the Merger Directive as a result of Case Law.	N/A.

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
<u>10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies</u> Article 10a of the Merger Directive has not been implemented in the Latvian legislation (see also 3.2).	N/A.

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit See 10a.1.	N/A.

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit See 10a.1.	N/A.

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders See 10a.1.	N/A.

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company See 10a.1.	N/A.

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
<u>10b.1 Exit taxation</u> The transfer of the registered office of an SE would not give rise to exit taxation under the Latvian legislation.	N/A.

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
<u>10b.2 The term 'head office'</u> According to Sec. 6 of SEA, the head office of the European company is defined as the address of the location of the administration of the SE.	Sec. 6 SEA

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
<u>10b.3 Head office and tax residency</u> <u>10b.3.1 Concept</u> <u>10b.3.1.1 Tax residency under domestic law</u> According to the TDA, for the purposes of tax legislation, a taxpayer which is not a natural person shall be considered a resident, if it is established and registered or if it should have been established and registered in accordance with the laws of the Republic of Latvia (see 3.3.1). <u>10b.3.1.2 Tax residency under Double tax conventions</u> The double tax conventions concluded by the Republic of Latvia generally do not provide one tiebreaker criterion for the tax residency of corporations. There are two main criteria – place of effective management and place of incorporation. However, the Double tax conventions provide	Sec. 14 (4) TDA Article 4 (3) of various Latvian double tax conventions

for any other criteria of similar nature to be used as tiebreaker criterion for tax residence qualification. There is no hierarchy between the different criteria mentioned. Where by reason of tax residency on grounds of place of management, place of incorporation or any other criterion of a similar nature person other than an individual is resident of both Contracting States, the competent authorities shall endeavour to settle the question by mutual agreement. In absence of such agreement, for the purposes of the double tax convention, the person shall not be entitled to claim any benefits provided by the convention. 10b.3.2 Conclusion Generally, the concept of 'head office' does not coincide with the criteria to determine the tax residence. According to the Latvian legislation, the main criterion for tax residence is the place of incorporation of the company.	

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
10b.4 Assets and liabilities not effectively connected with a permanent establishment The relief is not granted in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred, this would be deemed disposal of assets at fair market value and taxed accordingly. The taxation of the assets not effectively connected with the permanent establishment complies with Article 10b of the Merger Directive. However, in our view it might be contrary to EU Treaty freedoms.	Sec. 13 (3^1) CITA

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
10b.5 Tax deferral There have been no specific amendments or administrative guidance in respect of the legislation implementing the Merger Directive as the result of Case Law. See also 10b.4.	N/A.

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
<u>10c.1 The term 'comparable circumstances'</u> According to the general rules of the CITA, the losses may be carried forward for a period of next five tax periods (five years). The provisions of the CITA enacting the Merger Directive provide that the losses of an SE or an SCE may be offset chronologically against the taxable income of the permanent establishment as from the tax period when the losses were calculated to the relevant SE or SCE. Accordingly, the change of the tax status has no impact on the availability of Latvian tax loss carry forward of the SE or the SCE. However, the CITA prescribes special rules in case the ownership of the company has changed. Namely, if during a tax period control of the company is acquired by a person or a group of persons that previously did not control such company, tax losses of previous tax periods of such company shall not be covered in the tax period or in subsequent tax periods. For the purposes of the above-mentioned requirements, it should be considered that a person controls another person if the first owns, directly or by way of participation in one company or in several companies, more than 50% of all the shares issued by the other person and they have more than 50% of all the votes of shareholders (owners of shares), as may be counted in any voting. In order to qualify for the tax loss carry-forward criteria the legal entity is required to keep the basic economic activity it was engaged in during the two year period before the change in the controlling owners. This economic activity has to be kept for the next five years after the change in the controlling owners to retain rights to transfer tax losses from previous taxation years. If the legal entity had more than one economic activity during the two year period before the change in controlling owners, the basic activity is assumed to be the one that represents the biggest part in the turnover of the legal entity. If the legal entity changes its basic activity during this five year period, it loses the opportunity to cover the losses during the five year period after the change in the controlling owners. Moreover, the legal entity has to recalculate taxable income for the period after the change in the controlling owners. Increased and unpaid amount of tax is treated as a late payment, therefore, based on the TDA late payment penalties are calculated on the amount of unpaid taxes.	Sec. 14 (1^2) (2) (3) CITA Clause 114, 115 Reg. No 556

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
<u>10c.2 Loss recapture for permanent establishments</u> No specific rules in respect of losses attributable to a permanent establishment in a third Member State are implemented in the Latvian legislation. As a result of the Case *Marks & Spencer plc*, the CITA has implemented the provisions regarding the transfer of losses within the group of companies under the condition that a non-resident has exhausted the possibilities available in its state of residence of having the losses taken into account. However, the CITA does not provide clear rules regarding the offset of losses of a Latvian company derived from its permanent establishment located abroad, if there is no group of companies.	Sec. 14^1 CITA

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>10d.1 Deemed liquidation</u> According to the Latvian legislation, the transfer of registered office of an SE/SCE would not be considered to give rise to a deemed liquidation.	N/A.

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>10d.2 Tax treatment of third country residents</u> The transfer of registered office of an SE/SCE would not give rise to the taxation of the shareholders irrespective of their residence.	N/A.

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
11.1 Transposition of anti-abuse provisions Anti-abuse provisions (Article 11 (1) (a) of the Merger Directive) have been implemented only regarding the transfer of registered office of an SE or an SCE: The relief is not available in case of the transfer of the registered office of an SE or an SCE, if it is determined that the main purpose of the transfer of registered office or one of the main purposes is not to pay taxes or to avoid the payment of taxes. If the transfer of registered office is not carried out for valid commercial reasons, this may lead to an assumption that the main purpose or one of the main purposes of the transfer of registered office is not to pay taxes or to avoid the payment of taxes. There is no praxis relating the application of this anti-avoidance legislation. According to the CITA, the following tax benefits would be withdrawn after the transfer of registered office of SE/SCE from Latvia: (a) the carry over of tax values of fixed assets connected with the permanent establishment of SE/SCE in Latvia, (b) the carry over of tax losses by the permanent establishment of SE/SCE in Latvia; (c) the carry over of provisions and reserves by the permanent establishment of SE/SCE in Latvia.	Sec. 26^1 CITA

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
11.2 General anti-abuse provision The tax administration may apply also general anti-abuse provisions defined in the TDA. According to the provisions of the TDA, the tax evasion is considered to be the deliberate provision of false information in tax returns, the non-submission of tax returns, informative returns or requested information necessary for tax administration and control, unlawful application of tax	Sec. 1 (14) TDA

relief, tax benefits or tax allowances or any other deliberate action or inaction the result of which is that the taxes are not paid in due amount.	

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' The concept of 'wholly artificial arrangement' has not implemented in the Latvian legislation.	N/A.

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions The relief will not be applied if the securities of the receiving company which have been received by the transferring company are not in its ownership at least three years after the transfer thereof, unless the transferring company justifiably proves that the alienation of such securities has not been performed for the purpose of reducing its taxable income and not to pay the taxes payable in Latvia or to reduce the amount thereof (see also 4.4, first paragraph).	Sec. 6^2 (4) CITA

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' The concept of 'valid commercial reasons' has not been interpreted in the Latvian legislation. The examples for 'valid commercial reasons' such as restructuring or rationalization of the activities have not been implemented in the Latvian legislation.	Sec. 26^1 (2) CITA

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof Generally, according to the APL, the initial burden of proof shall have the tax authority. However, in relation to the specific anti-abuse provisions (see 11.4) the burden of proof is with the taxpayer.	Sec. 150 (1) APL Sec. 6^2 (4) CITA

LITHUANIA

Abbreviations

English	Lithuanian	English	Lithuanian
CIT	PM	Corporate Income Tax	Pelno mokestis
Law on CIT	PMĮ	Law on Corporate Income Tax	Pelno mokesčio įstatymas
OF	VŽ	Official Journal	Valstybės žinios
GAAP	VAS	Generally Accepted Accounting Principles	Verslo apskaitos standartai
CC	CK	Civil Code	Civilinis kodeksas
MD		Merger Directive	Direktyva 90/434/EEB
SE		Societas Europaea	Europos bendrovė
Law on Companies	ABĮ	Law on Companies	Akcinių bendrovių įstatymas
Law on SE	EBĮ	Law on Societas Europaea	Europos bendrovių įstatymas
STI	VMI	State Tax Inspectorate	Valstybinė mokesčių inspekcija
Law on TA	MAĮ	Law on Tax administration	Mokesčių administratvimo įstatymas
OC	Komentaras	Official Commentary	Apibendrintas mokesčio įstatymo komentaras

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
<u>Overall state of implementation</u> The Merger Directive has been implemented in the Law on CIT as of December 29, 2001 (Official Journal 2001, No. 110-3992), which came into force on January 1, 2002. Amendments of the Merger Directive as of February 17, 2005 were followed by the amendments of the Law on CIT as of December 25, 2005, which came into force on January 1, 2006. The latter law implemented the amendments of the Merger Directive as well as made corrections to the previous implementation. An official commentary of the Law on CIT implementing the Merger Directive is prepared by the State Tax Inspectorate under the Ministry of Finance of the Republic of Lithuania. Although the commentary is not legally binding, it expresses an opinion of a competent state authority regarding the application of the Law on CIT. A taxpayer has also a right to seek for an individual consultation of the tax authorities on a specific tax issue, but there is no obligation to follow the tax advice provided. The tax consultation does not bind the tax authorities. However if a taxpayer violates the law due to a faulty tax consultation, it may serve as grounds for the release from penalties.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> Provisions of the Law on CIT regulating the recognition of income and losses in cases of mergers, divisions, partial divisions, transfers of assets, exchanges of shares and transfer of registered office are applicable both to the entities and their shareholders (i.e., parent companies) provided that the transfer of assets, rights and obligations takes place between (1) the Lithuanian entities or (2) the Lithuanian entities and foreign entities which take on one of the forms of business organisation listed in the Annex to the Merger Directive and are resident in a Member State for tax purposes as well as between (3) the said foreign entities.	Law on CIT, Article 41.1

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
<u>1.2 Foreign Member State and third State merger</u> Following the amendments to the Law on CIT national legislation is applicable even if the transfer of assets, rights and obligations takes place between foreign entities which take on one of the forms of business organization listed in the Annex to the Merger Directive and are resident in a Member State for tax purposes. Benefits of the Merger Directive are not applicable under the Lithuanian law if one of the merging companies is from a third (non-EU) State. It is not explicitly stated in the Law on CIT or in the official commentary whether the national legislation would be applicable if a transaction involved two companies from Member States and a company from a third state. There has also been no practice on this issue yet. As national legislation is only applicable in certain cases when all the conditions, including residence of the companies involved, are met, in our opinion, national legislation will not be applicable in the situation described. It shall not be an infringement of the Directive as the Directive according to the Article 1(a) should be applied to mergers, divisions, partial division, transfer of assets and exchange of shares of qualifying companies only.	Law on CIT, Article 41.1

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
<u>2.1 The term 'securities'</u> An exchange of 'securities' under the Lithuanian implementing legislation encompasses exchange of shares (securities in limited liability companies), interests (securities in cooperative companies) and member shares (securities in partnerships).	Law on CIT, Article 41

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' Following the Law on CIT, cash payments not exceeding the nominal value of shares may only be allowed to cover the difference in the price of the shares exchanged. However, the Law does not refer to the calculation basis of cash payments allowed. In practice cash payments are made in order to avoid the situation where a fraction of a share would need to be issued. Taking into consideration the company law regulating company mergers, divisions and partial divisions, it shall be concluded that possibility of a 10% cash payment is more likely to be applied per shareholder basis and the shares of all shareholders must be exchanged. With respect to the aforementioned, it may be assumed that the cash buy-out of minority shareholders is not allowed.	Law on CIT, Article 41 Law on Companies, Article 67.5

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger In addition to the types of merger listed in the Merger directive, the Law on CIT provides for a partial division allowing a partial transfer of assets, rights, and obligations not constituting a branch of activity as well as separation of the shareholders (in case of non pro rata share issue). Under the Law on CIT a tax relief shall be applicable where a entity without being dissolved transfers one or more parts of its assets, rights, and obligations to one or more entities and divides all its assets, rights and obligations in proportion to the number of the shares left in the transferring entity and shares transferred to the receiving entity. Tax relief under partial division is provided both to Lithuanian and foreign entities.	Law on CIT, Article 41.2.8

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares Following the wording of the Law on CIT, an exchange of shares covers the exchange where an entity seeks to obtain the control over another entity (i.e. a holding of shares conferring 2/3 or more of the voting rights) as well as a subsequent exchange that may consolidate the control. Since the Law is explicitly referring to the purpose and not to the result in the control, it may be reasonably assumed that each successive exchange of shares contributing to the build-up of the control shall be covered by the relief if they are part of the same operation with the expressed purpose to achieve the control. The burden of proof that acquisition of stake was done with the purpose to acquire the control lies within the taxpayer. Moreover, it should also be noted that the term 'majority' was implemented in national law as meaning the holding of shares conferring 2/3 or more of the voting rights, not the majority but the control of a company. In our opinion the aforementioned threshold is incompliant with the provisions of the Merger Directive.	Law on CIT, Article 41.2.7

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
2.5 Consolidation of qualifying holding Further exchange of shares that consolidates an existing holding is granted a relief, no additional conditions apply.	Law on CIT, Article 41.2.7

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00'*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
2.6 The term 'branch of activity' The Law on CIT defines a 'branch of activity' as assets, rights and obligations which from an organizational point of view constitute an independent business, that is to say an entity capable of functioning by its own means.	Law on CIT, Article 41.2.5 OC

Following the Official Commentary as well as individual explanations of the tax authorities, a 'branch of activity' is interpreted as a whole of tangible and intangible assets together with rights and liabilities related to these assets (i.e. liabilities to suppliers, liabilities to employees, permissions, licenses, technologies, customer and supplier lists etc.) which allow to identify a 'branch of activity' and to exclude it from the activity of the company as an independent entity. Also a branch of activity should provide a basis to pursue the transferred activity in the acquiring entity independently. Though Case C-43/00 '*Andersen og Jensen'* clarifies that the independent operation of business must be assessed primarily from a functional point of view – the assets transferred must be able to operate as an independent undertaking without needing to have additional resource, however the tax authorities tend to disregard the functional aspect and asses existence of an independent business by the organizational structure of the company, i.e. separate subdivision is required to be in place. Moreover, the tax authorities tend to argue that a 'branch of activity' needs to include all possible elements (assets, liabilities to suppliers, liabilities to employees, financial liabilities) even if some of the elements are not relevant to the business activity in questions. In practice it often leads to exclusion of certain activities, for example, lease or trading of securities from the application of the benefits of the Merger Directive. Such practice, in our opinion, is not consistent with the provisions of the Directive.	

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> According to the Law on CIT the benefits of the Merger Directive is applied to entities resident in EU Member States listed in the Annex only, however application is extended to other types of Lithuanian legal entities. The extension of the Directive benefits to Lithuanian entities but not to any other foreign entity not listed in the annex.	Law on CIT, Article 41.1

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>3.2 Transparent entities</u> There is no concept of transparent entities in Lithuanian tax legislation.	N/A.

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency Under the Law on CIT, a legal person is considered to be a tax resident in Lithuania if it is incorporated in Lithuania. Usually the tax residency tiebreaker criterion is not specified in the double tax conventions concluded by Lithuania and the residency is subject to the mutual agreement of the competent authorities.	Law on CIT, Article 2.2

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject-to-tax clause Lithuanian Law on CIT gives a reference to the Merger Directive in order to implement the subject-to-tax clause. No specific guidance has been issued. However the obligation to have documents sufficient to prove that a company is subject-to-tax lies with the taxpayer. According to the Official Commentary, a certificate confirming that the company is subject-to-tax issued by the foreign tax authority is expected in such cases. The certificate shall include a name of the tax payer, tax payer's code and the confirmation that it is subject-to-tax. According to the Official Commentary a foreign entity incurring losses shall meet the requirements of the subject-to-tax clause.	Law on CIT 41.1 OC

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
3.5 Shareholder requirements No limitations for the companies owned or controlled by EU or EEA nationals or residents are applicable under the Law on CIT.	N/A.

Article 4 – Carry over of balance sheet value

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1) (a)) been interpreted and transposed into your national legislation?	Reference
4.1 The concepts of 'real values' and 'value for tax purposes' The Law on CIT does not directly refer to the concept of real values. However it is stated that any increase in the value of assets in case of the mergers, divisions, partial divisions, transfers of assets, exchanges of shares or transfer of registered office shall not be included in the taxable income of the acquiring entity. The 'value for tax purposes' in the Law on CIT is referred to the 'acquisition price of assets', i.e., the acquisition price of such assets with respect to the receiving entity shall be the acquisition price of the assets before the transfer was effected. The receiving entity shall continue to calculate the depreciation or amortisation of such assets according to the rules applied by the transferring entity before the transfer was effected. The 'acquisition price of assets' in the Law on CIT is defined as all expenses incurred in the course of acquiring assets, including the commissions and taxes (levies) paid, except for VAT, in connection with the acquisition of such assets.	Law on CIT, Article 42, 14.1

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions There is no specific guidance for divisions/partial divisions. The same provisions apply, i.e., if in the case of a division, partial division an entity transfers assets to the other entity, the receiving entity continues to calculate the depreciation or amortization of such assets according to the rules applied by the transferring entity before the transfer was effected.	Law on CIT, Article 42

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' The term "effectively connected" has not been transposed into the Lithuanian tax legislation. The law on CIT refers to all assets, rights and obligations that are transferred in case of the merger. A merger is granted a relief only if a foreign acquiring entity continues to carry on its activities through a permanent establishment in the territory of Lithuania on the	Law on CIT, Article 41.3, 2.18

basis of the assets, rights and obligations acquired. The term 'permanent establishment' is defined in the Law on CIT as expression of activities of a foreign entity in Lithuania. A foreign entity is deemed to carry on its activities through a permanent establishment if it: permanently carries on its activities in Lithuania; or carries on its permanent activities through a dependent representative (agent); or uses a building site, a construction, assembly or installation project in Lithuania; or makes continuous use of installations or structures in Lithuania for prospecting or extracting natural resources, including wells or vessels used for that purpose.	

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
<u>**4.4 Limitation of the scope of relief**</u> The scope of relief is not limited in Lithuania, i.e. the receiving entity is obliged to calculate the depreciation or amortization of such assets received according to the rules applied by the transferring entity before the transfer was effected.	Law on CIT, Article 42.8

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
<u>**4.5 Assets and liabilities not effectively connected with a permanent establishment**</u> Please see 4.3. If a foreign acquiring entity does not continue to carry its activities through a permanent establishment in Lithuania on the basis of all assets and liabilities transferred, a merger, division or partial division is not subject to tax relief, i.e. no reallocation of assets is allowed and gain or loss is computed and taxed the same as if all assets had been sold at a fair marker value.	Law on CIT, Article 41.3

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
<u>**4.6 Tax treatment of shares of the receiving company**</u> There is no specific reference in the Law on CIT, however taking into consideration that according to the law the increase in the value of assets are not treated as taxable income, it may be reasonably assumed that any gains accruing to the receiving company upon the cancellation of its holding in the capital of the transferring company shall not be recognized for tax purposes.	Law on CIT, Article 42.2

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral There is no exit taxation in the Lithuanian tax system.	N/A.

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities There is no concept of transparent entities in the Lithuanian legislation.	N/A.

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief According to the Law CIT, division, partial division, transfer of assets, and exchange of shares is subject to tax relief only if an entity or its members do not sell or otherwise transfer the ownership of securities (including the merger) received by the means of an exchange for a period of 3 years, except for the subsequent cases of division, partial division, transfer of assets and exchange of shares. We believe that this limitation was set on the basis of the Article 11(1)(a) of the Merger Directive and it is not an infringement of the Directive.	Law on CIT 42.10

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
5.1 The term 'provisions and reserves' The terms provisions and reserves are only defined in the accounting standards. According to the standards a reserve is a set up to limit distribution of profit committed to the purposes set by the owners of the company. A provision is a liability, the amount or maturity of which can not be defined exactly but which can be measured reliably. However, in practice provisions or reserves are carried over without any restrictions as under the Law on CIT the receiving company takes over not only assets and liabilities but also the rights and obligations of the transferring company.	N/A.

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments Article 5 of the Directive has not been implemented separately in the Lithuanian legislation. However, transfer of provisions and reserves is subject to the same rules as transfer of all other assets, rights and obligations.	N/A.

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves Please see 5.2.	N/A.

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves N/A.	N/A.

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry-over of losses The on CIT defines 'loss' as a negative result from deducting non-taxable income, allowable deductions and deductions of limited amounts from income during the fiscal year. Carry forward of the tax losses (excluding losses from transfer of securities and derivative financial instruments) is unlimited. Carry forward of losses resulting from transfer of securities and derivative financial instruments is limited to 5 years. Following the provisions of the Law on CIT the receiving company is allowed to take over the tax losses of the transferring company which had not yet been exhausted for tax purposes (excluding losses from transfer of securities and derivative financial instruments). However the receiving company is only allowed to take over the losses related to the branch of activity transferred provided that it continues such activity for a period not shorter than 3 years. If one of the entities involved is a financial institution, the receiving entity is allowed to take over the losses resulting from transfer of securities and derivative financial instruments which had not yet been exhausted for tax purposes. As no exceptions are explicitly stated in the law it should be assumed that the same limitations apply to domestic as well as cross border situations. According to the proposed official commentaries to the Law on CIT, the tax losses related to the branch of activity transferred shall be calculated with respect to the criteria set in the accounting (management accounting) policy (i.e. taking into consideration income and direct and indirect costs attributable to the transferred activity) and provisions of the Law on CIT.	Law on CIT, Article 30.1., 43 OC

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment The rules indicated in 6.1 are equally applied to Lithuanian and foreign entities. Since the foreign entity as the receiving entity is required to continue its activities in Lithuania through the permanent establishment, it may take over the tax losses of the transferring company which had not yet been exhausted for tax purposes and offset such losses with the future income of its permanent establishment in Lithuania.	Law on CIT, Article 43.1

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
<u>6.3 Specific legislation for divisions/partial divisions/transfer of assets</u> In the cases of partial division, the transferring entity shall reduce its tax losses which had not yet been exhausted for tax purposes with the amount of losses taken over by the receiving entity. According to proposed commentaries and official commentaries to the Law on CIT, the transferring and receiving entities may agree if the losses are taken over by the receiving entity or will remain in the transferring entity. In the case of exchange of shares entities shall continue carrying over their losses.	Law on CIT, Article43.3, 43.4 OC

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
<u>6.4 Further conditions for carry over of losses</u> In addition to the requirements listed in 6.2, if after 3 year period the receiving entity discontinues transferred branch of activity, the receiving entity shall have no right to the further carry forward of losses starting from the tax period in which the activity was discontinued.	Law on CIT, Article 43.1

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
<u>7.1 Amended holding threshold</u> The holding threshold has not been set in the Lithuanian national legislation as there is no specific implementation of Article 7 of the Merger Directive in Lithuanian laws, but according to the provisions of the Law on CIT, such capital gain is not taxable.	N/A.

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses On the basis that the decrease in the value of assets shall not be recognized for the CIT purposes, it may be reasonably assumed that any loss accruing to the receiving company upon the cancellation of its holding in the capital of the transferring company shall not be recognized.	Law on CIT, Article 42.2

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder Generally, the Law on CIT does not eliminate economic double taxation in most cases of merger, division or partial division as it provides that (1) the acquisition price of such of assets transferred with respect to the receiving entity shall be the acquisition price of the assets before the transfer was effected and (2) the acquisition price of the new shares (interests, member shares) received by the members of an entity is the acquisition price of the shares (interests, member shares) exchanged before the transfer was effected. This may not result in double taxation since many disposals of shares by companies are exempt under substantial shareholding exemption; however this exemption is not applicable to individuals. If the exemption is applicable no tax would be due on the subsequent disposal of shares in the transferee company but the subsequent disposal of the underlying assets would be subject to tax. According to the official commentaries on the Law on CIT, economic double taxation is eliminated in the case of exchange of shares as the acquisition price of the shares (interests, member shares) received by the acquiring entity is deemed to be the price of issue of the shares. The price of issue is the market value of the shares.	Law on CIT, Article 42.1 OC

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
8.2 Computation of the capital gain All cash payments that are made on the merger, division, partial division or exchange of shares are treated as the income of the shareholder and are taxed according to the general provisions of the Law on CIT.	Law on CIT, Article 42.11

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
8.3 Further conditions for tax relief Please see 4.9.	Law on CIT, Article 42.10

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
9.1 Avoidance of economic double taxation at the level of the transferring company Please see 8.1. There is no guidance what shall be considered to be the value shares received due to the transfer of assets.	Law on CIT, Article 42.2

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
9.2 Further conditions for tax relief Please see 4.9.	Law on CIT, Article 42.10

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
9.3 Tax deferral N/A.	N/A.

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
10.1 Loss recapture for permanent establishments in third Member States Article 10(1) is not directly transposed into Lithuanian legislation. There are no loss recapture rules in the Lithuanian taxation.	Law on CIT, Article 30.5

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
10.2 Permanent establishment in the Member State of the receiving company Article 10 (1) is not directly transposed into Lithuanian legislation and the compliancy remains doubtful. Following the provisions of the Law on CIT, the merger, division or partial division is granted a relief only if a foreign acquiring entity on the basis of the assets, rights and obligations acquired continues to carry on its activities through a permanent establishment in the territory of Lithuania. There is no guidance if the indicated requirements shall be applicable where assets, rights and obligations transferred include a permanent establishment of the transferring company which is situated in a Member State other than that of the transferring company. In our opinion, this requirement has no economic sense and should not be applicable in the cases when the permanent establishment transferred was in another Member State. Where the assets transferred in a merger, a division, a partial division include a permanent establishment, that permanent establishment shall not be taxed.	Law on CIT Article 42.3, 42.4, 42.5

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
10.3 Concept of worldwide taxation/tax credit system Lithuania applies worldwide taxation system. However where in the cases of the merger, division or partial division a Lithuanian entity transfers a branch of activity in a Member State of the European Union to a foreign entity, the increase in the value of assets is not treated as income of the transferring entity.	Law on CIT, Article 42.4

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
10.4 Tax deferral N/A.	N/A.

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies There is no concept of fiscally transparent in the Lithuanian legislation.	N/A.

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit N/A.	N/A.

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference

10a.3 Determination of notional tax credit N/A.	N/A.

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders N/A.	N/A.

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company N/A.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation No exit taxation applicable.	N/A.

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' Following the Law on Societas Europaea, the 'head office' is understood as the place where management or administrative organ of the SE is located.	Law on SE, Article 4.1.

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
<u>10b.3 Head office and tax residency</u> As defined in 3.3 tax residency is determined upon the place of incorporation/registration.	Law on CIT, 2.2

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>10b.4 Assets and liabilities not effectively connected with a permanent establishment</u> The term 'effectively connected' has not been implemented in the Lithuanian tax legislation. Law on CIT refers to all assets, rights and obligations that are transferred in case of the merger. A merger is granted a relief only if a foreign acquiring entity on the basis of the assets, rights and obligations acquired continues to carry on its activities through a permanent establishment in the territory of Lithuania.	Law on CIT, Article 41.3

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
<u>10b.5 Tax deferral</u> There is no exit taxation in Lithuania.	N/A.

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
<u>10c.1 The term 'comparable circumstances'</u> The term 'comparable circumstances' was not defined in Lithuanian legislation. According to the provisions of the Law on CIT the entity continuing activities in Lithuania through the permanent establishment after the transfer of its registered office shall have a right to carry forward all the losses which had been incurred and had not been exhausted for tax purposes.	Law on CIT, Article 43.1

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
<u>10c.2 Loss recapture for permanent establishments</u> There are no loss recapture provisions.	N/A.

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>10d.1 Deemed liquidation</u> There is no deemed liquidation from a tax perspective in the Lithuanian legislation.	N/A.

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>10d.2 Tax treatment of third country residents</u> There is no difference in treatment for EU and non-EU shareholders.	N/A.

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 *'Leur-Bloem'* and C321/05 *'Kofoed'*. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 *'Cadbury'*. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> The abovementioned Article has not been transposed into the Law on CIT. However the mergers, divisions, partial divisions, transfers of assets, exchanges of shares and transfer of registered office should be subject to general anti – avoidance provisions.	Law on TA, Article 69.1

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
<u>11.2 General anti-abuse provision</u> In the cases listed in the Article 11 of the Merger Directive, the tax administrator would apply general anti–avoidance rule, substance over form principle, as stated in the Law on TA, i.e. in cases where a taxpayer's transaction, economic operation or any combination thereof is concluded purely with objective to achieve a tax benefit. i.e., without any valid commercial reasons. In this instance, the tax administrator shall apply the substance-over-form principle for the purpose of calculating the tax. In this case, the tax administrator shall not take into account formal expression of the taxpayer's activity and will recreate the distorted or hidden circumstances associated with taxation as provided for in tax laws and calculate the tax pursuant to the relevant provisions of the said tax laws.	Law on TA, Article 69.1

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
<u>11.3 The concept of 'wholly artificial arrangement'</u> 'Wholly artificial arrangement' falls within the meaning of 'cases where a taxpayer's transaction, economic operation or any combination thereof is concluded purely with objective to achieve a tax benefit'.	Law on TA, Article 69.1

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
<u>11.4 Specific anti-abuse provisions</u> According to the Law on CIT, division, partial division, transfer of assets, and exchange of shares is subject to tax relief only if an entity or its members do not sell or otherwise transfer into ownership the shares (interest, member shares) received by means of an exchange for a period of 3 years, except for the subsequent cases of division, partial division, transfer of assets and exchange of shares. Although there is no specific reference, in our opinion, this limitation was set in reliance on Article 11(1)(a) and it is not an infringement of the Directive.	Law on CIT, Article 42.10

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' The concept of 'valid commercial reasons' concept has not been defined in the legislation or interpreted by the Tax Authorities.	N/A.

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof According the Law on TA, the tax administrator must substantiate the tax and related amounts calculated in respect of the taxpayer. Where the taxpayer disagrees with a specific tax and related amounts calculated by the tax administrator, he must substantiate the incorrect calculation thereof. The initial responsibility to provide proof falls on the tax administrator.	Law on TA, Article 67.1

LUXEMBOURG

Abbreviations

English	French/German	English	French/German
ITL	LIR	Income Tax Law	Loi de l'impôt sur le revenu
DTC		Double Tax Convention	
MD		Merger Directive, as modified	
AL	StAnpG	Adaptation Law	Steueranpassungsgesetz
CIT		Corporate Income Tax	

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
<u>Overall state of implementation</u> The following laws and administrative circulars implemented the MD: (a) law of December 20, 1991, which became effective on January 1st, 1992; (b) law of December 21, 2001, which became effective on January 1st, 2002; (c) parliamentary commentaries n°4855 to the draft law of December 21, 2001 are used as guidance for the interpretation of the law; (d) circular 22bis-1 ITL of November 27, 2002; (e) circular 59bis-1 ITL of February 12, 2003; (f) law of December 21, 2007, which became effective on January 1st, 2007; and (g) parliamentary commentaries n°5708 to the draft law of December 21, 2007 are used as guidance for the interpretation of the law.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> The expression 'in which companies from two or more Member States are involved' has not been explicitly interpreted when the MD was implemented under Luxembourg Law. The Law that implemented the MD refers to mergers, divisions, partial divisions and transfers of assets between a Luxembourg resident company and a company resident in an EU Member State other than Luxembourg irrespective of who their parent companies are. (Article 170bis, 170ter, 171 ITL) In the case of an exchange of shares with a Luxembourg resident entity as parent company of the acquired company, the acquired company and the acquiring company could be from the same Member State or even from a	Article 170bis, 170ter, 171 and 172 ITL Article 22bis (2) No. 4 ITL

third State or States. (Article 22bis (2) No. 4 ITL) As a general rule, the provisions implementing the MD apply under Luxembourg law to merging companies from a third State if this third State is a Member State of the European Economic Area and if the companies are capital or cooperative companies fully subject to a tax which is comparable to the CIT. For an exchange of shares to be tax-neutral for the shareholders of the acquired company, the acquired and acquiring companies should also be capital companies fully subject to a tax comparable to the Luxembourg CIT, wherever their place of residence is.	

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
<u>**1.2 Foreign Member State and third state merger**</u> (a) 1st question: Please see 1.1. (b) 2nd question: Under Luxembourg law in case of the transfer, in the framework of a merger or division, of a permanent establishment located in Luxembourg, such transfer can be done at book values. The transferring company and the transferee entity could be in the same foreign Member State (Article 172(4) ITL). In case of an exchange of shares where the parent company of the acquired is a Luxembourg resident entity, the acquired company and the acquiring company could be in the same foreign Member State (Article 22bis (2) ITL).	Article 172 (4) ITL Article 22bis (2) ITL Article 22bis (1) ITL

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
<u>**2.1 The term 'securities'**</u> The term 'securities' has not been defined or interpreted in implementing Luxembourg law. It has been transposed under Luxembourg law under the same term as the one used in the MD, i.e. 'securities representing the capital'.	Article22bis ITL Article 170bis ITL Article 170ter ITL Doc.parl.5708 p.12

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' The possibility to allow 10% cash payment for reorganization at book value has been implemented in Luxembourg law concerning mergers. In the case of a division of a company resident in Luxembourg the Luxembourg tax law provides for the possibility of a 10% cash payment. As for the case of a division of a company resident in a Member State other than Luxembourg the provisions of Article 170ter (1) ITL applicable to the merger of a company resident in an EU Member State apply in a corresponding way. An exchange of shares is allowed to be tax-neutral for the shareholder of the transferring company that receives shares of the receiving company, both in the case of a merger and a division with a 10% cash payment being accepted (explicit implementation for exchanges of shares as a result of mergers and divisions, partial divisions). Where a cash payment is specifically allowed, Luxembourg tax law implemented the wording of the Merger Directive.	Article 170bis (1) and (2) ITL juncto Article 170 ITL Article 170ter (1) and (2) ITL Article 22bis (3) ITL

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger Luxembourg law does not cover other types of merger.	Article 170bis and 170ter ITL

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares Luxembourg law grants relief in respect of the exchange that finally leads to the acquisition of a majority holding and in respect of each successive exchange of shares that consolidates an existing majority holding.	Article 22bis (2) 4 ITL

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
2.5 Consolidation of qualifying holding With regard to an exchange of shares that consolidates an existing majority holding, the grant of relief is not subject to any specific conditions.	Article 22bis (2) 4 ITL

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
2.6 The term 'branch of activity' In implementing the concept 'branch of activity', Luxembourg law did not refer to this term itself but to the term 'business' (*enterprise*) and 'independent part of a business' (*partie autonome d'entreprise*) that were used for domestic operations before the implementation of the MD. According to a circular issued by the tax authorities, 'business ' or 'independent part of a business ' has the same meaning as 'branch of activity'. According to another circular issued by the tax authorities, the term ' business' applies to a commercial, agricultural or forest business and to the net assets used for a liberal profession. An 'independent part of a business' should be a more or less independent 'ensemble' but does not necessarily mean that this part can survive on its own, while the above case law would require that this part would have to be able to survive on its own. According to the circular, the transferring company should keep at least one other independent part of the business, i.e. the independent part of business is defined in reference to the transferring company and not to the transferee. When a business is transferred, its essential basis should be transferred; in order to know whether a transferred asset is part of the essential basis of a business, its use within the business should be analysed. If it appears to be necessary for the achievement of the purpose of the business, it is part of the essential grounds of the business. As the term 'independent part of business' is much broader than the interpretation of 'branch of activity' given by the ECJ in '*Andersen og Jensen*', the term used in Luxembourg should be compliant with the term used in the Merger Directive.	Article 170bis (3) ITL Article 172 (4) ITL Article 59bis ITL Circular ITL n°59bis/1 of February 12, 2003 Circular ITL n°59/1 of February 12, 2003

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> Luxembourg law applies the MD to all entities covered by Article 3 of the MD. Additionally, the benefits of a tax-neutral merger, division and partial division also apply to capital and cooperative entities of a Member State of the EEA (European Economic Area) that is not a Member State of the EU, if this company is fully subject to a tax corresponding to the Luxembourg CIT. The benefits for the parent company regarding the tax-neutral exchange of shares apply if the merging companies either: (a) are covered by Article 3 of the MD; or (b) are capital or cooperative entities of a Member State of the EEA that is not a Member State of the EU subject to a tax corresponding to the Luxembourg CIT; or (c) are any other capital company subject to a tax corresponding to the Luxembourg CIT.	Article 22bis (1) ITL

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>3.2 Transparent entities</u> Under Luxembourg tax practice, an entity is tax transparent on the basis of its legal features, compared to the legal features of domestic transparent entities. The analysis of whether a foreign entity is tax transparent for Luxembourg tax purposes is made on a case by case basis. As examples, the French '*société civile*' and the Dutch closed limited partnership (closed '*Commanditaire Vennootschap*') are usually considered transparent. However, in implementing the MD, Luxembourg law provided that any entities referred to in Article 3 of the MD (that is any entity listed in the Annex to the MD) would be treated as fiscally non transparent for Luxembourg tax purposes. As a result, none of the entities referred to in Article 3 of the MD is regarded as being transparent under Luxembourg law.	Article 175 ITL

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
<u>3.3 Qualification of tax residency</u> Under Luxembourg law, a company is tax resident in Luxembourg insofar as its statutory seat **or** its central administration is located in Luxembourg. Most DTCs entered into by Luxembourg follow the OECD Model Convention with regard to the rules concerning the determination of residence. Therefore, the place of effective management is the most common tax residence tie-breaker rule in the DTC concluded by Luxembourg.	Article 159 (1) ITL Doc.parl. 5708, page 16

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>3.4 Subject-to-tax clause</u> Luxembourg law refers directly to Article 3 MD to determine which entities should benefit from the national provisions. No further interpretation of the subject-to-tax clause of Article 3(c) MD can be found in the Luxembourg national legislation.	Article 22bis (1) ITL

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>3.5 Shareholder requirements</u> Luxembourg law does not limit the benefits of the MD to companies owned or controlled by EU or EEA nationals or residents.	Article 170 ITL, Article 170bis ITL

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>4.1 The concepts of 'real values' and 'value for tax purposes'</u> The concepts of 'real values' and 'value for tax purposes' as indicated by Article 4(1) of the Merger Directive have not been interpreted into Luxembourg legislation when the Merger Directive was transposed. The Luxembourg Law expressly states in Art. 170 (2) and (3) ITL (in connection with Art. 170bis and Art. 170ter ITL) that the profits realized	Article 170bis (1) and (2) ITL, Article 170 (1), (2) and (3) ITL Article 169 ITL

upon transfer are not taxed in the case of a merger, division or partial division between EU resident entities. Thereby the application of the rules regarding liquidation proceeds (Art. 169 ITL), which normally also apply in such cases (Art. 170 (1) ITL), is excluded. In Luxembourg liquidation proceeds are calculated by reference to the difference between the value ascribed to the assets of the company in the tax balance sheet (book value) upon transmission and the remuneration obtained in exchange (Art. 169 and 170(1) ITL). If there is no remuneration or if remuneration is not arm's length, the fair market value would apply. It is noted that the net assets available for distribution are the existing ones at the end of the fiscal year preceding the transfer computed as such for the purposes of calculating the CIT (Art. 169(5) ITL). Invested net assets refer to all the assets used in a commercial business (Conseil d'Etat, doc. Parl. 571-16, p.122, note 2 under Art. 170 ITL). Remuneration refers to any asset or consideration obtained in exchange for the invested net assets, including the profit realized upon cancellation of existing participations (note 6 under Art. 170 ITL). Although the concepts of 'real values' and 'value for tax purposes' have not been transposed as such into the Luxembourg Tax Law, the Luxembourg legislation is in compliance with the directive by completely exonerating the profits realized upon the transfer from Luxembourg taxation.	

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions No specific guidance has been issued in respect of divisions and partial divisions.	

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' The Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' have not been interpreted and implemented as such in the Luxembourg law implementing the MD. Reference has been made only to the term 'permanent establishment'. The parliamentary commentaries to the draft law indicate that upon a merger or division where the transferring company is a Luxembourg resident company, the receiving company holds a Luxembourg permanent establishment (doc.parl. 4855, p.41). In the same vein, these commentaries indicate that, upon a merger, the transferred assets stay	Doc.parl. 4855, ps.41 and 133.

connected to a permanent establishment (doc.parl. 4855, p.133).	

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
<u>**4.4 Limitation of the scope of relief**</u> Luxembourg law limits the scope of relief with a general provision according to which the transfer must be effected in such a way that transferred hidden reserves remain subject to ultimate Luxembourg taxation. No. 2 of Article 170 (2) ITL states that in order for the tax exemption to apply to the profit arising on the transfer, among other conditions, the transfer must be carried out in such a way that the profit that would have been taxable in Luxembourg, if no such provision existed, will be taxable there at a later date. Practically this could be achieved by transferring the assets of the acquired company to a Luxembourg permanent establishment of the acquiring company maintaining the book values of the acquired company. This provision is not applicable in case of a foreign permanent establishment transferred to an entity resident in a Member State that has concluded a DTC with Luxembourg.	Article 170bis (3) ITL, Article 170 (2) ITL

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
<u>**4.5 Assets and liabilities not effectively connected with a permanent establishment**</u> This is not considered under Luxembourg tax law. No. 2 of Article 170 (2) ITL states that in order for the tax exemption to apply to the profit arising on the transfer, among other conditions, the transfer must be carried out in such a way that the profit that would have been taxable in Luxembourg, if no such provision existed, will be taxable there at a later date (see 4.4). However, Luxembourg tax law does not explicitly consider that the transferred assets and liabilities are effectively connected with a permanent establishment. The law is therefore unclear as to whether assets/liabilities that do not remain connected with a permanent establishment would jeopardize the tax neutrality of the whole transfer, including that of the assets and liabilities connected to a permanent establishment, or whether this simply entails that a gain realized upon the transfer of these assets and liabilities that do not constitute a permanent establishment will be taxable. In our view, the result of this provision should be in compliance with the Directive.	Article 170 (2) No. 2 ITL

<table>
<tr><th>Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?</th><th>Reference</th></tr>
<tr><td>
<u>4.6 Tax treatment of shares of the receiving company</u>

A merger profit is tax exempt at the level of the receiving company if the profit can be allotted to shares of the receiving company in the transferring company and the receiving company holds a participation of at least 10% in the transferring company. Otherwise, the merger profit would be taxable, unless the Luxembourg participation exemption regime applies to this merger profit.

The Luxembourg participation exemption covers dividends, liquidation proceeds and capital gains.

In order for the exemption to apply, the parent company has to be:
(a) a fully taxable Luxembourg resident company; or
(b) a Luxembourg permanent establishment of either:
• a collective entity covered by Article 2 of the Parent-Subsidiary directive; or
• a capital company that is resident of a country with which Luxembourg has signed a tax treaty.

The subsidiary must be:
(a) a collective entity that is covered by Article 2 of the Parent-Subsidiary directive;
(b) a fully taxable Luxembourg resident company;
(c) a fully taxable non-resident company with capital company that is subject to income tax at a rate comparable to the Luxembourg corporate income tax.

The conditions for the participation exemption include a minimum participation of 10% (or a participation having a minimum acquisition price of EUR 1,200,000 to qualify for the dividends and liquidation proceeds exemption and EUR 6,000,000 to qualify for the capital gains tax exemption) and the retention of ownership of the participation for at least 12 months. A commitment to hold the minimum shareholding for an uninterrupted period of at least 12 months satisfies this condition.
</td><td>Article 171 ITL</td></tr>
</table>

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>4.7 Tax deferral</u> No particular account has been taken of the judgment in Case C-470/04 *'N'*.	

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
<u>4.8 Criteria to determine tax transparent entities</u> Please see 3.2. As any entity referred to in Article 3 of the Merger Dirctive is not considered as tax transparent under Luxembourg law, Article 4(2) of the Merger Directive did not need to be transposed in Luxembourg law.	Article 175 ITL

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
<u>4.9 Further conditions for tax relief</u> The relief under Article 4 of the Merger Directive has not been made subject to any conditions not set out in that Article. The Luxembourg Tax Law complies with Article 4 of the Merger Directive.	Article 170 (3)3. ITL

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>5.1 The term 'provisions and reserves'</u> Luxembourg law has not implemented any specific rules regarding provisions or reserves except for provisions in relation to pension payments. The content of provisions and reserves is codified in the Luxembourg commercial code, which generally is also decisive for the tax treatment, as the tax balance sheet is based on the commercial balance sheet in Luxembourg. As a general rule, under Luxembourg law, tax deferrals obtained by the transferring company before the merger or the division are transferred to the receiving company if the latter registers the transferred assets / liabilities at book value. The tax guidelines and the parliamentary	Article 170(4) ITL Note 12 under Article 170 ITL that refers to Articles 53 and 54 ITL. Doc.parl. 4855, p. 133 that refer to Articles 54 and 166 ITL.

commentaries provide for examples of such capital gains subject to tax deferrals. The Luxembourg Law therefore should be in compliance with the Merger Directive.	

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments The Luxembourg legislator has not made specific regulations with respect to provisions/reserves derived from foreign permanent establishments.	

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves See above under 5.2.	

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves N/A.	

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry-over of losses The concept of 'loss' has not been defined for the purposes of implementing Article 6. Article 6 of the MD has not been transposed under Luxembourg law since the latter does not allow the receiving company to take over the losses of the transferring company which has not yet been exhausted for tax purposes if the operations were conducted between Luxembourg companies.	Article 114 (2) 3. ITL

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment Luxembourg law does not provide for any specific method of allocation of losses to a permanent establishment. As a general rule, the profits or losses attributable to a permanent establishment would be calculated in accordance with the ITL relating to the calculation of business profits. In this respect, Luxembourg follows a balance sheet based taxation system for computing commercial profits, with profits or losses being computed by comparing the balance sheet at the end of the fiscal year with the opening balance sheet. As a general rule, the tax balance sheet should follow the commercial balance sheet, unless provided otherwise by tax law. If the permanent establishment prepares commercial accounts, these would normally be used as the basis for calculating its profits or losses.	Paragraph 16 of the adaptation law;

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets No specific legislation has been enacted.	

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses N/A.	

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Amended holding threshold The 10% holding threshold has been implemented under Luxembourg law by the law dated December 21, 2007 and is applicable as from the tax year 2007.	Article 171 (3) ITL

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses The treatment of losses has not been specified under Luxembourg law or administrative guidance. Luxembourg law refers to the profit of the receiving company that held a participation in the transferring company. The parliamentary commentaries to the law implementing the MD indicate that this profit corresponds to the difference between the fair market value (*'valeur d'exploitation'*) of the cancelled participation and its accounting value. In the parliamentary commentaries no indication as regards the treatment of losses that might occur in such transaction can be found.	Article 171 (3) ITL Doc.parl. 4855, p.135

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder Luxembourg tax law provides for the avoidance of economic double taxation, by not imposing that the shares received by the acquiring company from the shareholders of the acquired company are considered to have been received at accounting value.	Doc. Parl. 4855-3, pages 18 and 19.

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
8.2 Computation of the capital gain In the situation covered by Article 8(9), Luxembourg law indicates that the acquisition price of the shares received from the acquiring company by the shareholders of the acquired company (corresponding to the acquisition price of the shares given in exchange) should be reduced by the amount of the cash payment. The parliamentary commentaries indicate that the taxation of the whole capital gain is thus deferred until the future realization of the shares received from the acquiring company.	Article 22bis(4) ITL Doc.parl. 4855, page 95

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>8.3 Further conditions for tax relief</u> Relief under Article 8 has not been made subject to conditions not set out in that Article	

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>9.1 Avoidance of economic double taxation at the level of the transferring company</u> Strictly speaking, the provisions on transfers of assets do not provide for the avoidance of economic double taxation. However, economic double taxation would be avoided under the Luxembourg implementation of the Parent-Subsidiary Directive (please see 4.6).	Article 59bis ITL

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>9.2 Further conditions for tax relief</u> Luxembourg law only transposed Article 9 of the MD to the following situations: (a) where a Luxembourg resident entity transfers a business or part of a business to a Luxembourg permanent establishment of a company resident in a Member State other than Luxembourg; (b) where a Luxembourg resident entity transfers a permanent establishment located in another Member State to a company resident in a Member State other than Luxembourg; (c) where a company resident in a Member State other than Luxembourg transfers a business or a part of a business constituting a permanent establishment located in a Member State other than Luxembourg to a Luxembourg resident entity. (d) where a company resident in a Member State transfers a permanent establishment located in Luxembourg to a company resident in a Member State.	Article 59bis ITL Article 172 (4) ITL

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>9.3 Tax deferral</u> No account has been taken of the judgment in Case C-470/04 *'N'*.	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Loss recapture for permanent establishments in third Member States</u> Luxembourg tax law provides for loss recapture only in the case of a transferred permanent establishment located in a Member State with which Luxembourg has not concluded any tax treaty. This recapture rule applies in connection with the derogation of Article 10(2). Luxembourg applies a system of taxing worldwide profits. Article 10(2) has therefore been transposed, but only in the case of a Luxembourg resident entity transferring a permanent establishment located in a Member State with which Luxembourg has not concluded a DTC. In case the transferred permanent establishment has incurred losses prior to its transfer, up to the amount of the recaptured losses no tax relief (no notional tax credit) is given. Whereas, concerning the tax on the profits resulting from the transfer of the permanent establishment a notional tax credit is granted for the tax that, but for the provisions of the MD, would have been charged on those profits or capital gains in the Member State in which that permanent establishment is situated. In case of a permanent establishment located in a Member State with which Luxembourg has a DTC, based on Luxembourg's DTCs, the right to tax profits attributable to the permanent establishment would be allocated to the other contracting state and Luxembourg would grant an exemption.	Article 59bis (4) and 170bis (3) ITL Doc.parl. 4855, page 101 Article 2 (2) ITL

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> The provision referred to in the second bullet of 9.2 also applies if the permanent establishment is situated in the same Member State as the recipient company.	Article 59bis (1) No. 2 and (4) ITL

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
10.3 Concept of worldwide taxation/tax credit system Please see 10.1.	

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
10.4 Tax deferral No account has been taken of the judgment in Case C-470/04 '*N*'.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies In implementing the MD, Luxembourg law provided that any entities referred to in Article 3 of the MD (that is any entity listed in the Annex to the MD) would be treated as fiscally non transparent for Luxembourg tax purposes. As a result, none of the entities referred to in Article 3 of the MD is regarded as being transparent under Luxembourg law. As a result, Luxembourg law did not need to transpose Article 10a.	Article 175 ITL

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit See above under 10a.1.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit See above under 10a.1.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders See above under 10a.1.	

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company See above under question 10a.1.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ("the SE Statute") requires that the "registered office" islocated in the same Member State as the "head office". It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation Luxembourg law does not differentiate between SEs (or SCEs) and other resident entities referred to in Article 3 of the MD. As a general rule, the transfer of the registered office and head office (under Luxembourg law "central administration") of a Luxembourg resident entity outside of Luxembourg gives rise to exit taxation. However, in case the net assets of the former head office remain belonging to a Luxembourg permanent establishment of the company that was previously resident in Luxembourg, there will be no exit taxation. This is in line with the MD.	Article 172 (1) ITL

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' The term 'head office' (under Luxembourg law central administration) has replaced the term 'principal establishment' under Luxembourg law implementing the Merger Directive as well as under Luxembourg corporate law in order to comply with Article 7 of Regulations 2157/2001. However, no definition has been given. According to Luxembourg corporate tax law, the central administration of a company is presumed to be located where its registered office is located, unless proven otherwise. The use of the term 'central administration' instead of 'principal establishment ' should not have any practical consequences according to the parliamentary commentaries since the Luxembourg tax authorities have always assimilated both terms. As the parliamentary guidance refers expressively to the Merger Directive, when introducing the term 'head office' to the Luxembourg law, and as no further definition has been given, it can be concluded that the Luxembourg implementation is in compliance with the Merger Directive.	Article 2 alinea 3 of the Corporate law dated 1915 Doc.parl. 5708, page 16

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency The concept of 'central administration' coincides with one of the two criteria used to determine tax residence under Luxembourg tax law (please see 3.3 and 10b.2.). The concept of 'central administration' does not strictly correspond to the criterion mostly used in the tiebreaker clauses of DTCs concluded by Luxembourg, which is the place of effective management. However, in practice, these two criteria are considered to be largely similar.	Article 159 (1) ITL

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
10b.4 Assets and liabilities not effectively connected with a permanent establishment Luxembourg law has not indicated what applies in respect of assets not connected to a Luxembourg permanent establishment. According to Article 172 (2) ITL exit taxation will not be triggered	Article 172 (1) and (2) ITL

provided that 'the assets' remain belonging to a permanent establishment in Luxembourg. There is no distinction what applies in case only parts of the assets are allocated to such a permanent establishment. The law is therefore unclear as to whether assets/liabilities that do not remain connected with a permanent establishment would jeopardize the tax neutrality of the whole transfer, including that of the assets and liabilities connected to a permanent establishment, or whether this simply entails that a gain realized upon the transfer of these assets and liabilities that do not constitute a permanent establishment will be taxable.	

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
10b.5 Tax deferral No account has been taken of the judgment in Case C-470/04 *'N'*.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 The term 'comparable circumstances' Article 10c(2) has not been transposed in Luxembourg law. No specific rules apply to SEs and SCEs.	

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Loss recapture for permanent establishments Luxembourg law does not consider this situation.	

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>**10d.1 Deemed liquidation**</u> The transfer of registered office and head-office of an SE/SCE from Luxembourg would be considered to give rise to a deemed liquidation from a tax perspective unless the assets stay connected to a Luxembourg permanent establishment. In that case, it would also be considered to give rise to a deemed distribution of latent capital gains. Under Luxembourg law, this profit is considered as a capital gain and therefore would not give rise to any dividend withholding tax. At the level of the shareholder, if it is a Luxembourg resident entity, it would be tax exempt provided that the conditions for the Luxembourg participation exemption regime are fulfilled. In case the shareholder is not a Luxembourg tax resident and has held a participation of more than 10% for less than 6 months, the liquidation profit would be taxed in Luxembourg, unless an applicable tax treaty would provide otherwise. The transfer of registered office only would not give rise to taxation provided the head-office remains in Luxembourg. If the SE is transferred from one Member State to another Member State and provided there is continuance of legal personality, this transfer would not be a taxable event at the level of the Luxembourg shareholder. From a tax perspective, there is not discrimination of non-resident shareholders, on the contrary the situation of non-resident shareholders is better than the situation of resident shareholders.	Article 172 (I) ITL

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>**10d.2 Tax treatment of third country residents**</u> See above under question 10d.1.	Article 99 No. 2 ITL, Article 100 (II) ITL

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
11.1 Transposition of anti-abuse provisions Article 11(1)(a) has not been transposed into Luxembourg law. Luxembourg law has a general anti-abuse provision according to which simulated operations should not be taken into account by the tax authorities as well as the abuse of law concept for the purpose of reducing taxation.	Paragraphs 5 and 6 of the Adaptation law

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
11.2 General anti-abuse provision The tax authorities may rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance'. See above under 11.1.	Paragraphs 5 and 6 of the Adaptation law

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the '*Cadbury*' judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' As the Luxembourg tax law does not foresee any specific anti-abuse rules, no further steps needed to be taken by the Luxembourg tax authorities to bring the Luxembourg provisions in line with the principles of the '*Cadbury*' judgment. Therefore it is to be assumed that the Luxembourg tax law is in line with the principle of the '*Cadbury*' judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions The Luxembourg tax authorities have not sought to rely on Article 11(1)(a) in order to impose any requirements.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' Article 11 has not been transposed as such in Luxembourg law.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof Due to the fact that Luxembourg has not, to this date, transposed Article 11 of the Directive in question, no analysis of the impact of this Article on the national law can be conducted for the time being.	

MALTA

Abbreviations

English	English
CIR	Commissioner of Inland Revenue
PE	Permanent Establishment

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.

Overall state of implementation

The Directive of 23rd July, 1990 adopted by the Council of the European Communities on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States (90/434/EEC) ('Directive'), was transposed into Maltese law by Legal Notice 238 of 2003. The Act of transposition did not refer to any derogation but merely stated that the Directive 'shall have effect in relation to the Income Tax Acts.'

In that same year, a new Article, Article 27A was added to the Income Tax Act by Act II of 2003 (via Article 13 of Act II). Article 27A grants the Minister of Finance the power to make rules relating to the tax treatment of mergers and divisions of companies. More importantly, it incorporates certain definitions drawn from the Directive. Article 27A reads as follows:

'**27A.** Notwithstanding the provisions contained in the Income Tax Acts, the Minister may make rules regulating the tax treatment of companies and their members and other similar bodies or persons concerning mergers and divisions of companies, transfer of assets between companies and exchange of shares concerning companies and for the purposes of this Article:

(a) 'merger' shall mean an operation whereby:

- one or more companies, on being dissolved without going into liquidation, transfer all their assets and liabilities to another existing company in exchange for the issue to their shareholders of securities representing the capital of that other company, and, if applicable, a cash payment not exceeding such percentage as may be prescribed of the nominal value, or, in the absence of a nominal value, of the accounting para. value of those securities,
- two or more companies, on being dissolved without going into liquidation, transfer all their assets and liabilities to a company that they form, in exchange for the issue to their shareholders of securities representing the capital of that new company, and, if applicable, a cash payment not exceeding such percentage as may be prescribed of the nominal value, or in the absence of a nominal value, of the accounting para. value of those securities,
- a company, on being dissolved without going into liquidation, transfers all its assets and liabilities to the company holding all the securities representing its capital;

(b) 'division' shall mean an operation whereby a company, on being dissolved without going into liquidation, transfers all its assets and liabilities to two or more existing or new companies, in exchange for the pro rata issue to its shareholders of securities representing the capital of the companies receiving the assets and liabilities and, if applicable, a cash payment not exceeding such percentage as may be prescribed of the nominal value or, in the absence of a nominal value, of the accounting par value of those securities;

(c) ‘transfer of assets’ shall mean an operation whereby a company transfers without being dissolved all or one or more branches of its activity to another company in exchange for the transfer of securities representing the capital of the company receiving the transfer;

(d) ‘exchange of shares’ shall mean an operation whereby a company acquires a holding in the capital of another company such that it obtains a majority of the voting rights in that company in exchange for the issue to the shareholders of the latter company, in exchange for their securities, of securities representing the capital of the former company, and, if applicable, a cash payment not exceeding such percentage as may be prescribed of the nominal value or, in the absence of a nominal value, of the accounting par value of the securities issued in exchange;

(e) ‘transferring company’ shall mean the company transferring its assets and liabilities or transferring all or one or more branches of its activity;

(f) ‘receiving company’ shall mean the company receiving the assets and liabilities or all or one or more branches of the activity of the transferring company;

(g) ‘acquired company’ shall mean the company in which a holding is acquired by another company by means of an exchange of securities;

(h) ‘acquiring company’ shall mean the company which acquires a holding by means of an exchange of securities;

(i) ‘branch of activity’ shall mean all the assets and liabilities of a division of a company which from an organizational point of view constitute an independent business, that is to say an entity capable of functioning by its own means.’

The fact that partial divisions are not listed could be a potential infringement. Nevertheless we would not speak of an infringement because the act of transposition was unconditional. By `act of transposition was unconditional` we mean that the act of transposition did not include any derogation or limitation.

Legal Notice 238 of 2003 which transposed the Directive was amended in 2006 by Legal Notice 59 of 2006. The amendment implemented the amendments to the Directive made in 2005.

In fact the salient amendment reads as follows. By `salient amendment' we refer to the amendment bearing the most importance to the transposition of the amendments to the Directive made in 2005 into Maltese law.):

By referring directly:

‘The Directive of 23 July, 1990 adopted by the Council of the European Communities on a common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States (90/ 434/EEC) as amended by Council Directive 2005/19/EC of 17 February, 2005 amending Directive 90/434/EEC 1990 on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States shall have effect in relation to the Income Tax Acts.’

The Acts of transposition (legal notices 238 of 2003 and 59 of 2006) did not refer to any derogations but stated that the Directive "shall have effect in relation to the Income Tax Acts". So this means that the directive was transposed without any special derogations.

There have not been any judicial or quasi-judicial pronouncements on the directive and no ad hoc rules were passed. The latter is probably due to the fact that subsidiary legislation containing rules relating to cross-border merger was passed very recently by legal notice 415 2007 - the Cross-Border Mergers of Limited Liability Companies Regulations, 2007 (passed on 14 December 2007).

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
1.1 Involved companies As explained, the Merger Directive was implemented into Maltese Law without any derogation from the original text as emanated by the EU, or any additional explanatory notes. Mergers 'in which companies from two or more Member States are involved' have only become possible in Malta as from 14 December 2007. To date, the expression 'in which companies from two or more Member States are involved' has not been subject to any judicial pronouncements to date. The term 'companies involved' has also not been subject to any interpretation, whether judicial or otherwise, and should be assumed to be in line with current interpretation as per ECJ rulings.	N/A.

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
1.2 Foreign Member State and third state merger We would expect the local authorities to apply the directive to companies from two different Member States. Mergers between two local companies are not exempt from tax.	Article 5(14) of the Income Tax Act.

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term 'securities' Implementing legislation did not incorporate any definitions. Administrative guidelines have not been published. Similar definitions to the above have been incorporated in Article 27A of the Income Tax Act dealing with the Minister's powers to enact subsidiary legislation. Article 5	Article 27A of the Income Tax Act.

of the Income Tax Act defines securities as: 'securities' shall mean shares and stocks and such like instrument that participate in any way in the profits of the company and whose return is not limited to a fixed rate of return, units in a collective investment scheme as defined in Article 2 of the Investment Services Act, and units and such like instruments relating to linked long term business of insurance.'	

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
<u>2.2 The term 'cash payments'</u> Article 27A reproduced below refers to cash payments without specifying any percentage. 27A. 'Notwithstanding the provisions contained in the Income Tax Acts, the Minister may make rules regulating the tax treatment of companies and their members and other similar bodies or persons concerning mergers and divisions of companies, transfer of assets between companies and exchange of shares concerning companies and for the purposes of this Article: (a) 'merger' shall mean an operation whereby: • one or more companies, on being dissolved without going into liquidation, transfer all their assets and liabilities to another existing company in exchange for the issue to their shareholders of securities representing the capital of that other company, and, if applicable, a cash payment not exceeding such percentage as may be prescribed of the nominal value, or, in the absence of a nominal value, of the accounting par value of those securities, • two or more companies, on being dissolved without going into liquidation, transfer all their assets and liabilities to a company that they form, in exchange for the issue to their shareholders of securities representing the capital of that new company, and, if applicable, a cash payment not exceeding such percentage as may be prescribed of the nominal value, or in the absence of a nominal value, of the accounting par value of those securities, • a company, on being dissolved without going into liquidation, transfers all its assets and liabilities to the company holding all the securities representing its capital; (b) 'division' shall mean an operation whereby a company, on being dissolved without going into liquidation, transfers all its assets and liabilities to two or more existing or new companies, in exchange for the pro rata issue to its shareholders of securities representing the capital of	Article 27A of the Income Tax Act.

the companies receiving the assets and liabilities and, if applicable, a cash payment not exceeding such percentage as may be prescribed of the nominal value or, in the absence of a nominal value, of the accounting par value of those securities;…' The requirement of a 10% cash payment for reorganisation at book value is not present, therefore the limit of the cash payment must be 100% of the nominal value or accounting par value of the securities.	

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger Article 27A lists 3 types of merger without covering other or further types of merger. These have been listed in 2.2 above.	Article 27A of the Income Tax Act.

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares The definition of exchange of shares contained in Article 27A is different from the definition of the directive. The definition is being reproduced below. Acquisitions of further holdings are not contemplated. ''exchange of shares' shall mean an operation whereby a company acquires a holding in the capital of another company such that it obtains a majority of the voting rights in that company in exchange for the issue to the shareholders of the latter company, in exchange for their securities, of securities representing the capital of the former company, and, if applicable, a cash payment not exceeding such percentage as may be prescribed of the nominal value or, in the absence of a nominal value, of the accounting par value of the securities issued in exchange;' Amendments to the Income Tax Act giving effect to the Mergers Directive do not include the phrase, 'or holding such a majority, acquires a further holding'. Maltese implementing legislation seems to grant relief only for an exchange of shares leading to the obtaining of a majority of the voting rights. The law does not seem to contemplate relief in the case of acquisition of further holding. On the basis of the wording of national law, any further exchange that may consolidate the majority is not regulated	Article 27A of the Income Tax Act.

and as a result is not subject to the remit of the law. However, the act of transposition was unconditional, so we suspect that should the issue relating to the acquisition of further holdings arise, we would expect the Revenue authorities to apply the directive unconditionally.	

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>2.5 Consolidation of qualifying holding</u> No.	N/A.

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>2.6 The term 'branch of activity'</u> Branch of activity is defined in Article 27A as: 'branch of activity' shall mean all the assets and liabilities of a division of a company which from an organizational point of view constitute an independent business, that is to say an entity capable of functioning by its own means.'	Article 27A of the Income Tax Act.

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> No.	N/A.

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>3.2 Transparent entities</u> No. See also 4.8.	N/A.

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
<u>3.3 Qualification of tax residency</u> Registration for companies registered in Malta after 1 July 1994; Management and control in respect of foreign registered companies. The most common tax residence tiebreaker in double taxation conventions is the place of effective management and control.	Article 2 of the Income Tax Act.

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>3.4 Subject-to-tax clause</u> There has not been any administrative guidance on the issue and there have not been any judicial pronouncements.	N/A.

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>3.5 Shareholder requirements</u> National legislation does not limit the benefits of the directive.	N/A.

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>4.1 The concepts of 'real values' and 'value for tax purposes'</u> The terms have not been interpreted as yet. The instruments of transposition did not incorporate ad hoc rules. The rules relating to the computation of the capital gain is in such situations are contained in the capital gains rule. A synopsis of the rules is contained below.	N/A.

<u>Capital Gains Rules</u> For the purpose of computing income on capital gains, one should draw a distinction between two types of transfers: (a) Transfer of a non - controlling interest (b) Transfer of a controlling interest In the case of share transfers of a non controlling interest, the capital gain is computed as the consideration received less the cost of acquisition. If however, the latter shares have been acquired prior to 25th November 1992, the cost of acquisition is deemed to be the higher of the actual price paid and the net asset value on the last balance sheet date submitted to the CIR by 18th December 1992 as adjusted for the market value of immoveable property in the books at 1992. A controlling interest is considered as such when the shareholder either holds more then 25% of the nominal value of the issued share capital or voting rights of the company or the company is entitled to appoint a director. When computing the capital gain chargeable to tax of a share transfer of a controlling interest, the consideration will be deemed to be the higher of the transfer value or market value. Market value is essentially an adjusted book value of the company based on the previous year's financial statements. These adjustments include amongst others, the introduction of an element of goodwill; immoveable property is to be revalued to market value; shareholdings of 10% or more in other companies are revalued to market value, whilst any preference shares are deducted. It is also worth noting that transfers within an 18 month period by the shareholder or related persons are aggregated in order to determine whether a transfer is one of a controlling interest Share transfers also attract duty on documents at the rate of €2 for every €100 or part thereof. If more then 75% of the assets of the company consist of immoveable property, the rate will increase to €5 for every €100 or part thereof. Share traded on the Malta Stock Exchange do not attract Duty on Documents. Capital Gains taxation will be deferred.	

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
<u>4.2 Specific guidance for divisions/partial divisions</u> No. Partial division is contemplated in Article 27A.	Article 27A of the Income Tax Act.

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' There have neither been any administrative guidelines nor interpretations. Please note that the allocation of assets either (a) from the Head Office to a branch OR (b) from the branch to the Head Office is not considered to amount to a transfer because, from a Maltese legal and tax point of view, there is no passage of title. Consequently there will not be any tax liability. The allocation is effected by an accounting entry. We do not have a definition of permanent establishment in domestic law. The definition found in the OECD Model Convention for the elimination of double taxation would be followed.	N/A.

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief No.	N/A.

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment There are no domestic ad hoc rules relating to the issue. Additional please note that if there will be a cross-border merger in respect of which the MD will apply one cannot really speak of a transfer of assets from one company to another because there will merely be a transfer of assets into the amalgamated entity. Consequently we would not expect immediate taxation and one cannot speak of an infringement but the matter should be clarified by the Maltese authorities. Assets which are owned by the company would fall in the deferral envisaged in the Mergers Directive. Amalgamated entity refers to the merging companies as one entity following the merger.	N/A.

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company There have not been any derogations therefore the exemption would apply.	N/A.

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral The instruments of transposition merely transposed the directive without taking recent judgements of the ECJ specifically into account.	N/A.

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities No administrative guidelines relating to tax transparency have been published. Article 2 of the Income Tax Act incorporates a definition of the term 'company'. Bodies of persons which do not fall within the definition would be considered to be transparent. 'Company' means: (a) any partnership constituted under the Companies Act or under the Commercial Partnerships Ordinance, being either a partnership 'en commandite', the capital of which is divided into shares, or a partnership 'anonyme': Provided that in the case of a cell company as defined in the Companies Act (Cell Companies Carrying on Business of Insurance) Regulations, (in this proviso referred to as 'the Regulations') as may be amended from time to time, or in any other law or regulations replacing the Regulations, for all intents and purposes of the Income Tax Acts, every cell of a cell company and that part of a cell company in which non-cellular assets are held, shall each be deemed to be a separate company and any words and expressions in the Income Tax Acts which are relevant to a company shall be construed accordingly. The interpretation of such words and expressions insofar as applicable to a cell company shall be made on the basis of the relevant provisions of the Regulations; (b) any body of persons constituted, incorporated or registered outside Malta, and of a nature similar to the aforesaid	Article 2 of the Income Tax Act.

partnerships; (c) any co-operative society duly registered as such under the appropriate law for the time being in force in Malta;' Please note that under Maltese law a co-operative society (which has the characteristics of a transparent entity in terms of international tax law) is attributed opaque characteristics in terms of Maltese law. The annex to the Mergers Directive refers only to nontransparent entities.	

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
<u>**4.9 Further conditions for tax relief**</u> No. The commercial or accounting rules on provisions and reserves are relevant for tax purposes.	N/A.

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>**5.1 The term 'provisions and reserves'**</u> No.	N/A.

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
<u>**5.2 Exclusion of 'provisions and reserves' from permanent establishments**</u> There are no specific rules in national law.	N/A.

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves There are no specific rules in national law. Please see 5.2 and 5.3. Applicable tax regime: - Accounting rules would apply.	N/A.

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves There are no specific rules in national law.	N/A.

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry-over of losses There is no specific definition of loss in the instruments which transpose the merger directive. The general definition contained in Article 2 of the Income Tax Act would apply. The definition reads 'losses in relation to a trade, business, profession, or vocation means loss computed in like manner as profits'.	Article 2 of the Income Tax Act.

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment In practise attribution on the basis of source but national law does not contemplate attribution rules. As explained, there are no local rules on attribution of losses to permanent establishments. Losses are attributed 'on the basis of source' meaning that losses are considered to have been incurred in the country where they have been actually suffered.	N/A.

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
<u>6.3 Specific legislation for divisions/partial divisions/transfer of assets</u> Article 27A (which is the only relevant law) refers to division and transfers of assets but not to partial divisions.	N/A.

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
<u>6.4 Further conditions for carry over of losses</u> No further conditions.	N/A.

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
<u>7.1 Amended holding threshold</u> Article 27A refers to a holding threshold 'as may be prescribed'. 'As may prescribed' refers to the conditions which the Minister responsible for the Income Tax Acts may determine from time to time . It seems that the EU instrument has anticipated the Minister's legal notice. The Minister would be expected to acknowledge the minimum holding established by the Directive.	N/A.

Article 7(1) covers <u>gains</u> accruing on the cancellation of a holding. It does not cover <u>losses</u> that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
<u>7.2 Treatment of losses</u> It has not been dealt with. There is no legislation dealing with this situation. Losses would be deductible provided that, had the transaction given rise to a gain, such a gain would have been taxable.	N/A.

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder The law vests the Minister of Finance with the power to pass subsidiary legislation to regulate similar situations, but the Minister has not yet passed regulation in this respect. There used to be an exemption in respect of capital gains arising upon an exchange of shares upon a restructuring of holdings but it was abrogated in 2004. Consequently in an exchange of shares there are two deemed transfers both of which are taxable. An extract from the law follows: 5 (14) "Where a transfer involving the exchange of shares on restructuring of holding upon mergers, demergers, divisions, amalgamations and reorganisation takes place it shall be deemed that no loss or gain has arisen from such transfer and the cost of acquisition upon a subsequent transfer shall be deemed to be the cost of acquisition of the original shares: Provided that the provisions of this sub-article shall only apply in such manner and in such circumstances as may be prescribed by the Minister: Provided further that the first proviso hereof shall not apply to divisions and mergers where the draft terms of the said divisions and mergers had been forwarded to the Registrar of Companies for registration in terms of the provisions of the Companies Act on or prior to the 24th November, 2003 and the Registrar had published the relevant statement in the Government Gazette in terms of the said Act on or prior to the 31st December, 2003, provided that a copy of the relative publication is attached to the relative deed." However please note that the intra-group exemption was retained and there is an exemption from tax which applies in respect of transfers of shares between companies which are owned and controlled by the same persons (more than 50%). An amalgamation refers to a merger between companies. Divisions and mergers forwarded to the Registry of Companies: These divisions and mergers would not be subject to the effects of the Directive and would thus be subject to taxation of any capital gains arising. Transfers of taxable assets made in the course of a merger generally give rise to taxation. Rule 7 of the Capital Gains Rules provides that the tax exemption contained in article 5(14) of the Income Tax Act will apply where the exchange of the shares does not produce any change in the individual direct or indirect beneficial owners of the companies involved or in the proportion in the value of each of the companies involved represented by the shares owned beneficially directly or indirectly by each	Article 27A of the Income Tax Act.

such individual.	

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>**8.2 Computation of the capital gain**</u> No specific guidance; normal capital gains rules would apply and in certain cases cash payments will be taxed.	Article 5 of the Income Tax Act.

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>**8.3 Further conditions for tax relief**</u> No further conditions.	N/A.

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>**9.1 Avoidance of economic double taxation at the level of the transferring company**</u> No.	N/A.

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>**9.2 Further conditions for tax relief**</u> No further conditions.	N/A.

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>9.3 Tax deferral</u> National legislation merely transposed the directive.	N/A.

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Loss recapture for permanent establishments in third Member States</u> National law does not contemplate ad hoc rules but merely transposed the directive.	N/A.

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> National law does not contemplate ad hoc rules but merely transposed the directive.	N/A.

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> There is neither ad hoc national legislation nor an administrative guideline. The Merger Directive has been implemented without derogations and reservations. Additional please note that unrealized gains are not taxable in terms of domestic law either. By means of Legal Notice 59 of 2006 which transposes into Maltese Law the provisions of Council Directive 2005/19/EC of 17 February 2005 in its entirety, both Articles 10.1 and 10.2 found in such Directive apply in Malta.	N/A.

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
10.4 Tax deferral No particular account of ECJ case law has been taken.	N/A.

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies There has neither been any specific national legislation implementing Article 10(a) nor any administrative guidance. By means of Legal Notice 59 of 2006 which transposes into Maltese Law the provisions of Council Directive 2005/19/EC of 17 February 2005 in its entirety, Article 10a was adopted under Maltese Law. The directive lists exclusively non-transparent entities.	N/A.

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit There is no special definition.	N/A.

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit There is no special ad hoc legislation providing for the notional tax credit to be credited in terms of Article 10a (2).	N/A.

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders National legislation does not contemplate legislation which expressly distinguishes between 10a (3) and 10a (4).	N/A.

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company Given that national corporate law contemplates only mergers between bodies of persons of the same type (transparent/non-transparent), there are no tax rules relating to the taxation of mergers between transparent entities to non-transparent entities.	N/A.

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation Under Maltese national law no exit taxation is applicable. Therefore the transfer of the registered office of an SE would not give rise to exit taxation.	N/A.

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' 'Head office' has not been defined in our legislation.	N/A.

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency The concept of 'head office' does not coincide with the criterion used to determine tax residence.	N/A.

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
10b.4 Assets and liabilities not effectively connected with a permanent establishment No specific rules. Presumable the gains will be linked to those assets taxed at the time of the transfer of the registered office. This issue has not yet been addressed specifically.	N/A.

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
10b.5 Tax deferral No particular account has been taken in our legislation of ECJ case law and of the judgment in the *'N'* case.	N/A.

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 The term 'comparable circumstances' The term has not been defined.	N/A.

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
<u>10c.2 Loss recapture for permanent establishments</u> The losses may be availed of by the principal provided that the losses are calculated in terms of Maltese law. The issue of a set-off of losses attributable to a PE before the transfer of the registered office has not been specifically addressed, but such losses would probably be allowable. The losses of a PE offset by the head office before the transfer of the registered office, are they recaptured and taxed when such a transfer takes place? - Presumably yes but this issue has not yet been addressed.	N/A.

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>10d.1 Deemed liquidation</u> Redomiciliation does not give rise to a deemed liquidation.	L.N. 344 of 2002

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>10d.2 Tax treatment of third country residents</u> No special rules, redomiciliation does not give rise to a deemed liquidation.	L.N. 344 of 2002

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> Yes, via a very brief and concise act of transposition, which merely states	L.N. 238 of 2003.

that the directive has been implemented.	

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
11.2 General anti-abuse provision N/A.	N/A.

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the '*Cadbury*' judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' No specific steps have been taken/general anti-avoidance rules would apply.	Article 51 of the Income Tax Act.

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions No. Jurisprudence on the economic purpose test is available for anti-avoidance situations. The applicability of the test to restructurings is not excluded.	N/A.

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' In the absence of case law relating to the Merger Directive, one would need to fall back on general case law on anti-avoidance. We are aware of case law dealing with anti-avoidance which refers to the concept of economic purpose but not to case law dealing with restructuring and nationalization. The Maltese concept of economic or commercial purpose for the purposes	Article 51 of the Income Tax Act.

of tax avoidance is the common law concept (i.e. Furniss v. Dawson). Maltese case law (BSC 9/95) has referred to similar concepts on the matter.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof The tax payer, in the case of an assessment.	N/A.

NETHERLANDS

Abbreviations

English	Dutch	English	Dutch
CITA	Wet Vpb 1969	Corporate Income Tax Act 1969	Wet op de vennootschapsbelasting 1969
BNB	BNB	N/A	Beslissingen in belastingzaken
DADT	Bvdb	Decree for the Avoidance of Double Taxation	Besluit voorkoming dubbele belasting
GTA	AWR	General Tax Act	Algemene Wet inzake Rijksbelastingen
NMC	NSV	Netherlands Model Convention	Nederlands Standaardverdrag
Plc	NV	Public Limited Company	Naamloze Vennootschap
SCE	SCE	N/A	Europese Coöperatieve Vennootschap
SE	SE	N/A	Europese Vennootschap
N/A	VN	N/A	VakstudieNieuws

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.

<u>Overall state of implementation</u>

The Merger Directive has been implemented by Law of 10 September 1992 (Law Gazette 1992, 491), with retroactive effect to 1 January 1992. This law covered the requirements of exchange of shares, legal mergers and transfer of assets. The requirements of legal divisions were, by contrast, not yet covered as under Netherlands civil law, as it stood at that time, legal divisions were not possible.

However, by Law of 17 June 1998 (Law Gazette 1998, 350) also the requirements of legal divisions have been implemented with retroactive effect to 1 February 1998 since as of that date also legal divisions became possible under Netherlands civil law. Since the Netherlands civil law requirements for legal mergers were amended at the same time, the implemented requirements of legal mergers were amended accordingly with retroactive effect to 1 February 1998.

As a result of the decision by the ECJ of 17 July 1997, Case C-28/95 (*'Leur Bloem'*), the Netherlands requirements of all types of transactions covered by the Merger Directive have been amended by Law of 11 May 2000 (Law Gazette 2000, 215) and Law of 11 May 2000 (Law Gazette 2000, 216), effective as of 1 January 2001, in order to comply with the Merger Directive. The requirement that the acquiring company has to carry on business itself or that there has to be a permanent merger, from a financial and economic point of view, of the business of two companies into a single unit, has been deleted from national implementing legislation. This requirement was, as a result of the *'Leur Bloem'* decision, already made ineffective under Netherlands published policy, thereby introducing at the same time the requirement that the transaction has not as its principal objective or as one of its principal objectives tax evasion or tax avoidance (Decree State Secretary of Finance dated 7 May 1998, nr. DB98/720).

In addition, the requirement that any merging or splitting company had to be incorporated according to the laws of and effectively managed and controlled in the Netherlands was deleted also. It follows that each merger or division which is allowed under the civil law of the Netherlands or under the civil law of an EU Member State is covered by the Netherlands implementation legislation. These amendments take effect as of 1 January, 2001.

By Law of 18 December 2003 (Law Gazette 2003, 527) and by Law of 15 December 2005 (Law Gazette 2005, 683), effective as of 8 October 2004 and 18 August 2006 respectively, the SE and SCE are treated on the same footing as a Netherlands NV. Accordingly, both the SE and SCE are eligible under Netherlands implementing legislation to comply with the requirements of all types of transactions covered by the Merger Directive under the same conditions as a Netherlands NV. According to the Netherlands legislator in an official Circular dated 31 May 2006, no. DB2006/290, the Netherlands has complied with the requirements following from Directive 2005/19/EC and which entered into force on 1 January, 2006.

In addition, according to the Netherlands legislator in the aforesaid Circular, the Netherlands already complied with all other requirements following from Directive 2005/19/EC and which entered into force on 1 January, 2007. Accordingly, no further legislative action was considered necessary. The European Commission has been notified in this regard.

For the rest, a number of technical, non-substantive amendments have been made in the Netherlands implementing legislation in the course of time. These technical amendments are not further elaborated on.

Guidance issued by the tax administration relevant for the interpretation of the implementation of the Merger Directive is included in the following publications:

(a) Decree State Secretary of Finance dated 19 December 2000, no. CPP2000/2682. Conditions and explanatory memorandum with respect to the tax facilitated partial legal division;

(b) Decree State Secretary of Finance dated 25 February 2002, nr. CPP2002/158. Conditions and explanatory memorandum with respect to the tax facilitated legal merger;

(c) Decree State Secretary of Finance dated 19 December 2000, no. CPP2000/3041. Conditions and explanatory memorandum with respect to the tax facilitated transfer of assets.

In addition, a large number of rather technical administrative guidelines have been published, such as those regarding concurrence between the legal merger or legal division on the one hand and the Netherlands group consolidation regime on the other. These technical guidelines are not further elaborated on.

The Dutch Supreme Court recently requested a preliminary ruling from the ECJ on the interpretation of the Merger Directive regarding a transaction to avoid Dutch real estate transfer tax. The Court wants to know whether the business merger facility in the context of the CIT can be denied in case the transactions at hand have the aim to avoid Dutch taxes other than those mentioned by the Merger Directive. Provided that the denial is proportionate our opinion would be yes. In our view, however, full denial of the merger facility in the CIT is disproportionate. The perceived abuse should therefore be combatted in the context of the Dutch real estate transfer tax rather than in the context of the Dutch CIT.

Article 1 – Scope

Please describe how the expression ‘in which companies from two or more Member States are involved’ has been interpreted and implemented. Has the term ‘companies involved’ been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> The expression ‘in which companies from two or more Member States are involved’ would, absent any specific provision, have been interpreted under reference to the Netherlands criteria determining the place of residence of a company. However, following a specific provision to this end in the General Tax Act, this term must be interpreted under reference to the tax legislation of the Member State(s) where the involved companies are established. The Netherlands criteria are thus not decisive in this respect. The expression ‘companies involved’ has been interpreted as comprising only the companies directly involved in the transaction and not the parent	Article 4(1) GTA Sec. 4(3) GTA Sec. 3.55(2)(b), 3.56(2) and 3.57(2) ITA; Sec. 14a(11) and 14b(8) CITA Sec. 3.55(2)(a),

companies. The following remarks are added. It is noted that to the extent the companies involved are all resident in the Netherlands, the transaction will also fall under the scope of the national implementing legislation. The national implementing legislation therefore does not distinguish between domestic and cross-border transactions. Furthermore, with respect to transfers of assets both the transferring and the receiving company are not required to be an EU-resident. Lastly, in the case of exchange of shares, the benefits of the Merger Directive also apply where a Netherlands company acquires shares in a company resident in a third country.	3.56(2) and 3.57(2) ITA; Sec. 14a(11) and 14b(8) CITA Sec. 14(1) CITA Sec. 3.55(2)(c) ITA

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
1.2 Foreign Member State and third state merger The fact that the parent companies were from two different Member States would not, as such, suffice to bring the merger within the scope of the national implementing legislation (see above, section 1.1). It is noticed that this is without prejudice to the right of tax relief at the level of the shareholders of the companies involved as granted by the Merger Directive. The Netherlands would apply the benefits of the Merger Directive if the merging companies were from a single (foreign) Member State. Lastly, in the case of transfer of assets, the Netherlands also applies the benefits of the Merger Directive if the transferring and/or the receiving company are resident in a third state.	Sec. 14a(11) and 14b(8) CITA; Article 3.55(2)(b) ITA Article 14(1) CITA

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term 'securities' In the context of exchange of shares, the term 'securities' has been defined as shares and profit-sharing rights. In the context of legal division, legal merger and transfer of assets, the term 'securities' has been defined as shares, which are deemed to include	Sec. 3.55(2) ITA Sec. 3.56(5)(b) and 3.57(5)(a) ITA and Sec. 14(6) and 14a(10) CITA

profit-sharing rights, certificates of entitlement and membership-rights. With respect to the position of the shareholders in a merging or splitting company, in addition, tax relief at the level of the shareholders is available not only with respect to their shares in the merging or splitting company, but also with respect to loan receivables from the merging or splitting company. In the case of legal division and legal merger, the term 'securities' also includes (option) rights to acquire shares and profit sharing rights in or loan receivables from the splitting or merging company.	Sec. 3.56(2) and Sec. 3.57(2) ITA Sec. 3.56(5)(c) and 3.57(5)(b) ITA

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
<u>2.2 The term 'cash payments'</u> In case of an exchange of shares, a cash payment may not exceed 10% of the par-value of the issued securities in order to qualify under the Merger Directive. The literal wording of the text does not seem to exclude the possibility to determine the 10% threshold on an overall basis. However, both from legislative history and from the underlying rationale of the 10%-maximum requirement one may derive that this requirement should apply on a per shareholder basis. From the legislative history, it can nevertheless be derived that under certain (bonafide) circumstances, an overall approach may be allowed. For completeness sake, it is observed that no relief is granted with respect to an allowed cash payment. As regards legal mergers and divisions, as stated in the Introduction, the Netherlands implementing legislation is applicable to all legal mergers and divisions which are allowed under the civil law of the Netherlands or an EU-Member State. In the case a cash payment is allowed under civil law (in the Netherlands, for instance, a cash payment with a maximum of 10% is allowed), such is therefore automatically followed by the Netherlands implementing legislation. For completeness sake, it is noted that no relief is available for any cash payment received in the case of a legal merger of division. In case of transfer of assets, a cash payment is allowed with a maximum of 4,500 Euro, for which no relief is granted.	Sec. 3.55(4)(a) Sec. 3.56(2) and 3.57(2) ITA Para 3.6 of the Decree State Secretary of Finance dated 19 December 2000, no. CPP2000/3041

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger Yes. As stated in the Introduction, the Netherlands implementing legislation is applicable to all legal mergers and divisions which are allowed under the civil law of the Netherlands or an EU-Member State. It follows that, for instance, Netherlands triangular mergers and so-called 'quarrel' divisions (i.e. divisions resulting from the fact that the shareholders do not agree and do not want to participate together anymore) are covered by the Netherlands implementing legislation, although not covered by the Merger Directive.	

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares The Netherlands implementation legislation covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. It does not seem to cover, by contrast, successive exchanges of shares that finally lead to the acquisition of a majority holding. It may, however, be argued that to the extent successive exchanges are related, the benefits of the Merger Directive should be granted in each exchange separately, and not only to the exchange of shares leading to the acquisition of a majority holding.	Sec. 3.55(3) ITA

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
2.5 Consolidation of qualifying holding With regard to an exchange of shares that consolidates an existing majority holding, the grant of relief is subject to the conditions imposed by the Merger Directive. However, no additional conditions are imposed.	Sec. 3.55(3) ITA

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>2.6 The term 'branch of activity'</u> Firstly, it is noted that the requirement of 'branch of activity' is not imposed under Netherlands civil law in the case of a legal merger or full division. Since the Netherlands implementing legislation follows civil law in these cases, the requirement of 'branch of activity' is not imposed in the case of a legal merger or full division. By contrast, the requirement of 'branch of activity' is imposed, however, in the case of a partial division or transfer or assets. Following the administrative guidelines issued by the Netherlands State Secretary of Finance, the term 'branch of activity' should be interpreted substantively as meaning a permanent organization of capital and labour. Nevertheless, from both Netherlands legislative history and the objective and purpose of the Merger Directive one may infer that the term 'branch of activity' should be interpreted more broadly as to also include types of investment activities, conducted by an investment fund, for instance.	Para 3.2 of the Decree State Secretary of Finance dated 19 December 2000, no. CPP2000/3041

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> No, except for the case of transfer of assets. In that case, all entities subject to Netherlands corporate income tax may qualify, irrespective of its legal form or place of residence (*i.e.* open to both residents and non-residents).	Sec. 3.55(5)(1º), 3.56(2), 3.57(2) ITA; Sec. 14a(11), 14b(8) CITA

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>3.2 Transparent entities</u> Whether or not any of the listed entities are regarded as tax transparent should be determined on the basis of the relevant criteria under national tax law. From Netherlands legislation and case law one may infer that the factors of legal personality, transferability of the interests and direct entitlement to the profits of the entity are relevant in this respect. There is, however, no clear consensus in this respect. Guidance has therefore been provided by the Netherlands State Secretary of Finance in his Decree published on 18 December 2004. According to this Decree, four main	Decree of 18 December 2004, no. CPP2004/2730M

factors are addressed by way of the following questions: (a) Can the entity hold the legal title to the assets that are used to carry out its activities? (b) Does the entity have at least one participant that has unlimited liability for the debts and the other obligations of the entity? (c) Does the entity have a capital divided into shares? (d) Can the admission or the replacement of the participants take place without the consent of all of the participants (other than in the situation in which the interest is passed on by inheritance or legacy)? Depending on the answers to these questions, the entity is classified as transparent or not transparent. This is determined according to the following two rules: First, if the answer to (a) is 'yes' and that to (b) is 'no', it is assumed that the entity is not transparent. Secondly, if the answer to (a) is 'yes' or 'no' and that to (b) is 'yes', questions (c) and (d) must be considered. If the answers to (c) and (d) are 'yes', the entity is not transparent. If the answer to either (c) or (d) is 'no', the entity is transparent. In addition, if the entity is comparable to a Netherlands limited partnership only factor (d) must be considered. It follows that, for instance, the Belgian 'société en nom collectif' is considered transparent from a Netherlands tax law perspective. On the other hand, the Latvian Sabiedribas ar Ierobezotu Atbildibu, for example, is considered non-transparent from a Netherlands tax law perspective. In Annex 2 attached to the Decree of 18 December 2004, no. CPP2004/2730M foreign entities and their principle treatment under Netherlands tax law as transparent or non transparent entities are listed and categorized, although non-exhaustively. Taxpayers can rely on the above Decree and Annex 2 based on the general principles of good governance respectively good faith. They are, however, not legally bound by this Decree.	

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency As a general rule, a company established according to the laws of the Netherlands is deemed to be a Netherlands resident, irrespective of its actual place of management and control. This general rules does, however, not apply in the case of a legal merger or division. In such case, the company's place of residence needs to be evaluated based on the relevant facts and circumstances. Netherlands case law points out that the place of effective management of a company is the most important criterion in deciding where a company resides. From a Netherlands tax perspective, effective management has been described in case law as the location where the management of a company (i.e. place of day-to-day and strategic management) is in fact carried on. Substance, hereby, prevails over form. The above also holds well with respect to companies which are not incorporated according to the laws of the Netherlands. The most common tax residence tiebreaker criterion in the double tax conventions concluded by the Netherlands is similar to Article 4(3) of the OECD Model Convention (*i.e.* place of effective management).	Sec. 2(4) CITA Sec. 4(1) GTA Netherlands Supreme Court 23 September1992, BNB 1993/193 Sec. 4(1) GTA Sec. 4(3) NMC

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject-to-tax clause The subject-to-tax clause has been implemented as being subject to one of the taxes as mentioned in the Merger Directive, without having a choice and without being exempt. In the context of a similar requirement under the former Netherlands participation exemption rules, several issues arose in this respect, for instance in the case of tax holidays. In an officially published Decree, it was held by the Netherlands State Secretary of Finance that the subject to tax requirement may be met in the case of a tax holiday of 10 years. By contrast, in the case of a tax holiday of 50 years, this requirement was not met. Similar issues may arise in the context of the Merger Directive.	Sec. 3.55(5) ITA Decree of State Secretary of Finance dated 1 February 2006, no. CPP2005/2702M, para. 1.2.4.4

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>3.5 Shareholder requirements</u> No.	

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>4.1 The concepts of 'real values' and 'value for tax purposes'</u> No specific implementing legislation applies in this respect. The general Netherlands concept of 'total profit' applies. That is to say, the total profit (*e.g.* trading profit and capital gains) derived by a taxable entity during its whole existence is taxable. The concept of 'real value' is therefore interpreted as the fair market value of the assets at the time of the transaction. The concept of 'value for tax purposes' is interpreted as the tax book value of the assets in the books of the transferring company at the time of the transaction.	Sec. 8(1) CITA

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
<u>4.2 Specific guidance for divisions/partial divisions</u> Yes. Where a splitting company has a share interest which does not fall under the Netherlands participation exemption, and this share interest is transferred to the acquiring company, specific guidance applies in the case of a partial division in order to safeguard the Netherlands tax claim. In such case, the book value of the transferred shares is attributed on a pro rata basis to the shares the acquiring company has directly after the division. The pro rata attribution means that the fair market value of the split assets must be compared to the fair market value of the assets received by any acquiring company. Since the Netherlands grants roll-over in combination with taxation upon disposal of the shareholding, there should be no conflict with the Directive. Although no published guidance applies in the case of a full division, the above *mutatis mutandis* applies in the case of a full division.	Decree State Secretary of Finance dated 19 December 2000, no. CPP2000/2682, Sec. 6.

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>4.3 The concepts of 'effectively connected' and 'permanent establishment'</u> The concept of the allocation of assets effectively connected with a permanent establishment is developed in the Netherlands case law and similarly applies within the context of the Merger Directive. It follows from this case law that the main criterion is whether or not an asset can be considered instrumental in or subservient to the conduct of business by the permanent establishment. If that is the case, the asset should be considered to be effectively connected to the permanent establishment. Whether or not an asset is instrumental in the conduct of business by the permanent establishment should be determined based on the nature of the asset at hand. It should, in addition, be assessed whether or not the permanent establishment personnel controls the relevant asset and who manages and supervises its exploitation. The Netherlands Supreme Court thus seems to follow an economic or functional rather than a legal approach in this respect. The concept of 'permanent establishment' has also developed in Netherlands case law. From this case law, the following basic principles can be derived: (a) there must be a tangible property which is fixed during a certain amount of time (for instance, a circulating circus tent did meet this test); (b) which is at the disposal of the taxpayer during a certain amount of time; and (c) which is properly equipped in order to have the taxpayer exercised its activities. The Netherlands definition thus resembles, but not entirely corresponds to the concept of 'permanent establishment' as employed under the OECD Model Convention.	For instance, Dutch Supreme Court 20 December 2002, BNB 2003/246

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief Yes. In all cases, the scope of relief can be limited in cases of abuse. Furthermore, under circumstances the granted relief may be recaptured in cases where the rolled-over claim would otherwise be lost. This would notably be the case where a company has a shareholding in a merging or splitting company which shareholding does not qualify for the Netherlands participation exemption prior to the merger or division whereas it starts qualifying for the Netherlands participation exemption after the merger or division. In order to safeguard the Netherlands tax claim in such cases, the participation exemption (on capital gains) can subsequently be excluded to the extent relief was granted upon the merger or division ('compartmentalization'). Since the Netherlands grants roll-over in combination with taxation upon disposal of the shareholding, there should be no conflict with the Directive.	Sec. 3.55(4)(b), 3.56(4) and 3.57(4) ITA;Sec. 14(4), 14a(6) and 14b(5) CITA Sec. 13h CITA

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment In case the Netherlands would lose the right to tax the gain on the disposal of the transferred assets with the receiving corporate entity or such right would be limited, the respective transferred assets, including any intangible assets not acquired for a consideration or self-developed must be valued at fair market value in the closing balance sheet of the transferring company and will in principle be taxed. Based on '*X and Y*' (para. 59), '*Laysterie du Saillant*' and the '*N.' case*, it can be questioned whether this is in accordance with the EC Treaty freedoms, since less restrictive measures are imaginable (*e.g.* deferral until the gain is actually realized). Based on '*Marks & Spencer*' and '*Lidl*', however, it could also be argued that less restrictive measures can only be achieved by means of harmonization.	Sec. 14(1), 14a(1) and 14b(1) CITA

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company Where the receiving company has a holding in the capital of the transferring company also the profit which can be allotted to shares of the receiving company in the transferring company can be profit tax exempt under the Netherlands rules of the participation exemption. The participation exemption applies where a company has a shareholding of at least 5% in a subsidiary, unless the assets of this subsidiary consist for 50% or more of passive, lowly taxed assets. In the latter case, a credit method applies. In case the participation exemption does not apply, deferral may apply only upon request. If deferral is denied upon request, the compatibility with the Directive may be questioned. It is, however, difficult to say in the abstract whether such denial is in conflict, since this is very dependent on the actual case of the requesting taxpayer.	Sec. 13(1) CITA Sec. 13(2) CITA Sec. 13k(5) CITA

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral Where no Netherlands permanent establishment remains after the transaction, which for instance may occur where the transfer of intellectual property is involved, no relief is granted and immediate taxation takes place, without any deferral. No account has been taken in these situations of the case law of the ECJ in the context of exit-charges, for instance Case C-470/04 ('N'). One can argue, however, that less restrictive measures are conceivable, such as deferral until the moment of actual realization.	

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities No specific implementation legislation has been enacted in this respect. The general Netherlands criteria to determine whether an entity is tax transparent or not, apply (please see 3.2). No further specific legislation or administrative guidelines have been implemented or issued in this	

respect. In case of transparent entities, the Netherlands applies a 'look-through' approach and will grant the benefits of the Merger Directive at the level of the participants, provided that all other requirements for the Merger Directive are met. Issues may nevertheless arise in case an entity is considered non-transparent by the Netherlands tax authorities whereas it is considered to be fiscally transparent by the tax authorities of another Member State. In such case, the 'subject to tax'-requirement may not be met from a Netherlands tax perspective. Accordingly, the benefits following from the Netherlands implementing legislation may not be granted.	

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief Yes. In case of transfer of assets, legal division and legal merger, two types of relief apply: automatic relief and relief upon request. Automatic relief applies provided that the following three conditions are met: (a) For the determination of the taxable profit, the same provisions apply to both the transferring and the receiving company; (b) The receiving company has no existing claim i) to carry forward former losses, ii) to relief for double taxation for foreign income, iii) to apply the Netherlands 'patent-box' regime or iv) to apply the indirect credit method under the Netherlands participation regime; and (c) The future taxation of the rolled-over gain is ensured. In case one of the above requirements are not met, relief can nevertheless be obtained but only upon request. In such case, however, further requirements may be imposed by the Netherlands tax authorities which serve to ensure the levy and collection of the tax which would have been due if relief would not have been granted. In addition, further requirements can be imposed with respect to the yearly determination of the taxable profits of the receiving company, the allowed tax reserves, loss-compensation, the relief for double taxation for foreign income, the application of the Netherlands 'patent-box' regime or the indirect credit method under the Netherlands participation regime and in cases where the fair market value of a transferred assets is below its book value. These requirements have been published and further elaborated on in the so-called 'standard conditions. Since these standard conditions are of a very technical nature, we will not elaborate on them in more detail. Nevertheless, the fact that relief is granted only upon request in case one of the above requirements are not met, is considered not to be in conflict with the Directive. In individual cases, the application of these standard	Sec. 14(1), 14a(1) and 14b(1) CITA Sec. 14(2), 14a(2) and 14b(2) CITA Decree State Secretary of Finance dated 19 December 2000, no. CPP2000/2682; Decree State Secretary of Finance dated 25 February 2002, nr. CPP2002/158; Decree State Secretary of Finance dated 19 December 2000, no. CPP2000/3041

conditions may contain some kind of 'overkill'. In such case, the compatibility with the Directive may be questioned. It is, however, difficult to say in the abstract whether these conditions are in conflict, since this is very dependent on the actual case of the requesting taxpayer. In case of relief, the receiving company shall inherit the tax attributes regarding the valuation of assets, the depreciation method, the reserves reducing the profits for tax purposes, etc. of the transferring company. No partial relief is possible. An 'all-or-nothing' approach applies.	

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>**5.1 The term 'provisions and reserves'**</u> No specific implementation legislation has been enacted in this respect. The general Netherlands rules apply. Therefore, the following applies. The term 'provisions and reserves' is interpreted independently from IAS/IFRS. The Netherlands Supreme Court has formulated three conditions that have to be met to capitalize a provision for tax purposes: (a) Origin requirement: the future expenses are a result of facts and circumstances, which has occurred in the period preceding the balance date; (b) Attribution requirement: The future expenses can also be attributed to that period; and (c) There is a reasonable extent of certainty that the future expenses will occur. These conditions thus similarly apply in the context of the Merger Directive. Under Netherlands tax law, no definition of tax reserves exists. Reserves can be considered as amount that are put aside with a certain purpose and constitute part of the equity of a company. Reserves can only be formed if this is provided for in Netherlands tax law. At this moment, the following reserves can be formed by a company: (a) equalization reserve; (b) reinvestment reserve; and (c) revaluation reserve. In the context of the Merger Directive, the same principles apply.	Netherlands Supreme Court 19 June 1996, BNB 1996/264 Sec. 3.53 (1)(a) ITA Sec. 3.54 ITA Sec. 13ba(1) CITA

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments There is no specific regulation in this respect.	

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves There is no specific regulation in this respect. The general principles for attribution to a permanent establishment, as explained above, *mutatis mutandis* apply (see above, section 4.3).	

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves With respect to the carry-over of provisions and reserves, the general conditions for relief apply as set out above (automatic relief and relief upon request, section 4.9). However, no further specific regulation applies in this respect.	

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry-over of losses The concept of 'losses' is not specifically defined for the purposes of implementing Article 6 of the Merger Directive. Therefore, the general Netherlands principles apply. Basically it can be held that 'loss' is negative taxable profit, as defined. Loss is the negative result of business profits, including capital gains, less business costs and capital losses. Carry-over losses are formalized each year.	Sec. 8(1) CITA Sec. 20b CITA

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment There is no specific regulation in this respect. The general principles for attribution to a permanent establishment, as explained above, *mutatis mutandis* apply (see above, section 4.3).	

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets As a general principle, losses are attributed to the taxpayer and not to the taxpayer's enterprise. Accordingly, losses can not be transferred to another taxpayer. This principle also holds true in the case of legal mergers, divisions and transfer of assets. However, based on Netherlands policy, the following exceptions apply in this respect. In the case of a legal merger, as a general rule no transfer of profits is possible. However, upon request, losses of the transferring company can be transferred to the acquiring company, provided that certain requirements are met. In the case of full division, as a general rule no transfer of losses is possible. However, based on Netherlands published policy, transfer of losses is possible, upon request, provided that the division is dominantly driven by valid commercial reasons. Additional requirements may be imposed by the Netherlands tax authorities. Since these requirements are of a very technical nature, we will not elaborate on them in more detail here. In the case of transfer of assets, as a general rule no transfer of profits is possible. However, upon request, losses of the transferring company to the receiving company is allowed in the case a Netherlands permanent establishment of a foreign company is contributed into a new established or existing Netherlands company.	Decree State Secretary of Finance dated 25 February 2002, nr. CPP2002/158, para. 3. Decree State Secretary of Finance dated 7 July 2000, no. CPP2000/811M Decree State Secretary of Finance dated 19 December 2000, no. CPP2000/3041, para. 8.1

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses Carry-over losses existing upon the legal merger, legal division or transfer of assets are 'labelled'. Such 'pre-merger losses' can, as a general rule, only be offset against profits made after the transactions mentioned to the extent loss-compensation would have been possible in case the transactions would not have taken place. The post-merger profit must	Decree State Secretary of Finance dated 19 December 2000, no. CPP2000/2682, para. 3; Decree State Secretary of

therefore be separated for purposes of carry-over pre-merger losses. Specific detailed rules apply in this respect on how to determine the order of loss compensation. Since these rules are very complex and technical, we will not elaborate on them in more detail.	Finance dated 25 February 2002, nr. CPP2002/158, para. 3

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
<u>7.1 Amended holding threshold</u> No. Where the receiving company has a holding in the capital of the transferring company, any gains accruing to the receiving company on the cancellation of its holding are exempt provided that the participation exemption is applicable. The participation exemption applies where a company has a shareholding of at least 5% in a subsidiary. However, if the assets of such subsidiary consist for 50% or more of passive, lowly taxed assets, no exemption applies (only a credit is given). In case the participation exemption does not apply, deferral may apply only upon request. If deferral is denied upon request, the compatibility with the Directive may be questioned. It is, however, difficult to say in the abstract whether such denial is in conflict, since this is very dependent on the actual case of the requesting taxpayer.	Sec. 13(1) CITA Sec. 13(2) CITA Sec. 13aa CITA Sec. 13k(5) CITA

Article 7(1) covers <u>gains</u> accruing on the cancellation of a holding. It does not cover <u>losses</u> that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
<u>7.2 Treatment of losses</u> This situation is not specifically dealt with under Netherlands tax law of administrative guidelines. In case the participation exemption applies, liquidation losses can be deducted, provided that certain requirements are met, notably that the taxpayer is liquidated and the conduct of the (former) enterprise of the liquidated taxpayer is not continued by an affiliated company. All other capital losses are exempt and thus not deductible. If the participation exemption does not apply, capital losses are deductible.	Sec. 13d CITA Sec. 13(1) CITA Sec. 8(1) CITA

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
<u>8.1 Avoidance of economic double taxation at the level of the shareholder</u> Yes. Based on the above said Netherlands concept of total profit, the shares received by the acquiring company should be valued at their fair market value upon issuance. Accordingly, double taxation of the rolled-over claim is avoided.	Sec. 8(1) CITA

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>8.2 Computation of the capital gain</u> Cash payments received constitute taxable income. Hence, no relief applies to that extent. However, under circumstances, such payments are not taxed, for instance in case the participation exemption applies.	

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>8.3 Further conditions for tax relief</u> Except for the anti-abuse requirements as set out below (section 11), no further conditions for tax relief, like nationality or continuity requirements, apply.	

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>9.1 Avoidance of economic double taxation at the level of the transferring company</u> Yes. Based on the above said Netherlands concept of total profit the	Sec. 8(1) CITA

shares received by the transferring company should be valued at their fair market value upon issuance.	

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>9.2 Further conditions for tax relief</u> Except for the anti-abuse requirements as set out below (section 11), no further conditions for tax relief, like nationality or continuity requirements, apply.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>9.3 Tax deferral</u> Where no Netherlands permanent establishment remains after the transaction, which for instance may occur where the transfer of intellectual property is involved, no relief is granted and immediate taxation takes place, without any deferral. No account has been taken in these situations of the case law of the ECJ in the context of exit-charges, for instance Case C-470/04 ('N'). One can argue, however, that less restrictive measures are conceivable, such as deferral until the moment of actual realization.	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Loss recapture for permanent establishments in third Member States</u> As a general rule, carry over losses should be recaptured to the amount of the (deemed) gain arising upon merger from the permanent establishment in the third Member State. To the extent no deemed gain arises, no recapture generally applies. Special rules apply in case of re-emigration within 8 years. Under these rules, the recapture can not be avoided by emigrating from and re-migrating to the Netherlands within a period of 8 years. Nevertheless, to the extent a Netherlands taxpayer in fact transfers its foreign permanent establishment in a foreign subsidiary to which the Netherlands participation exemption becomes applicable, a further	

recapture applies to carry over losses not yet recovered. In such case, the Netherlands participation exemption is not applicable on profits derived from the foreign subsidiary to the amount of the carry over losses not yet recovered upon the merger. To the extent the losses of the foreign permanent establishment are definite but nevertheless a recapture applies on profits derived from the foreign subsidiary (note that the value of the shares of the foreign subsidiary do not necessarily correspond to the value of the former permanent establishment), the recapture may infringe the free movement of establishment, based on the '*Marks & Spencer*' and '*Lidl Belgium*' cases.	

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>**10.2 Permanent establishment in the Member State of the receiving company**</u> The implementing legislation also covers the situation described in the final sentence of Article 10(1). In case a foreign entity transfers its Netherlands permanent establishment to a Netherlands company against the issuance of shares, tax relief can be obtained, provided that all other national requirements are met as specified above, section 4.9. Specific guidelines for the transfer of carry-over losses apply (see above, 6.3).	Sec. 14(1) CITA Decree State Secretary of Finance dated 19 December 2000, no. CPP2000/3041, para. 8.1

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>**10.3 Concept of worldwide taxation/tax credit system**</u> No.	

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
<u>**10.4 Tax deferral**</u> Since Article 10(2) has not been implemented in Netherlands tax law, no account has been taken of the ECJ case law.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies No specific implementation legislation has been enacted in this respect. The general Netherlands criteria to determine whether an entity is tax transparent or not, apply (please see 3.2). In the context of the Merger Directive, no further specific legislation or administrative guidelines have been implemented or issued in this respect. In case of transparent entities, the Netherlands applies a 'look-through' approach and will grant the benefits of the Merger Directive at the level of the participants, provided that all other requirements for the Merger Directive are met.	

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit No specific implementation legislation applies. The general concept of total profit applies.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit No specific implementation legislation applies.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders No.	

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company No specific implementation legislation applies.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation To the extent the SE is not considered a tax resident of the Netherlands anymore as a result of its transfer of seat, either under Netherlands tax law or under a double tax treaty, an exit charge applies to the extent the transferred assets do not remain effectively connected with a permanent establishment of the SE in the Netherlands. Such may be in breach with the EC Treaty (see below, under 10b.5).	Sec. 15c(1) CITA

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' This term has not been further defined or clarified.	

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency The concept of 'head office' is generally understood as to coincide with the concept of effective place of management of a company, which is the main criterion to determine tax residence under Netherlands law and under most tiebreaker clauses of double tax treaties.	

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
10b.4 Assets and liabilities not effectively connected with a permanent establishment With respect to assets not connected to a permanent establishment in the Netherlands, an immediate exit charge applies.	Sec. 15c(1) CITA

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the '*N*' case?	Reference
10b.5 Tax deferral The relevant ECJ case law, such as ECJ 11 March 2004, Case C-09/02 ('Lasteyrie du Saillant') has been considered by the Netherlands legislator in this respect. However, based on ECJ 27 September 1988, Case C-81/87 ('*Daily Mail*') the Netherlands legislator is of the opinion that immediate taxation upon transfer of seat of a company does not constitute a breach of the EC Treaty freedoms. In Netherlands literature, this view is, however, strongly opposed. It is then argued that '*Daily Mail*' is not the appropriate case in this respect. Consequently, it is highly questionable whether immediate taxation constitutes in all circumstances a proportionate means to safeguard the balanced allocation of taxation powers and/or fiscal coherence respectively.	Circular State Secretary of Finance dated 9 February 2005, no. WDB 2005/77U

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 The term 'comparable circumstances' This term has not been defined in Netherlands tax law or administrative guidelines. Nevertheless, under Netherlands tax law, the right to carry over of losses is attributed to the taxpayer and not to the taxable base. Accordingly, a SE transferring its seat from the Netherlands abroad while leaving behind a permanent establishment in the Netherlands, can use its carry over losses in order to compensate possible profits deriving from its Netherlands permanent establishment in the same way as would be possible if the SE had not transferred its seat.	

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Loss recapture for permanent establishments Carry over losses should be recapture to the extent a deemed gain arises from the permanent establishment in the third Member State upon transfer of seat. To the extent no deemed gain arises, no recapture generally applies. Special rules apply in case of re-emigration within 8 years.	Sec. 15c(1) CITA Sec. 35 DADT; Sec. 45 DADT

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
10d.1 Deemed liquidation Netherlands tax law would, as a general principle, follow the civil law perspective. Accordingly, no deemed liquidation should be recognized.	

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>10d.2 Tax treatment of third country residents</u> No distinction is made between EU/EEA and non-EU country residents. In case of non-resident individual portfolio investors, the transfer of seat from the Netherlands abroad does not result in a taxable event. In case of non-resident individual substantial shareholder (i.e. at least 5 percent of the shares), the transfer of seat from the Netherlands abroad does, under circumstances, result in a taxable event (provided that the substantial shareholding can not be allocated to a Netherlands permanent establishment of the non-resident taxpayer and provided that the right to tax is also allocated to the Netherlands under the relevant double tax treaty, if applicable). This is, in fact, tantamount to an exit-taxation for non-residents, which may be in conflict with the EC Treaty and, in case of a SE, also in breach with the Directive.	Sec. 7.7(2) ITA *a contrario* Sec. 7.5(6) and 7.5(7) ITA.

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> Yes. With respect to the legal merger, legal division, exchange of shares and transfer of assets, Netherlands tax law stipulates that no relief is granted where the relevant transaction is dominantly directed to the avoidance or postponement of taxation. A case is currently pending before the Netherlands Supreme Court where the question is whether the avoidance of Netherlands transfer tax, being no corporate income tax, is also covered. Moreover, the question is whether the criterion of 'postponement of taxation' can be considered a correct implementation of Article 11(1)(a) of the Merger Directive and if so, under which circumstances. It could be held that in cases where the transactions reflect economic reality, applying this criterion would be in breach with the Merger Directive. In cases where, by contrast, the sole aim of a transaction is to postpone taxation, applying this criterion may be allowed under the Merger Directive. The relevant transaction is deemed to be dominantly directed to the avoidance or postponement of taxation if the transaction does not take place for valid commercial reasons such as the restructuring or rationalisation of the active activities of the companies participating in the operation, unless prove to the contrary can be provided for by the	Sec. 14(4), 14a(6) and 14b(5) CITA

taxpayer. Based on *Test Claimants in the Thin Cap GLO*, such reversal of proof is permitted, unless such reversal of proof has as a result that it becomes *de facto* impossible for a taxpayer to show that the relevant transaction was business motivated. In case of legal division and transfer of assets, no valid commercial reasons are deemed to be available if the shares in the transferring or receiving company are sold in part or in whole to an unrelated party, unless the taxpayer can provide for prove to the contrary. When a comparison is made between the wording of the Article 11 of the Merger Directive and the Netherlands implementing legislation, the following differences can be recognized (Merger Directive *versus* domestic law): (a) principal objective or one of its principal objectives versus dominantly directed to; (b) tax evasion or tax avoidance versus avoidance or postponement of taxation; (c) restructuring or rationalisation of the activities *versus* restructuring or rationalisation of the active activities It is notably questionable whether or not, and if so under which circumstances, the postponement of taxation constitutes abuse in the meaning of the Directive.	

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
11.2 General anti-abuse provision Article 11(1)(a) has been transposed to Netherlands tax law.	

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the '*Cadbury*' judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' No concrete steps have been undertaken by the Netherlands legislator in this respect. In a recent circular of the Netherlands State Secretary of Finance dated 14 February, 2008, it was held that there are no Netherlands anti-abuse measures of which it is established that they are contrary to EC Law.	

Nevertheless, as the pending case discussed above (please see 11.1) shows, this is questionable as far as the implementation of Article 11(1)(a) of the Merger Directive is concerned. Notably, it is questionable when the postponement of taxation constitutes abuse in the meaning of the Directive.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions Yes, see above (please see 11.1). However, no specific ownership, nationality or residence requirements apply. Prior approval is not required. However, certainty in advance is possible.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' The concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' are not further explained in Netherlands tax law. From parliamentary history one can infer that the contribution of shares by a Netherlands substantial shareholder in a Netherlands holding against issuance of shares, followed by an immediate sale of shares by the holding to a third party, which sale is exempt under the Netherlands participation exemption, would not qualify since in such case, deferral is an aim in itself. In addition, according to the State Secretary, shareholders motives do not qualify as valid commercial reasons. However, from Netherlands case law one may draw the opposite conclusion. In addition, from a Circular of the Netherlands State Secretary of Finance, it follows that the following motives are considered to be valid commercial reasons by the State Secretary of Finance: (a) scale-advantages; (b) increase of efficiency by streamlining organization; (c) use of one another's sale channels; and (d) advantages as a result of complementary product assortments. In practice, for instance the following situations were considered to be business motivated by the Netherlands tax authorities: (e) partial division of real estate companies outside the group as a	Parliamentary proceedings II, 1998/1999, 26 727, no. 3, pp. 114-115. Circular State Secretary of Finance, undated, VN 1991/1490, point 19.

result of the introduction of an employee stock-options plan; (f) partial division of part of a particular business unit since this division had developed separately from other business units; (g) partial division of head quarter activities and subsidiaries in connection with the promotion of competition between two shareholders; and (h) partial division with the aim of cleaning the corporate structure. In Netherlands case law, a share to share merger between investment companies in order to consolidate the portfolio investments, to increase yields and to deduce costs was considered business motivated. Similarly, the limitation of civil liability was considered to be business motivated. The contribution of pension liabilities and investments in separate entities, by contrast, was not considered to be based on valid commercial reasons. It was, however, not to be considered to be dominantly driven by the avoidance or postponement of taxation.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
<u>11.6 Burden of proof</u> The Netherlands tax authorities have the initial burden of proof to establish that the relevant transaction is deemed to be dominantly directed to the avoidance or postponement of taxation. Avoidance or postponement of taxation is deemed available, if the tax authorities can prove that the transaction does not take place for valid commercial reasons such as the restructuring or rationalisation of the active activities of the companies participating in the operation, unless prove to the contrary can be provided for by the taxpayer. In case of legal division and transfer of assets, no valid commercial reasons are deemed to be available if the shares in the transferring or receiving company are sold in part or in whole to an unrelated party, unless the taxpayer can provide for prove to the contrary.	Sec. 14(4), 14a(6) and 14b(5) CITA

POLAND

Abbreviations

English	Polish	English	Polish
Accounting Act	u.o.r.	Act on Accounting	Ustawa o rachunkowości
CCC	KSH	Companies Commercial Code	Kodeks Spółek Handlowych
CIT Act	PDOP	Corporate Income Tax Act	Ustawa o podatku dochodowym od osób prawnych
FEAA	SGDu	Freedom of Economic Activity Act	Ustawa o swobodzie działalności gospodarczej
O.J.	Dz.U.	Official Journal	Dziennik Ustaw
OPE	ZCP	Organized part of an enterprise	Zorganizowana część przedsiębiorstwa
SE	SE	Societas Europea	Spółka Europejska
SE Act	s.e.u.	Societas Europea Act	Ustawa o Europejskim Zgromadzeniu Interesów Gospodarczych i Spółce Europejskiej
Tax Code	OP	Tax Code	Ordynacja Podatkowa
CLC	k.c.	Civil Law Code	Kodeks Cywilny

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.

<u>**Overall state of implementation**</u>

Poland has not implemented the original, 1990 Merger Directive (hereinafter referred to as the '1990 Directive') in one single act. The relevant provisions have been divided between the CCC (the definition of 'merger' and 'division') and the CIT Act (provisions regarding the taxation of the relevant transactions).

In particular, the provisions of the 1990 Directive have been implemented in the following acts:

(a) the CCC dated September 15, 2000 (O.J. 2000 No. 94 It. 1037) which came into force January 1, 2001;

(b) the Act amending the CIT Act, dated 27 July 2002 (O.J. 2002 No. 141 It. 1179) which came into force January 1, 2003;

(c) the Act amending the Personal Income Tax Act, the CIT Act and several other acts, dated April 20, 2004 (O.J. 2004 No. 93 It. 894) which came into force May 1, 2004.

The provisions of the Directive 2005/19/EA (hereinafter referred to as the '2005 Directive') have been implemented in the Act amending the CIT Act dated November 16, 2006 (O.J. 2006 No. 217, It. 1589) which came into force January 1, 2007.

Please note that certain provisions implementing the Directives have been designed not only to cover EU/EEA reorganizations but also to limited extent third country reorganizations (see no. 1.1).

The SE Regulation (No. 2157/2001) and the SCE Regulation (No. 1435/2003) have been implemented with the SE Act. However, the provisions ensuring the tax neutrality of the movement of the registered seat of the SE have not yet been implemented.

The Polish Ministry of Finance did not issue any official guidelines regarding the institutions covered by neither Directive. However, any potential doubts regarding the interpretation of the provisions implementing the Directives can be clarified by means of the official ruling procedure. According to the provisions of the Tax Code, every taxpayer has the right to apply to the Ministry of Finance (acting via one of the designated tax chambers) for a tax ruling on the interpretation of Polish tax provisions in his individual case. The application for a tax ruling should concern current or future events. Obtaining a tax ruling from the Ministry of Finance takes up to three months.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> The provisions of the CIT Act implementing the Directive do not restrict the 'territorial scope' only to EU/EEA mergers, divisions and partial divisions. In particular, the scope of Article 12 (4) No. 12 of the CIT Act (constituting the general rule that gains derived by the shareholder of the merged or divided companies being the nominal value of the shares received in the surviving or newly established entity do not constitute taxable income) is not limited to shareholders resident in EU / EEA countries, but applies also to shareholders from non-EU/EEA countries. At the same time, certain provisions introducing the taxation regime as stipulated in the Directive, limit the applicability of this regime on the level of the targets involved, in particular: <u>1.1.1. Mergers and Divisions</u> The tax neutrality of Mergers and divisions in ensured only in the following situations: (a) Polish companies acquiring the assets of an other Polish company; (b) Polish companies acquiring the assets of an company resident for tax purposes in one of EU Member States or an other EEA Member State; (c) companies being tax resident in one of the EU Member States or in an other EEA Member State taking over the assets of a Polish company. Additionally, Article 10 (6) of the CIT Act encompasses a provision stating that the beneficial regime is applicable to companies indicated in the Annex to the CIT Act. The Annex to the CIT Act does not include all types of companies indicated in the Annex to the Directive. In consequence, this could – in our view – potentially result in a violation of the Directive (for further details please refer to section 3.1). Note that the application of the beneficial regime as stipulated by the Directive is in no way dependent on the residency of the parent companies of the merging companies. <u>1.1.2 Exchange of shares</u> The beneficial regime stipulated by the Directive for the exchange of shares is applicable only if both the acquiring and the acquired company	Article 1 CIT Act Article 10 (2), (5), (6) CIT Act Article 12 (4d), (11) CIT Act

are resident in one of the EU Member States or another EEA Member State. Additionally, the abovementioned regulations encompass a provision stating that the beneficial regime is only applicable to companies indicated in the Annex to the CIT Act (which – according to the Polish legislator implements the Annex to the 2005 Directive). Note that, according to the Polish provisions, the application of the beneficial regime as stipulated by the Directive is not dependent on the residency of the parent companies of the companies performing the exchange of shares.	

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
<u>**1.2 Foreign Member State and third state merger**</u> As mentioned above (section 1.1) the beneficial taxation regime on the level of the receiving company can be applied only if either: (a) the receiving company is a Polish resident and the transferring company is resident in an EU/EEA Member State, or (b) the transferring company is a Polish resident and the receiving company is resident in an EU/EEA Member State, or (c) both, the receiving company and the transferring company are Polish. The CIT Act does not refer to the transactions performed between two non-resident EU companies having a PE in Poland. This could potentially be seen as an infringement of the Directive. Please note however that – in our view – the tax consequences should be determined in accordance with the general rules stipulated in the Tax Code. Also in such cases the provisions of the Directive could be invoked directly. In light of the above, the risk of infringement should be limited. However, the beneficial taxation regime on the level of the shareholders is applicable independently from the tax residence of the shareholders.	Article 10 (5) CIT Act

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term 'securities' The term 'securities' has been transcribed into the Polish law as 'shares or interest'. The term 'interest' in this context means interest in a company's capital.As the Polish tax law does not define these terms, their interpretation is possible only by referral to the company law (in particular the rules regarding the initial capital of joint stock companies (pol. 'spółka akcyjna') or limited liability companies (pol. 'spółka z ograniczoną odpowiedzialnością').	Article 152, 302 CCC

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' 2.2.1 Mergers and divisions Article 10(1) No. 5 of the CIT Act states that in case of a merger or a division any additional cash payments received by the shareholders of the transferred company, the merged companies or the divided companies constitute taxable income. However, the relevant corporate law provisions (i.e. Article 492 § 2 CCC for mergers and Article 529 § 3 CCC for divisions and partial divisions) allow only for additional payments not greater than 10% in total of the balance sheet value of the allocated shares determined in accordance with the accounting statement, or 10% of the nominal value of the shares of the newly formed company. According to legal interpretations available to us, the above CCC restrictions should apply only on a per shareholder basis. Nevertheless, for tax purposes any additional payments made in connection with a merger / division are subject to tax, unless the entire transaction benefits from the exemption regime stipulated in the CIT Act. 2.2.2 Exchange of shares According to Article 12(4)(d) of the CIT Act, one of the conditions in order to apply the beneficial taxation regime for an exchange of shares is that the additional payments received by the shareholders of the acquiring company do not exceed 10% of the nominal value of the received shares.	Article 492 § 2 CCC Article 529 § 3 CCC Article 10 (1) No. 5 CIT Act

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
<u>**2.3 Further types of merger**</u> No other forms of merger are regulated.	N/A.

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
<u>**2.4 Qualifying exchange of shares**</u> According to the CIT Act the relief is granted both in respect of the exchange of shares that finally leads to the acquisition of a majority shareholding and each subsequent exchange of shares consolidating that majority.	Article 12 (4d) CIT Act

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>**2.5 Consolidation of qualifying holding**</u> No, any further conditions are stipulated. If the acquiring company already owns a majority holding any further exchanges of shares (including the contribution of non-voting shares) would be treated as a qualifying exchange of shares.	Article 12 (4d) CIT Act

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>**2.6 The term 'branch of activity'**</u> Some Polish regulations implementing the Directive transpose the term 'branch of activity' as 'zorganizowana część przedsiębiorstwa' (eng. organized part of an enterprise; further: OPE). OPE is defined as a complex of material and non-material components organizationally and financially separated in an existing enterprise,	Article 4a (4) CIT Act

including liabilities, designed for the fulfillment of specific economic tasks, which could form an independent enterprise fulfilling such tasks on its own. As results from the above definition, the OPE requirement is stricter than the 'branch of activities' requirement stipulated in the Directive, as the CIT Act requires a financial separation of the OPE from the enterprise which is interpreted by the tax authorities as own accounts / balance sheet / income statement. The Directive does not provide for such requirements. There is no administrative guidance on this term (apart from official rulings issued in individual cases).	

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
3.1 Types of entities The Polish legislation does not cover all entities indicated in the Annex to the Directive. In particular: (a) The following company types under Belgian law are not mentioned in the Annex to the CIT Act: • 'société coopérative à responsabilité illimitée'/'coöperatieve vennootschap met onbeperkte aansprakelijkheid', • 'société en nom collectif'/'vennootschap onder firma', • 'société en commandite simple'/'gewone commanditaire vennootschap' (b) As regards companies under Danish law, the Polish law does not include the reference to 'Other companies subject to tax under the Corporation Tax Act, insofar as their taxable income is calculated and taxed in accordance with the general tax legislation rules applicable to 'aktieselskaber' as indicated in the Annex to the Directive. (c) The following company types under German law are not mentioned in the Annex to the CIT Act: • 'Versicherungsverein auf Gegenseitigkeit', • 'Erwerbs- und Wirtschaftsgenossenschaft', • 'Betriebe gewerblicher Article von juristischen Personen des öffentlichen Rechts', Also, the Polish Annex does not refer to *'other companies constituted under German law subject to German corporate tax'*. Additionally, the Annex to the CIT Act expressly mentions the company type 'bergrechtliche	(a)

Gewerkschaft'. (d) The Annex to the CIT Act does not refer to 'εταιρεία περιορισμένης ευθύνης (Ε.Π.Ε.)'·and other companies constituted under Greek law subject to Greek corporate tax. (e) The following company types under French law are not mentioned in the Annex to the CIT Act: • 'sociétés par actions simplifiées', • 'sociétés d'assurances mutuelles', • 'caisses d'épargne et de prévoyance', • 'sociétés civiles' which are automatically subject to corporation tax, • 'coopératives', • 'unions de coopératives'. Additionally, the Annex to the CIT Act mentions 'industrial and commercial public establishments and undertakings, and other companies constituted under French law' without the reference that such companies should be 'subject to French corporate tax'. (f) The Annex to the CIT Act expressly names the following companies under the Irish law: • 'public companies limited by shares or by guarantee', • 'private companies limited by shares or by guarantee'. Additionally, the annex to the CIT Act does not mention 'trustee savings banks within the meaning of the Trustee Savings Banks Act, 1989'. (g) The Annex to the CIT Act does not refer to the following companies under Italian law: • 'società cooperative', • 'società di mutua assicurazione'. (h) The Annex to the CIT Act does not refer to the following companies under the laws of Luxembourg: • 'société coopérative', • 'société coopérative organisée comme une société anonyme', • 'association d'assurances mutuelles', 'association d'épargne-pension', 'entreprise de nature commerciale, industrielle ou minière de l'Etat, des communes, des syndicats de communes, des établissements publics et des autres personnes morales de droit public'. (i) The Annex to the CIT Act does not refer to other companies constituted under Luxembourg law subject to Luxembourg corporate tax.	

(j) The Annex to the CIT Act does not refer to the following companies under Dutch law: • 'Open commanditaire vennootschap', • 'Coöperatie', • 'onderlinge waarborgmaatschappij', • 'Fonds voor gemene rekening', • 'vereniging op coöperatieve grondslag', • 'vereniging welke op onderlinge grondslag als verzekeraar of kredietinstelling optreedt'. The Annex to the CIT Act does not refer to other companies constituted under Dutch law subject to Dutch corporate tax. (k) The Annex to the CIT Act does not refer to the Austrian 'Erwerbs- und Wirtshaftsgenossenschaften'. (l) The Annex to the CIT Act does not refer to the following company types under Swedish law' • 'ekonomiska föreningar', • 'sparbanker', • 'ömsesidiga försäkringsbolag'. (m) The Annex to the CIT Act expressly indicates the SCE. (n) The Annex to the CIT Act **does not indicate the SE.** 3.1.1 Comments The consequences resulting from the abovementioned differences between the Annex to the Directive and the Annex to the CIT Act should be determined separately for non resident legal persons and for non-resident entities which are fiscally transparent. The omission of non resident companies should not trigger adverse tax implications, as the beneficial regime for mergers should be applicable to such companies according to the general provision stipulated in Article 10 (5) pt 3 of the CIT Act. However the omission of foreign fiscally transparent entities which are listed in the Annex of the Directive might infringe the Directive.	

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
3.2 Transparent entities Whether a given company should be regarded as fiscally transparent is decided solely on the basis of the law of the seat of the company in question.	Article 1 (3) CIT Act

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency Polish Double Tax Treaties provide for place of effective management as tie-breaker criterion for companies while Polish domestic regulations use the term 'place of management'. We believe the terms to have equal meaning as 'management' under the Polish law is interpreted as effective management.	Article 3 (1) CIT Act Article 4 (3) of various Polish double tax treaties

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject-to-tax clause According to the relevant provisions of the CIT Act, the beneficial regime for the transactions covered by the Directives is applicable only to companies which are subject to tax on their worldwide income in an EU Member State or an other EEA State. In practice, the beneficial regime should apply to foreign companies which will provide to the Polish tax authorities a certificate of tax residence indicating that they are subject to tax on their worldwide income in their country of residence.	Article 10 (5) No. 2 and 3 CIT Act Article 12 (4d) CIT Act

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
3.5 Shareholder requirements No, the benefits of the Directive are not restricted in respect of the nationality of the owner of the company.	N/A.

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
4.1 The concepts of 'real values' and 'value for tax purposes' The CIT Act does not define the terms 'real values' and 'value for tax purposes' for the purposes of the provisions regarding Mergers, Divisions and Partial divisions. The CIT Act provides the term 'market value' which we believe corresponds to the term 'real value'. The term market value is defined in Article 14 (2) of the CIT Act, according to which, the market value of assets is determined on the basis of market prices used in the turnover with assets of the same kind and taking into consideration the degree of usage of the assets and the time and place of their sale. The CIT Act does not include a definition of the term 'value for tax purposes', however this term is generally used to describe the tax initial value of the assets less tax depreciation write-offs.	Article 10 (1) No. 6; (2) No 1 CIT Act Article 12 (4) No. 12 CIT Act Article 14 (2) CIT Act

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions No specific guidance has been issued.	N/A.

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' **4.3.1 Mergers** Polish CIT law regarding mergers (implementing the Directive) refers neither to the term permanent establishment nor effectively connected. We believe this may be due to the fact that in case of an international merger, the assets of the acquired company should always constitute a permanent establishment for the acquiring company under Polish tax practice (accordingly, a merger shall always result in the creation of a permanent establishment).	Article 4a No. 11 CIT Act Article 5 of Polish Double Tax Treaties

4.3.2 Divisions and partial divisions. The provisions of the CIT Act regarding divisions and partial divisions do not refer to permanent establishment. As mentioned above (see 2.6) the provisions of the CIT Act introduce the OPE requirement for divisions and partial divisions (for the definition of OPE, please refer to 2.6). The tax neutrality of divisions and partial divisions is ensured only, if: (a) in case of a division the transferred assets; or (b) in case of a partial division both the transferred assets and the assets remaining with the transferring entity constitute an OPE. As mentioned above (please refer to 2.6). the OPE requirement is stricter than the 'branch of activities' requirement introduced by the Directive. There is no administrative guidance in this respect.	

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief No such limitation has been implemented.	N/A.

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment As mentioned above, in the case of mergers / divisions / partial divisions there is no reference to the concept of permanent establishment and assets being effectively connected. As the commercial law provisions regarding cross border mergers have just been introduced to the Polish legal system there is no practice in their interpretation. Nevertheless, we believe that the issue whether the assets / liabilities are effectively connected with a PE should be decided on the basis of general rules indicated in the Polish Tax Code (i.e. general succession rule). In case of divisions - as mentioned above - tax neutrality is subject to transferred and remaining assets constitute an OPE. If this condition is not met the divisions would not be tax neutral.	N/A.

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company Yes, according to Article 10 (2) No. 2 of the CIT Act, a merger is tax-neutral if the receiving company holds shares amounting to 10% or more of the initial capital of the transferred company.	Article 10 (2) No. 2 CIT Act

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral There have been no specific amendments of the CIT Act with respect to the ECJ judgments.	N/A.

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities CCC provides for the possibility of a merger with a transparent entity, provided that the transparent entity is not the receiving entity. The CIT Act does not provide any specific rules regarding the mergers with transparent entities. There are no administrative guidelines in this respect. The main criterion to define whether an entity is transparent or not is whether it is a legal person (non-transparent) or not (transparent). As mentioned above, whether a foreign enterprise has the status of a legal person is decided with reference to the statutory rules of the country where the registered seat of such entity is located (please see 3.2). Additionally, Article 5 (1) of the CIT Act states that the revenues and costs from participation in a transparent entity (in particular partnership), shall be added to the revenues of each partner proportionally to his share. If no contrary evidence is available, it shall be assumed that the shares of partners in the revenues are equal. Income received by the shareholders / partners of an entity transparent for tax purposes which is merged or divided is not exempt on the basis of the CIT provisions as they relate only to corporation entities (for further reference please refer to section 8).	Article 5 (1) CIT Act

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief Yes, in our opinion, the imposition of the OPE condition might infringe Article 4 of the Directive (for further reference please see 2.6 and 4.3).	N/A.

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
5.1 The term 'provisions and reserves' The CIT Act does not provide for these definitions. No administrative guidance in this respect has been issued. Please note however, that the Tax Code provides for the general tax succession rule in case of mergers, according to which a legal person formed (established) as a result of merger of: legal persons, commercial partnerships, commercial partnerships and companies takes over all rights and duties of each of the merging persons, partnerships or companies, said rights and duties envisaged in the provisions of tax law. We are of the opinion that the abovementioned provision would allow for a carry over of the provisions and reserves. Please note however that the scope of Article 93 Tax Code covers all mergers (i.e. is not limited to tax exempt mergers).	Article 93 TO

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments N/A (see 5.1). The CIT Act does not encompass any specific provision regarding the exclusion of provisions and reserves derived from foreign permanent establishments.	N/A.

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
<u>5.3 Allocation method for provisions and reserves</u> Polish tax law does not contain any specific provisions regarding the allocation of provisions and reserves to permanent establishments. However, in our view, potential inconsistencies with the Directive could be resolved on the basis of the general succession rule stipulated in the Tax Code and by direct application of the provisions of the Directive.	N/A.

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
<u>5.4 Further conditions for carry-over of provisions and reserves</u> N/A (see 5.1).	N/A.

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
<u>6.1 The concept of carry-over of losses</u> Article 6 has not been implemented in the CIT Act. According to the general rules stipulated in Article 7 (3) No. 4 of the CIT Act: (a) in case of the merger losses of the transferred companies are not taken into account while calculating the tax base of the receiving company; (b) in case of divisions losses of the divided company are not taken into account while calculating the tax base of the newly established or receiving company / companies. Additionally, in case of a partial division, losses not utilized for tax purposes remain with the transferring company. The term 'loss' is defined as the negative difference between the taxable income and the tax costs incurred within a tax year. The provision regarding tax losses are applicable for both cross border and domestic transactions.	Article 7 (1), (3) No. 4 CIT Act

What method is applied to allocate losses to the permanent establishment?	Reference
<u>6.2 Allocation of losses to the permanent establishment</u> N/A (please see our comments under 6.1).	N/A.

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
<u>6.3 Specific legislation for divisions/partial divisions/transfer of assets</u> Please see our comments under 6.1.	Article 7 (3) No. 4 CIT Act

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
<u>6.4 Further conditions for carry over of losses</u> N/A (please see our comments under 6.1).	N/A.

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
<u>7.1 Amended holding threshold</u> Poland has implemented the 10% holding. However, until 31 December 2008, the holding amounts to 15%.	Article 10 (2) No.2 CIT Act

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses No, Article 10(2) No.2 of the CIT Act mentions solely income resulting from the **surplus** of the value of the assets transferred over the taxable costs. A potential loss is not covered. There have been no additional guidance as to the interpretation of this provision, but we believe as merger revenue is not combined with regular business income subject to tax, loss on merger is not deductible. This may be seen as a restrictive treatment although we do not see how it could be incompliant with the Directive.	Article 10 (2) No.2 CIT Act

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholders 8.1.1 Mergers The CIT Act provides for the avoidance of double taxation on the shareholders' level in the following way: (a) the nominal value of the shares in the receiving or newly formed company does not constitute taxable income for the shareholders of the transferred company. (b) the receiving company recognizes the transferred assets in its books using the initial value specified in the records of the transferred company; (c) in case of a subsequent sale of the shares acquired during the merger, the shareholder may recognize as tax deductible costs the expenses for the purchase / take-over of the shares in the transferred company (i.e. step – up of tax value in shares takes place). 8.1.2 Exchange of Shares The CIT Act does not include any direct provision with regard to the valuation of shares by the acquiring company in case of an exchange of shares. However, in practice and per analogy to fixed assets contributed,	Article 10 (1) No. 6 CIT Act Article 12 (4) No. 12 CIT Act Article 15 (1k) No. 2 CIT Act Article 15 (1m) CIT Act Article 16g (9) CIT Act

the tax base in case of a subsequent sale of the received shares will be the nominal value of the shares of the acquiring company issued in return for the shares acquired during the exchange of shares. <u>8.1.3 Divisions and Partial divisions</u> The above rules are applicable also for divisions and partial divisions, if in case of divisions the transferred assets and in case of partial divisions both the transferred assets and the assets remaining with the transferring company constitute an OPE. Tax neutrality of divisions and partial divisions on shareholder level is secured also, if the abovementioned condition of an OPE is not fulfilled. In such a case: (a) the surplus, of the nominal value of shares issued by the receiving company over the costs of acquisition or taking up of shares in the transferred company constitutes taxable income for the shareholders of the transferred company; (b) the initial value of the assets received by the receiving company could be calculated at their market value (accordingly, step-up is possible); (c) in case of a subsequent sale of the shares, the shareholders may recognize the nominal value of the shares as tax deductible cost. As mentioned in section 2.6 the OPE requirement (as defined in the CIT Act) is stricter than the requirement of a 'branch of activities' and may thus infringe the Directive. There is no administrative guidance on this term (apart from official rulings issued in individual cases).	

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>8.2 Computation of the capital gain</u> We are not aware of any guidance issued by the Polish tax authority on the computation of the capital gain in the situation covered by Article 8(9). Any additional payments received in connection with mergers and divisions constitute taxable income for the shareholders. According to the Polish commercial law, the additional payments are possible only in cash.	Article 10 (1) No. 5 CIT Act

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>**8.3 Further conditions for tax relief**</u> No further conditions have been implemented.	Article 12 (4) No. 12 CIT Act

Article 9 – Transfer of asset

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>**9.1 Avoidance of economic double taxation at the level of the transferring company**</u> The Polish tax law ensures the tax neutrality of a transfer of an enterprise or an OPE by providing that the nominal value of the shares received by the transferring company does not constitute taxable income. It should be noted that in case of a future sale of the received shares, the tax cost is calculated as the nominal value of the shares on the day they have been received. Accordingly, when the nominal value of shares on the day they have been received equals its real / market value the transaction should be tax neutral. However, when the nominal value of shares is lower than the real / market value and the Polish tax authorities could assess the additional income (i.e. amounting of the difference between nominal and real value of shares at the time of the contribution) there is no mechanism to increase the tax basis of shares to the imputed market value. According to the Civil Law an enterprise is an organized set of tangible and intangible assets intended for business purposes. It includes, in particular: (a) individualizing specification of the enterprise or of a separate part thereof (business name of the enterprise); (b) ownership title to immovable or movable property, including equipment, materials, goods and products and other property rights to immovable or movable property; (c) rights under lease and tenancy agreements for immovable or movable property and rights to use immovable or movable property under other legal relationship; (d) receivables, rights attached to securities, and cash; (e) concessions, licenses and permits;	Article 12 (1) No. 7 CIT Act Article 12 (4) No. 4 CIT Act Article 55[1] Civil Law Article 15 (1k) Cit Act

(f) patents and other industrial property rights; (g) copyright and related property right; (h) business secrets; and (i) books and documents related to business activity '.	

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
9.2 Further conditions for tax relief No further conditions have been implemented.	N/A.

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
9.3 Tax deferral The Polish legislator has taken no special accounts with reference to the ECJ rulings.	N/A.

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
10.1 Loss recapture for permanent establishments in third Member States Poland has not implemented Article 10 of the Directive directly. Accordingly, the tax consequences of transactions covered by Article 10 of the Directive (i.e. mergers / divisions / partial divisions, where the transferred assets include a foreign PE of a Polish company) should be determined in accordance with the general rules resulting from the double taxation treaties signed by Poland. As a rule (i.e. where the respective double taxation treaties provides for the tax credit method) is shall be possible to utilize the losses of a foreign PE. However, if a respective DTC provides for the exemption method (which is a rule in Polish DTCs) the utilization of foreign PE's losses is not possible.	Article 23 of various double tax treaties

In light of the above, we believe that the Polish CIT Act is compliant with the Directive as far as the foreign PE is located in an EU Member State with which Poland has signed a DTC providing for the tax credit method. However, in case of PE's located in EU Member States with which Poland has signed a DTC providing for the exemption method, there is a risk that the Polish CIT Act might be considered as incompliant with the Directive. Please note however, that – due to the fact that the CIT Act does not provide specific rules governing transactions covered by Article 10 of the Directive – the Polish tax authorities, assessing the tax consequences of such a transaction might represent another point of view. In light of the above and taking into consideration that there is no administrative guidance and very little practice with respect to the analyzed transactions – each case should be analyzed separately.	

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> Poland has not implemented Article 10(1) of the Directive (please refer to section 10.1).	N/A.

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> Poland has not implemented Article 10(1) of the Directive (please refer to section 10.1).	N/A.

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	
<u>10.4 Tax deferral</u> The Polish legislator has taken no special accounts with reference to the ECJ rulings.	N/A.

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies Polish tax law does not include any special provisions regarding mergers with fiscally-transparent entities. The CCC indicates that fiscally transparent companies can not act as receiving companies within the meaning of the Directive. The tax consequences (on shareholder level) of mergers / divisions with fiscally transparent entities should be determined in accordance with the general rules. The wording of Article 12(4) No 12 of the CIT Act (stipulating the beneficial tax regime on shareholder level for mergers and acquisitions), this provision is applicable only in case of a merger or division of corporate entities. Accordingly, the wording of Article 12(4) No 12 of the CIT Act could suggest that the income realized by a shareholder of a transferred fiscally transparent entity should be subject to tax in Poland (i.e. this could be interpreted as an implementation of Article 10(1) of the Directive). Please note however that the CIT Act does not provide for a relief for the tax which, but for the provisions of this Directive, would have been charged on the fiscally transparent company on its income, profits or capital gains, in the same way and in the same amount as that State would have done if that tax had actually been charged and paid as stipulated in Article 10 (2) of the Directive. In light of the above we believe, the Polish provisions could be in violation of the Directive.	Article 12 (4) 12 CIT Act

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit Poland has not implemented Article 10a of the Directive (please see 10a.1).	N/A.

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit Poland has not implemented Article 10a of the Directive (pls. see 10a.1).	N/A.

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
<u>10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders</u> Poland has not implemented Article 10a of the Directive. However, note that - as mentioned under 3.2 above - whether a given company should be regarded as fiscally transparent is decided solely on the basis of the law of the seat of the company in question.	N/A.

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
<u>10a.5 Comparison with a resident fiscally transparent company</u> Poland has not implemented Article 10a of the Directive (please refer to section 10a.1).	N/A.

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
<u>10b.1 Exit taxation</u> Poland has implemented the Council Regulation 2157/2001 on the Statute for a European Company ('the SE Statute'). Accordingly – under Polish commercial law - a transfer of the registered seat without liquidation of the SE is possible. Nevertheless, Poland has not implemented Article 10b of the 2005 Directive. Therefore the CIT Act does not include any provisions regarding the transfer of the registered seat of the SE/SCE. Accordingly, the transfer of the registered seat of the SE/SCE would be subject to tax in Poland under the general rules i.e. only if – as a consequence of the transfer of the registered seat – the SE/SCE would be liquidated. The SE/SCE would be liquidated in case of infringement of the requirements indicated in the Council Regulation 2157/2001 on the	Article 10 (1) CIT Act

Statute for a European Company (i.e. in case when after the transfer of the registered seat of the place effective management would remain in Poland).	

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
<u>10b.2 The term 'head office'</u> As mentioned under 10b.1. Poland has not implemented Article 10b of the Directive. National legislation implementing Article 7 of Regulations 2157/2001 transposes the term 'head office' as 'the place of main management'. No further guidance as to the interpretation of this term has been issued.	Article 54 SE Act

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
<u>10b.3 Head office and tax residency</u> Yes. According to the Polish CIT Act, a company is treated as a Polish resident for tax purposes, if it has its registered seat or place of management within the territory of Poland. As mentioned above (please see 10b 2) the term 'head office' has been implemented into the Polish legal system as 'place of main management'. Additionally, Article 54 of the SE Act includes the requirement stipulated in Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') that the 'registered office' be located in the same Member State as the 'head office'. In light of the above, we believe that – due to the fact that the head office has to be localized in the same Member State as the registered office, the institution of the head office should have no impact on the question of residence of the SE.	Article 3 (1) CIT Act

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>10b.4 Assets and liabilities not effectively connected with a permanent establishment</u> Poland has not implemented Article 10b of the 2005 Directive, therefore the CIT Act does not include any provisions regarding the assets not connected to a permanent establishment in the Member State from the	N/A.

registered office is transferred. There are no rules regarding this issue. However transfer of permanent establishment is possible for commercial purposes according to general tax succession rules. In such a case no adverse tax implications should apply.	

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the *'N'* case?	Reference
<u>10b.5 Tax deferral</u> As the rules regarding the taxation of the transfer of the registered office of the SE/SCE have been not implemented into the Polish legal system, the legislation of the ECJ in this respect has had no impact on the Polish provisions.	N/A.

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
<u>10c.1 The term 'comparable circumstances'</u> Poland has not implemented this provision directly. Accordingly, the tax treatment of losses of permanent establishments of SEs or SCEs should be decided on the basis of general rules. According to the provisions of the CIT Act losses can be carried forward for not more than 5 consecutive years. However, in a single year not more than 50% of the loss can be utilized. The general rules are applicable for both Polish and EU based entities. In consequence we believe this issue is compliance with the Directive.	Article 3 (2) CIT Act Article 7 (5) CIT Act

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
<u>10c.2 Loss recapture for permanent establishments</u> Please refer to our comments under 10c.1.	N/A.

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>**10d.1 Deemed liquidation**</u> Article 10d of the Directive has not been transposed into the Polish tax law. However, according to the SE Act, if only the registered seat is transferred whilst the place of management is maintained, the relevant Register Court has the right to start a procedure which may finally lead to the liquidation of the SE/SCE. If the SE/SCE is liquidated, under current wording of CIT Law liquidation profits received by the shareholder are taxable at shareholder level this would lead to taxation of the liquidation proceeds based on general rules.	Article 48-57 SE Act

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>**10d.2 Tax treatment of third country residents**</u> Article 10d of the Directive has not been transposed into the Polish tax law.	N/A.

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>**11.1 Transposition of anti-abuse provisions**</u> Poland has encompassed Article 11(1) (a) of the Directive into Article 10(4) of the CIT Act, according to which the beneficial taxation regime for Mergers, Divisions and Partial Divisions is not applicable if the transaction in question is not carried out for valid commercial reasons but has as its principal or one of its principal objective tax avoidance or tax evasion. There has been almost no practice in the use of this provision by the tax authorities. In particular, the anti-abuse provision has been subject of only	Article 10 (4) CIT Act Official Ruling Sign.: ZD/423-251/04

one tax ruling, in which the tax office indicated that - as there are no general rules / guidance as to the determination whether a given transaction is carried out solely for the purpose of tax avoidance – each transaction should be analyzed separately. Please note also, that Article 10(4) of the CIT Act is applicable solely for Mergers, Divisions and Partial Divisions. Accordingly it does not apply to exchange of shares and transfer of assets.	

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
11.2 General anti-abuse provision N/A (see above 11.1).	N/A.

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the '*Cadbury*' judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' The Polish legislation has not been amended specifically in respect of the findings in '*Cadbury*'. Additionally, as mentioned above (please see 11.1) there has been very little practice in the interpretation / use of the anti-abuse provisions by the tax authorities.	N/A.

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions No such restrictions have been imposed.	N/A.

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' Please refer to our comments to 11.1.	N/A.

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof The burden of proof lies principally with the taxpayer.	N/A.

PORTUGAL

Abbreviations

English	Portuguese	English	Portuguese
CITC	CIRC	Corporate Income Tax Code	Código do Imposto sobre o Rendimento das Pessoas Colectivas
OG	DR	Official Gazette	Diário da República
CA	POC	Chart of Accounts	Plano Oficial de Contabilidade
GAAP	PCGA	Generally Accepted Accounting Principles	Princípios Contabilísticos Geralmente Aceites
CCC	CSC	Commercial Companies Code	Código das Sociedades Comerciais
GTL	LGT	General Tax Law	Lei Geral Tributária
SE	SE	Societas Europaea	Sociedade Europeia
SCE	SCE	European Cooperative Societies	Sociedade Cooperativa Europeia
PE	EE	Permanent Establishment	Estabelecimento Estável
DGT	DGCI	Directorate General of Tax	Direcção-Geral dos Impostos
PITC	CIRS	Personal Income Tax Code	Código do Imposto sobre o Rendimento das Pessoas Singulares
FMV	VM	Fair Market Value	Valor de Mercado

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.

Overall state of implementation

The Merger Directive has been implemented by the Decree-Law n.º 123/92, dated of 2 de July. Decree-Law n.º 123/92 has transposed the Merger Directive into domestic tax law by amending Article 62, 63 and 64 of the CITC and by introducing a new Article 62-A (Mergers and Divisions between companies of different Member States) to the CITC. Decree-Law n.º 123/92 came into effect on 1 January 1992.

The version introduced by Decree-Law n.º 123/92 was amended several times. The most important amendment was made by Decree-Law n.º 221/2001, dated of 7 August 2001, which has simplified tax neutrality regime by introducing in the CITC the definitions of merger, division, etc. The transfer of PE of non-resident entities located in Portugal was included in the regime. Basically, whilst in the previous version of the CITC Articles there was a separation between domestic and cross-border mergers, the new wording as from August 2001 has harmonized the regime and introduced a wording very similar to that of the Merger Directive. As a result, the tax neutrality regime has been included in Article 67 to 72 of the CITC.

Law n.º 60-A/2005, dated of 30 December 2005(2006 Budget Law), that came into force on 1 January 2006, introduced the exit taxation concerning the redomiciliation of companies. Amongst the provisions of Article 76-A to 76-C of the CITC, there are some rules of tax neutrality, inter alia, when the company that transfers registered office and place of effective management abroad maintains a PE in Portugal.

Law n.º 53-A/2006, dated of 29 December (2007 Budget Law), has transposed Council Directive n.º 2005/19/CE, dated of 17 February, and came into effect on 1 January 2007.

Guidance issued by the tax administration relevant for the interpretation of the implementation of the Merger Directive is included in the following publications:

(a) DGCI decision dated of 9 November 2003 regarding Article 67 – Exclusion of a 'transfer as a going concern' from the concept of the transfers of assets for tax neutrality purposes.

(b) Secretary of Tax Affairs decision 1204/2004 dated of 19 May – Denies the tax neutrality regime for downstream mergers.

(c) Secretary of Tax Affairs decisions 36/2005 and 37/2005, dated of 13 January 2005– Denies the tax neutrality regime for a merger where no exchange ratio was determined for the shareholders of the merged company (which could be the same of the incorporating company).

(d) Secretary of Tax Affairs decision dated of 2 June 2005 – Excludes from the merger definition the dissolution and liquidation of a company that transfers all its assets and liabilities to its sole shareholder.

(e) Ministry of Finance Circular 7/2005 dated of 16 May – States that the deduction of tax losses in case of merger, division and transfer of assets is limited to a deduction plan authorized by the Ministry of Finance and defines the methodology to utilize such transferred tax losses.

(f) DGCI decision dated of 21 July 2004 – Non-application of adjusted sales proceeds provision concerning the transfer of immovable property or rights attached thereto whenever a tax-neutral transaction is concerned.

(g) Sub-Director General decisions dated of 11 December 2001 and 19 March 2004 – Concerning the retroactive effects of mergers executed under the tax neutrality regime.

(h) Sub-Director General decision dated of 30 January 2008 – States that the mere detachment of shareholdings does not qualify for a tax-neutral division. However, if that is accompanied with the transfer of other assets and liabilities associated with the business of managing shareholdings, it can be considered as a branch of activity hence qualifying for tax neutrality.

(i) Ministry of Finance Circular 8/2004 dated 30 March – Regarding the maintenance of original acquisition date for shares acquired via a tax-neutral transaction.

Directive 2005/56/CE was not yet implemented despite of the transposition period has elapsed last 15 December 2007. In practice, local lawyers defend that it is possible to execute cross-border mergers.

The SE-Regulation (n.º 2157/2001) has been supplemented with Decree-Law n.º 2/2005, dated of 4 January, which has approved the legal regime of SE's and that has amended Commercial Registry Regulation, National Registry of Collective Bodies Regulation and Notary Code.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> The expression 'in which companies from two or more Member States are involved' has been interpreted as comprising only the companies directly involved in the transaction and not the parent companies. No reference is made to shareholders, except for exchange of shares. The transferring and the receiving companies must be established in European Union Member States, provided all companies meet the conditions of Article 3 of the Merger Directive.	Article 67(6) of CITC Article 67(7)(a) and (b) of CITC

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
<u>**1.2 Foreign Member State and third state merger**</u> CITC tax neutrality regime does not apply to third country companies, but only to EU companies. In case of mergers, divisions and transfer of assets no reference is made to the shareholders. The tax residency of the shareholder is only relevant for exchange of shares.	Article 67(6) of CITC Article 67(7)(a) and (b) of CITC

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
<u>**2.1 The term 'securities'**</u> With respect to the term 'securities', in the meaning of the CITC, it should correspond to shares and other interests representing the registered capital of companies in accordance with CCC (hereinafter referred as 'shares').	Article 67(1), (2), (3) and (5) of CITC

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
<u>**2.2 The term 'cash payments'**</u> CITC provides a 10% cap – based on nominal value of shares or, in its absence, on the corresponding book value – on cash payments for mergers, divisions, partial divisions and exchanges of shares, which applies on a per shareholder basis and not on an overall basis.	Article 67(1)(a) and (b) of CITC Article 67(2)(a) and (b) of CITC Article 67(5) of CITC

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
<u>2.3 Further types of merger</u> No other types of merger.	Article 67(1) of CITC

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
<u>2.4 Qualifying exchange of shares</u> The definition of exchange of shares includes the exchange that leads to the majority of voting rights and any further exchange of shares that increases the stake in the acquired company.	Article 67(5) of CITC

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>2.5 Consolidation of qualifying holding</u> No further conditions.	Article 67(5) of CITC

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>2.6 The term 'branch of activity'</u> CITC has transposed the definition of the Merger Directive above. Until 31 December 2006, the term 'branch of activity' – relevant both for divisions and transfers of assets – also included a shareholding or shareholdings of at least 10%. However, this reference was eliminated as from 1 January 2007 onwards, hence nowadays the term only includes 'business units'. Notwithstanding, we note that tax authorities have already recognized that	Article 67(4) of CITC

a transfer of shareholdings together with other resources can consubstantiate a 'branch of activity'.	

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> CITC applies the Merger Directive to all companies established in Portugal or in another EU Member State, provided all companies meet the conditions of Article 3 of the Merger Directive. CITC also applies the Merger Directive to other entities than companies subject to CIT and tax resident of Portugal, as well as to its members. Domestic law also allows the tax neutrality regime application to mergers and divisions, executed under the applicable law, concerning entities (other than companies) subject to CIT that are resident of Portugal and its members, as well as to transfers of assets and exchange of shares when a collective body (not a company) is involved. According to the Annex to the EU Merger Directive, are listed as covered entities all Portuguese commercial companies or civil companies under a commercial form as well as other collective bodies that carry out commercial or industrial activities (see paragraph u) of the Annex, currently in force). Further, our domestic tax law refers that when are involved companies resident in other EU Member States they can only benefit from the tax neutrality regime if they comply with the conditions stated in Article 3 of the EU Merger Directive, which includes being one of the entities listed in Annex. Therefore, we do not envisage a contradiction between our domestic tax law and the Directive.	Article 67(9) of CITC

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>3.2 Transparent entities</u> No.	

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
<u>3.3 Qualification of tax residency</u> <u>3.3.1 Tax residency under domestic law</u> A company is tax resident of Portugal if it's registered office or it's place of effective management is located in Portugal. <u>3.3.2 Tax residency under Double tax conventions</u> Portuguese double tax conventions provide for the tiebreaker criterion to determine the tax residency of companies based on place of effective management.	Article 2(3) of CITC Article 4(3) of OECD Model Tax Convention

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>3.4 Subject-to-tax clause</u> The subject-to-tax clause of Article 3 (c) of the Merger Directive has been implemented in the CITC. As a result, tax neutrality does not apply to transactions (mergers, divisions, partial divisions and transfers of assets) performed by entities that are exempt from CIT or which taxable profits are determined under the simplified regime of taxation. Based on old administrative guidance for the purposes of the same concept 'subject and not exempt from tax' in relation to the participation exemption regime applicable to dividends, one may say that should only be excluded companies that are subjectively exempt from taxes on a permanent and overall basis. Please find below the main features of the simplified regime of taxation: (a) no costs are allowed against the gross revenues to compute taxable income; (b) gross revenues (including capital gains) are taxed at an effective rate of 4% or 9% (20% rate x 20% or 45% deemed margin) depending on the activity. In order for a resident company that carries out a commercial, industrial or agricultural activity, neither exempt nor subject to a special tax regime, to fall within the scope of the simplified regime of taxation the following requirements must be met: (a) the company should not be subject to statutory audit;	Article 67(7)(a) of CITC

(b) the total annual gross revenues in the previous year should not exceed € 149.639,37; and (c) no election is made to apply the standard CIT regime of taxation. We note that under the anti-abuse provision stated in the tax neutrality regime, the tax authorities could always challenge tax neutrality if the operation was tax driven, which could result, inter alia, whenever the companies involved do not have all its income subject to the same CIT regime. Therefore, considering that companies under the simplified regime of taxation are subject to CIT and are obliged to maintain organized books, we see no major reason to not allow the tax neutrality, at least, when all entities involved are being taxed under the simplified regime.	

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>3.5 Shareholder requirements</u> No such limitation exists. However, in case of exchange of shares, the tax neutrality regime only applies to EU or third countries shareholders of the acquired company should they receive shares in a Portuguese resident acquiring company. Therefore, deferral is not available to EU shareholders of Portuguese acquired companies receiving shares in other EU country resident companies. Accordingly, taxation is triggered, but taxation on the capital gains realized by non-resident shareholders can be avoided under our domestic tax law (not applicable if any of the following situations occurs: i) the shareholder is located in a tax haven territory, or ii) the main assets of the Portuguese company are composed of immovable property located in Portugal, or iii) the foreign shareholder is held in 25% or more by Portuguese resident entities) or under a double tax treaty entered with Portugal (taxation in the country of residence of the beneficiary of the income and not in the source country, although with some exceptions). Whether the above restriction is contrary to the Directive it is doubtful. Indeed, at the time of the exchange of shares there seems to be discrimination between Portuguese resident and EU resident shareholders. Nevertheless, since non-residents are generally exempt from capital gains tax, in practice, there may be no tax impact. This potential ‘discrimination’ is based on the fact that a subsequent disposal of the shares in the acquired company – being this non-resident – would not be caught by Portuguese taxation. Accordingly, although tax neutrality is a deferral of taxation regime, allowing tax neutrality for a non-resident shareholder exchanging the shares in a Portuguese acquired company by the shares in a non-Portuguese acquiring company would result in a final exemption.	Article 71(2)(b) of CITC

Article 4 – Carry over of balance sheet value

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>4.1 The concepts of 'real values' and 'value for tax purposes'</u> According to CITC the concept of 'real value' with regards to fixed assets corresponds to market value, the same being applicable to other assets and liabilities. The 'value for tax purposes' should correspond to the book value determined in accordance with Portuguese GAAP and adjusted for tax purposes, which may also comprise revaluations of fixed assets performed under tax law. Results on transferred assets and liabilities shall be computed by receiving company as if no merger, division or transfer of assets had occurred, i.e., considering the same 'value for tax purposes'.	Article 43(3) of CITC Article 68(3) and (4) of CITC

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
<u>4.2 Specific guidance for divisions/partial divisions</u> The valuation of assets in case of divisions and partial divisions follows the same rules applicable for mergers.	Article 43(3) of CITC Article 68(3) and (4) of CITC

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>4.3 The concepts of 'effectively connected' and 'permanent establishment'</u> The concept of 'effectively connected' is not specifically defined. The concept of 'permanent establishments' is defined in the CITC and follows the OECD definition. However, tax neutrality for a merger, division or transfer of assets requires that the transferred assets and liabilities are either acquired by a Portuguese resident receiving company or allocated to a PE in Portugal of an EU Member State resident receiving company, as follows: (a) transfer from a Portuguese resident company to another Portuguese resident company; (b) transfer from a Portuguese resident company to an EU Members State resident company that allocates the assets and liabilities to a	Article 5 of CITC Article 68(1) of CITC

Portuguese PE; (c) transfer of a Portuguese PE from an EU Member State resident company to a Portuguese resident company, with the consequent extinction of the PE; (d) transfer of a Portuguese PE from an EU Member State resident company to another EU Member State resident company; (e) transfer of an EU Member State PE from a Portuguese resident company to another Portuguese resident company. The Portuguese PE definition is similar to the OECD Model Tax Convention. The main difference is the building site rule, where a 12-month period is stated in the OECD Model Tax Convention and a 6-month period is stated in the domestic tax law.	

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief No recapture of depreciation. However, depreciations by receiving company on transferred fixed assets should follow the same regime applied by the transferring company.	Article 68(4)(b) of CITC

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment There are no specific rules applicable to assets and liabilities not connected with a PE. In principle, they should be out of the scope of the tax neutrality regime hence taxable under Corporate Income standard rules, depending on the type of assets being transferred. In case of transfer of fixed assets not connected with a PE, a capital gain or loss will have to be computed. The gain or loss must be determined separately for each of the items included in the transfer (independently of its value or nature). Concerning fixed assets, the amount subject to taxation is the balance between the capital gains and capital losses, calculated for tax purposes. For tax purposes the fixed assets acquisition cost is adjusted by the application of a monetary coefficient. A partial relief can apply if the sales proceeds are reinvested in the acquisition of other fixed assets. In case of transfer of other assets, namely stock, a profit or loss will be computed. No monetary coefficients are applicable. There are specific rules concerning the disposal of shares, which may	

result in the full or partial exemption on capital gains as well as on the full or partial non deductibility of losses.	

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company Yes, no taxation should arise from the cancellation of the shareholding held by the receiving company in the transferring company.	Article 68(6) of CITC

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral Under PITC, tax rollover on capital gains for individual shareholders, as a result of tax-neutral transactions, ceases to apply should the individual changes his/her tax residency abroad. This exit taxation rule may be seen as contrary to EU Law. Once again, this rule is aimed at preventing a final exemption when tax neutrality only aims at tax deferral. Taxation for shareholders is also triggered, under exit tax rules when a company changes its registered office and place of effective management abroad (transfer of tax residence from Portugal to another country). Whether this taxation rule is contrary to EU Law It is doubtful since the potential taxation for the shareholders of a company that transfers its tax residence abroad applies to both resident and non resident shareholders.	Article 10(9) and (10) of PITC Article 76-C of CITC

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities Not applicable. The CITC only states rules applicable to resident transparent entities. It is not entirely clear whether resident tax transparent entities can enjoy from the tax neutrality benefits.	Article 6 of CITC

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
<u>**4.9 Further conditions for tax relief**</u> The receiving company shall inherit the tax attributes regarding the valuation of assets, the depreciation method, the provisions, etc of the transferring company. In addition, the period that the business assets and liabilities of the transferring company have been held shall also be transferred to the receiving company. Please note that tax neutrality requires that the receiving company accounts for the transferred assets and liabilities at the same amounts as previously stated in the books of the transferring company. No tax neutrality should apply if, as a result of a merger, division or transfer of assets, are transferred ships or aircrafts, or movable assets (non-immovable assets or assets other than real estate) associated with the exploration of ships or aircrafts, to an entity engaged in international traffic not resident in Portugal. Accounting and tax effects of mergers and divisions can be reported to a date prior to that of legal merger or division (registration at the commercial registry), provided that both dates fall within the same tax year and that retroactive effects are foreseen in the merger or division project. Transferring company should include in its tax file a declaration issued by the receiving company stating that the latter shall carry over book and tax values, depreciation, provisions, and so forth. If applicable, such company should also have a declaration issued by other EU Member State tax authorities confirming the eligibility of the companies involved for the purposes of the Merger Directive.	Article 68(3) and (4) of CITC Article 67(8) of CITC Article 68(7) and (8) of CITC Article 72(1) of CITC

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>**5.1 The term 'provisions and reserves'**</u> The term provisions follow Portuguese GAAP. For tax purposes, provisions will only be recognized if they meet the requirements of deductibility stated in the CITC. The following provisions can be deductible for tax purposes: (a) bad or doubtful debts, based on a judicial decision or on an ageing analysis of the accounts receivable; (b) inventory losses (inventory carrying values in excess of market value);	Article 34 to 38 of CITC

(c) provisions to cover obligations or expenses to be incurred with judicial claims; (d) technical provisions imposed by the Bank of Portugal or by the Portuguese Insurance Institute (e) trovisions created by oil extraction industries to the recovery of oil wells; (f) trovisions created by other industries to cover expenses incurred with the environmental recovery of extraction sites. Reserves derived from revaluation of fixed assets can only be created with taxable effect – increase of depreciation – under tax Decree-Laws.	

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments CITC only excludes from the tax neutrality regime the gains associated with provisions related to credits (receivables), stock (inventory) and obligations as well as incumbencies being transferred, provided they respect to a PE located outside the Portuguese territory and whenever they are transferred to non Portuguese resident entities. There are no specific rules for distinguishing the provisions from a foreign PE from provisions of the remaining company, but identification can be made in accordance with the allocation of the provisions in the books of the PE as well as considering where the underlying assets and liabilities are accounted for. In practice, such provisions should be disclosed in the closing tax balance sheet of the PE of the transferring company.	Article 68(1) of CITC

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves Identification can be made in accordance with the allocation of the provisions in the books as well as considering the underlying assets and liabilities / branch of activity being transferred.	

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves N/A.	

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry-over of losses The meaning of 'losses' is not defined for the purposes of the tax neutrality regime. Therefore, it should correspond to the tax loss computed based on the annual CIT return, i.e., accounting profits adjusted as per the CITC.	

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment The losses allocated to the Portuguese PE of the EU Member State receiving company are, as a rule, those brought forward by the transferring company, provided all assets and liabilities of the latter are allocated to the former and are considered for the computation of taxable profits at the level of the PE.	Article 69(3)(c) of CITC

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets Yes, specific rules apply. No transfer of tax losses is allowed when a partial division is concerned. Under a division, tax losses are attributed to the receiving companies proportionally to the net assets being transferred to each of those companies.	Article 69(3) of CITC

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
<u>6.4 Further conditions for carry over of losses</u> The transfer of tax losses is only allowed if there are valid commercial reasons for the transaction. Moreover, a petition to the Minister of Finance should be filed until the end of the month following that of registration of the transaction. The Minister of Finance can determine caps for the annual use of the transferring company tax losses against the receiving company taxable profits. These caps are based on the increase of taxable profits and the proportion of equities. The prior notification and caps are applicable to both domestic and cross-border restructurings. It is doubtful whether such procedures and limitations are contrary to EU Law. The purpose of the cap is to have an 'objective' rule to allocate the tax losses being transferred to the business that was transferred by the company that generated such losses, in comparison with the business of other companies involved.	Article 69(2), (4) and (5) of CITC

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
<u>7.1 Amended holding threshold</u> No threshold has been introduced for this purpose.	Article 68(6) of CITC

Article 7(1) covers <u>gains</u> accruing on the cancellation of a holding. It does not cover <u>losses</u> that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
<u>7.2 Treatment of losses</u> Yes, CITC refers also losses. Losses are not deductible.	Article 68(6) of CITC

Article 8 – Tax relief for shareholders

<table>
<tr><th>Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at ‘real’ or ‘market’ value?</th><th>Reference</th></tr>
<tr><td> <u>8.1 Avoidance of economic double taxation at the level of the shareholder</u>
The Portuguese CITC does not state a ‘real’ or ‘market’ value for the acquiring company in relation to the shares received in the acquired company under an exchange of shares. However, in practice, this is allowed, i.e., the acquiring company may book the shareholding in the acquired company at FMV and this amount can be relevant for tax purposes.
Shareholders of the acquired company are only required to attribute the same tax value of the contributed shares (as registered in the books) to the shares received in the acquiring company. The received shares should be registered separately in regards to other shares held by the shareholders in the acquiring company. Contrary to mergers and divisions, the shareholders of an acquired company are not obliged to maintain the same book value but only the tax value.
Shareholders of the acquired company should include in its tax file several documentation, namely:
(a) a declaration describing the exchange of shares, date of execution, identification of the entities involved, number and nominal value of shares contributed and received, value by which the contributed shares were registered in the books, amount in cash received (if any), gain or loss that would have been computed had the transaction been made at FMV;
(b) a declaration issued by the acquiring company confirming that, as a result of the exchange of shares, it became the holder of the majority of the voting rights in the acquired company;
(c) a declaration issued by other EU Member State tax authorities confirming the eligibility of the companies involved for the purposes of the Merger Directive or that the shareholder is resident therein (only required if non Portuguese companies are involved). </td>
<td> Article 71(1) and (4) of CITC Article 73(3) of CITC </td></tr>
</table>

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
8.2 Computation of the capital gain No guidance has been issued. In principle, the full cash amount should be subject to tax and the acquisition cost of the shares in the merged/divided/ acquired company should be used to compute taxable gains or losses in relation to the shares received in the receiving/acquiring company. Shareholders of merged or divided companies should maintain the same book (and tax) value of the shares in the transferring company for the shares received in the receiving company. For divisions, such value is divided proportionally to the net assets. Shareholders of merged or divided companies should include in its tax file a declaration stating: (a) the date of the transaction, nature of the transaction and identification of entities involved; (b) the number and nominal value of shares delivered and received, as well as the value by which the delivered shares were registered in the books and its respective acquisition date; (c) the amount received in cash (if any); (d) the percentage held before and after the transaction in the receiving company.	Article 70(1) and (3) of CITC Article 73(4) of CITC

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
8.3 Further conditions for tax relief Under exchanges of shares, tax rollover for foreign shareholders in a Portuguese resident acquired company is only available should the acquiring company also be Portuguese resident.	Article 71(2) of CITC

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>**9.1 Avoidance of economic double taxation at the level of the transferring company**</u> No since, under transfers of assets, shares received by the transferring company in the receiving company are deemed acquired, for tax purposes, by an amount equivalent to the net assets book value contributed by the former to the latter.	Article 68(5) of CITC

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>**9.2 Further conditions for tax relief**</u> The same as applicable to mergers. Please see 4.9 above.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>**9.3 Tax deferral**</u> Please refer to 4.7 above.	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Loss recapture for permanent establishments in third Member States</u> No loss recapture.	

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> Transfer of a Portuguese PE of an EU resident company into a Portuguese resident company could be deemed as a transfer of assets and benefit from the tax neutrality regime (including the transfer of losses), provided all the requirements of the regime are met.	

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> Yes, Portugal would tax the unrealized capital gains and would allow for a foreign tax credit. The amount of the foreign tax that would be due in the EU Member State of the PE, if the transaction was made at FMV and not under the Merger Directive, has to be certified by the other Member State tax authorities. Currently, if the company has no tax basis to offset the foreign tax credit in the same fiscal year, no carry back or carry forward of foreign tax credit is allowed (until 2005, there was a 5-year carry forward system applicable to foreign tax credits).	Article 68(2) of CITC Article 72(2) of CITC

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
<u>10.4 Tax deferral</u> No account has been taken so far.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
<u>10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies</u> N/A (Please see 3.2).	

How have the 'profits' of an <u>acquired</u> company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
<u>10a.2 Tax base for notional tax credit</u> N/A.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an <u>acquired</u> company?	Reference
<u>10a.3 Determination of notional tax credit</u> N/A.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
<u>10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders</u> N/A.	

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company N/A.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation No taxation, unless there is also a transfer of the place of effective management abroad. Even if both registered office and place of effective management are transferred abroad, taxation for the SE (or any other company for that matter) can be avoided in relation to the assets and liabilities that remain allocated to a PE in Portugal, provided certain requirements are met (similar to those applicable to mergers, divisions and transfers of assets) as follows: (a) the assets and liabilities are registered in the PE books by the same amount that had in the books of the resident company; (b) the above amounts derive from the application of the CIT Code provisions; (c) the future computation of results in the PE should be performed as if no change of residence had occurred; (d) depreciation and amortization should be calculated by the PE on the same basis it was determined in the resident company; (e) transferred provisions should have in the PE, for tax purposes, the same regime that was applicable in the resident company. Nevertheless, shareholders would still be subject to tax, since there is a deemed liquidation for taxation purposes. Indeed, contrary to the company, where a rule exists to apply the tax neutrality regime, there is no such provision concerning the shareholders.	Article 76-A of CITC Article 76-C(3) of CITC

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
<u>**10b.2 The term 'head office'**</u> The definition given for the term 'head office' should be that stated in the CCC and is equivalent to 'registered office'. No definition is stated in the tax law.	Article 12 of CCC

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
<u>**10b.3 Head office and tax residency**</u> The concept of 'head office' should be equivalent to that of 'registered office' hence is one of the criteria stated in the Portuguese CITC to define tax residency for companies.	Article 2(3) of CITC

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>**10b.4 Assets and liabilities not effectively connected with a permanent establishment**</u> Assets not connected to a Portuguese PE that is maintained by the SE after transferring both the registered office and the place of effective management abroad shall be deemed disposed or transferred at FMV. Capital gains would be subject to taxation. It is doubtful whether such taxation is contrary to EU Law. Once again, the rule is to prevent losing the right of taxation that would not be available in future under domestic law when the assets are disposed and no longer held by a resident company or allocated to a local PE of a foreign company. The same should apply to assets transferred out of a Portuguese PE or upon closing of the PE.	Article 76-A(1) of CITC Article 76-B of CITC

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the '*N*' case?	Reference
<u>**10b.5 Tax deferral**</u> None.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 The term 'comparable circumstances' No definition of the term 'comparable circumstances' is stated in the tax law. The tax losses could be transferred to the Portuguese PE provided an authorisation from the Ministry of Finance is obtained at request of the PE until the end of the month following the close of activity (transfer of residence abroad). Based on the wording of the tax law, there should be a correspondence between the tax losses and the assets and liabilities that remain allocated to a local PE.	Article 76-A(4) of CITC Article 15(1)(c)(1) of CITC

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Loss recapture for permanent establishments No loss recapture. Taxation should arise on assets allocated to a foreign PE, although no foreign tax credit is foreseen in the tax law as it occurs for mergers, divisions or transfers of assets. It is doubtful whether the absence of a (deemed) foreign tax credit is contrary to EU Law. If, in substance, the situation is similar to that of a cross-border merger whereby the resident company becomes a PE of an EU company, it makes sense to treat the foreign PE in the same way (including allowing a foreign tax credit).	

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
10d.1 Deemed liquidation If both the registered office and the place of effective management are transferred abroad, for tax purposes such transfer is treated as liquidation at the level of the shareholders, being taxed herein. Taxable gain should correspond to the difference between FMV of the company's assets and liabilities less the acquisition cost of the shares.	Article 76-C of CITC Article 75(2), (3) and (4) of CITC

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>**10d.2 Tax treatment of third country residents**</u> No different tax treatment for third country resident shareholders. However, we note that Portuguese resident shareholders may benefit from a full or partial tax exemption on the gain derived from deemed liquidation and treated as assimilated to investment income. We note that the exit rules simply refer to the provisions applicable in case of a company's liquidation. Therefore, one can argue that any potential discrimination is at the level of the liquidation taxation rules rather than at the level of the exit taxation rules. Basically, under domestic law, liquidation proceeds that are treated as investment income are assimilated to dividends (the capital gains portion is not frequent to exist). Thus, it may enjoy from a full or partial tax exemption at the level of the shareholders. In case the shareholder is a resident company, a full participation exemption may indeed apply (minimum holding requirements: 10% direct shareholding or € 20.000.000 acquisition cost and 1 year of holding of the shares), in which case no withholding tax applies on the investment income portion. Based on the above, it can be argued that, inter alia, a company resident in another EU country should also benefit from a withholding tax exemption when meeting the aforementioned minimum holding requirements (which are the same for the distribution of dividends by a Portuguese subsidiary to an EU parent company).	Article 76-C of CITC

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>**11.1 Transposition of anti-abuse provisions**</u> There is a general anti-abuse provision in domestic tax law and a specific anti-abuse provision stated under the tax neutrality regime that corresponds to the transposition of Article 11(1)(a).	Article 67(10) of CITC

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
<u>**11.2 General anti-abuse provision**</u> Once there is a specific anti-abuse provision for mergers, etc, it is not likely that the tax administration would rely on the general anti-abuse provision. This latter provision is very difficult to be applicable as the tax administration has to prove the tax driven intention of the taxpayers.	Article 38 of GTL

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
<u>**11.3 The concept of 'wholly artificial arrangement'**</u> No implication so far of the '*Cadbury*' judgment.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
<u>**11.4 Specific anti-abuse provisions**</u> Not that we are aware.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
<u>**11.5 The concept of 'valid commercial reasons'**</u> The concept of 'valid commercial reasons' can be found in the specific anti-abuse provision (Article 67 (10)). It is stated there that the tax neutrality regime shall not apply whenever the tax administration concludes that the transaction's main purpose was tax avoidance, which can be verified namely when the transactions were note realized by 'valid economic reasons', such as 'restructuring' or 'rationalization' of its activities. Thus, the concept 'restructuring' and 'rationalization' are used as examples of 'valid economic reasons'. In some case, we have seen the tax administration challenging the valid commercial reasons of mergers whenever the transferring companies had	Article 67(10) of CITC Article 69(2) of CITC

negative equity. However, the challenge was used to deny the transfer of tax losses but not for trigger the taxation of gains.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
<u>11.6 Burden of proof</u> The initial burden of proof is with the taxpayer. If the tax administration does not agree, it should prove that there were no 'valid commercial reasons'.	

ROMANIA

Abbreviations

English	English
CC	Commercial Code
CITA	Corporate Income Tax Act
RTA	Reorganisation Tax Act
FC	Law 571/2003 regarding the Fiscal Code as subsequently amended
OAAR	Order 1752/2005 for approving the accounting regulations in line with the European Directives as subsequently amended

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
Overall state of implementation Starting 1 January 2007 (i.e. date of EU accession), Romania took over into the Fiscal Code (Law 571/2004 as amended) the 1990 Directive as amended by Directive 2005/19/EC. However, some paragraphs and even Articles of the Directive have not been taken over (i.e. Article 1 para. (b), Article 2 para. (j), Article 4 para. 1 let. (a), Article 4 para. 2, Article 8 para. 3, 8 and 9, Article 10, Article 10a, Article 10b, Article 10c, Article 10d of the Merger Directive). There are no clarifications or guidance issued in the applications of the Directive.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
1.1 Involved companies The Romanian legislation has literally taken over the wording of the Directive in this respect and for the moment there are no further clarifications or guidelines regarding this issue. By way of interpretation, in our view, the provisions of the Directive will apply only to the 'merging' entities.	FC Art. 27^1 para. (2)

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
1.2 Foreign Member State and third state merger In our view, the provisions of the Directive will apply only to the 'merging' entities from two different Member States. The Romanian legislation has similar provisions to the transposed Merger Directive ones, applicable to domestic reorganizations (i.e. not cross-	FC Art. 27 and Art. 27^1

border). However, although such provisions aim at tax neutrality of business reorganizations between the Romanian companies in similar conditions as those provided by the Merger Directive, differences exist between such provisions and the transposed Merger Directive (for instance there is no definition of transferred assets and liabilities, or the exchange of shares is not conditioned by exchanging the full capital of the acquiring company).	

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term 'securities' The term was translated in Romanian as 'participation titles', which are defined as shares in any Romanian legal entity, or in any other legal entity or open investment fund.	FC Art. 27^1 para. (3) FC Art. 7 point 31

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' Yes. The wording of the Directive has been literally taken over by the Romanian Fiscal Code. No clarification is provided as to whether it applies on a per shareholder basis or an overall basis.	FC Art. 27^1 para. (3)

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger Only the types of merger provided by the Directive have been taken over by the Romanian legislation.	FC Art. 27^1 para. (3)

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
<u>2.4 Qualifying exchange of shares</u> The definition of exchange of shares seems to cover only the exchange leading to the obtaining of a majority of the voting rights (or shares). Thus, the exchange of shares is defined as an operation whereby a company acquires a holding in the capital of another company such that it obtains a majority of the voting rights or of the shares in that company, in exchange for the issue to the shareholders of the latter company, in exchange for their securities, of securities representing the capital of the former company, and, if applicable, a cash payment not exceeding 10% of the nominal value, in the absence of a nominal value, of the accounting par value of the securities issued in exchange.	FC Art. 27^1 para. (3) point 6

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>2.5 Consolidation of qualifying holding</u> Such exchange of shares is not specifically included in the scope of definition. This is contrary to the Directive provisions.	N/A.

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>2.6 The term 'branch of activity'</u> The Romanian legislation has literally taken over the wording of the Directive in this respect and for the moment there are no further clarifications or guidelines regarding this issue.	FC Art. 27^1 para. (3) point 11

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
3.1 Types of entities No.	N/A.

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
3.2 Transparent entities No. There are no transparent entities in the Romanian legislation.	N/A.

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency A Romanian tax resident is defined as the legal entity who meets one of the following criteria: (a) it is set up in accordance with Romanian legislation; or (b) it has the place of effective management in Romania. The most common tiebreaker criterion under tax treaties concluded by Romania would be the place of management.	FC Art. 7 point 24

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject-to-tax clause No clarification or guidance has been issued in this respect. The Romanian legislation provides that qualifying companies should pay profits tax or a similar tax, without the possibility of an option or an exception. Clarification or guidance would be needed, for instance in clarifying whether a company in a tax loss position qualifies, or whether micro enterprises, which pay a tax on turnover, would qualify.	N/A. FC Art. 27^1 para. (3) point 12 c)

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>3.5 Shareholder requirements</u> No such limitation.	N/A.

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>4.1 The concepts of 'real values' and 'value for tax purposes'</u> 'Real value' was translated in the law as market value. 'Value for tax purpose' was not defined for the purpose of the Directive (i.e. provisions of 4 (1) (a) are not in the Romanian law). The notion is however defined for the purposes of the Romanian Fiscal Code as following: (a) for assets and liabilities - the value when entering the patrimony; (b) for interests – the acquisition or contribution value used for the computation of the gain or loss, for income or profit tax purposes; (c) for depreciable fixed assets and lands – the acquisition cost, the production price or the market value of fixed assets acquired free of charge or established as contribution on entry into the taxpayer's patrimony, used for the computation of fiscal depreciation, where applicable. The fiscal value shall also include accounting revaluations performed according to the law. In case of revaluation of depreciable fixed assets which results in a decrease of their value below the acquisition cost, production price or market value of fixed assets acquired free of charge or established as a contribution, if the case, the net book value of depreciable fixed assets shall be re-computed up to the amount established based on the acquisition cost, production price or market value of fixed assets acquired free of charge or established as a contribution, if applicable. In case of the revaluation of lands which triggers a decrease of their value below the acquisition cost or market value of those acquired free of charge or set up as a contribution, where applicable, the fiscal value is the acquisition cost or the market value of those acquired free of charge or set up as a contribution, if the case; (d) for provisions and reserves – the deductible value, for taxable profit purposes.	FC Art. 27^1 para. (4) FC Art. 7 point 33

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions No.	N/A.

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' There was no guidance issued in this respect. There are no techniques provided by the Romanian legislation on how to allocate the assets to a permanent establishment. A permanent establishment is defined by the Romanian legislation very similar to the definition of the OECD Model Convention.	FC Art. 8

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief Not the case.	N/A.

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment There is no guidance in this respect. Given the lack of clarifications and/or additional legislation in this respect, the logical interpretation would be that transfer of assets not connected to a permanent establishment should be taxable. However, there is no provision on how the taxation should take place, as for instance regarding the taxable base or the taxable moment.	N/A.

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company There is no clarification or guidance in this respect.	N/A.

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral None.	N/A.

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities Article 4(2) of the Merger Directive was not taken over in the Romanian legislation. There are no transparent entities in the Romanian legislation.	N/A.

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief No.	N/A.

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
5.1 The term 'provisions and reserves' Provisions and reserves are generally defined by accounting legislation (provisions and reserves related to financial institutions are defined by specific legislation to the respective industry). As per the definition of the accounting law, provisions are intended to cover debts the nature of which is clearly defined and which at the date of the balance sheet are either likely to be incurred, or certain to be incurred	OAAR Art. 34 OAAR Art. 206

but uncertain as to amount or as to the date on which they will arise. Reserves are defined by each category, such as legal reserves, revaluation reserves, statutory reserves and other reserves. The tax law does not define provisions or reserves; hence, whenever they are mentioned under the tax law, the definitions by the accounting law should apply (or definitions by specific industry legislation, as the case may be). The tax law provides for specific tax treatment of various provisions and reserves, such as bad debts provisions, provisions for guarantee of service rendering or manufacturing, specific provisions for oil & gas and mining industry, legal reserve, specific reserves for financial institutions, reserve from revaluation of fixed assets, etc.	 FC Art. 22

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
<u>5.2 Exclusion of 'provisions and reserves' from permanent establishments</u> No clarification or guideline in this respect. Normally the separation done in the accounting books (i.e. through analytical accounts) should be used as the basis for such an assessment.	N/A.

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
<u>5.3 Allocation method for provisions and reserves</u> Normally provisions and reserves should be allocated based on their relation to the transferred assets. However, there is no specific legislative provision in this respect.	N/A.

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
<u>5.4 Further conditions for carry-over of provisions and reserves</u> No.	N/A.

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry over of losses No carry over of tax losses from the transferring entity is allowed under the Romanian legislation in case of operations referred to in Article 1 of the Merger Directive.	FC Art. 26 para. (2)

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment As mentioned above, carry over of tax losses from the transferring entity is not allowed under the Romanian legislation.	N/A.

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets Not specific tax legislation, only accounting one (even that is not clear and subject to different possible interpretations). Tax implications of such business reorganizations would derive from the accounting treatment applied (e.g. recognition or not of goodwill, cancellation of reserves, etc.).	Order 1376/2004

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses As mentioned above, carry over of tax losses from the transferring entity is not allowed under the Romanian legislation.	N/A.

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
<u>**7.1 Amended holding threshold**</u> Yes. The provisions of the Directive have been taken over in the Romanian legislation, the meaning being identical.	FC Art. 27^1 para. (8)

Article 7(1) covers <u>gains</u> accruing on the cancellation of a holding. It does not cover <u>losses</u> that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
<u>**7.2 Treatment of losses**</u> No. Under specific accounting rules, cancellation of holding should be done against equity items. If by doing this, reserves are cancelled, which have been previously deductible from profits tax, a taxable event occurs from a profits tax perspective (i.e. profits tax should be paid on the cancelled reserves).	OAAR Art. 203 para. (2) FC Art. 22 para. (5)

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
<u>**8.1 Avoidance of economic double taxation at the level of the shareholder**</u> No. The Romanian legislation has literally taken over the wording of the Directive in this respect and for the moment there are no further clarifications or guidelines regarding this issue.	N/A.

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>**8.2 Computation of the capital gain**</u> Paragraph 8 and 9 of Article 8 of the Merger Directive has not been taken over by the Romanian legislation. The consequence would be that the tax neutrality should be kept even for the cases described by paragraphs 8 and 9 of the Merger Directive.	N/A.

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>8.3 Further conditions for tax relief</u> No.	N/A.

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>9.1 Avoidance of economic double taxation at the level of the transferring company</u> No. The Romanian legislation has literally taken over the wording of the Directive in this respect and for the moment there are no further clarifications or guidelines regarding this issue.	N/A.

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>9.2 Further conditions for tax relief</u> No.	N/A.

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>9.3 Tax deferral</u> None.	N/A.

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Loss recapture for permanent establishments in third Member States</u> Article 10 of the Merger Directive was not taken over by the Romanian legislation. The Romanian legislation allows the offset of losses of a permanent establishment of a Romanian company only against revenues of the same permanent establishment over the next 5 years.	FC Art. 26 para. (1), (3)

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> Please refer to our comments at 10.1.	N/A.

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> The Romanian legislation taxes revenues of a permanent establishment of a Romanian company, with a tax credit granted for the tax paid by the permanent establishment, up to the tax payable on the same profits in Romania.	FC Art. 31 para. (1), (2)

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
<u>10.4 Tax deferral</u> No account has been taken of the relevant ECJ case law.	N/A.

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
<u>**10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies**</u> Articles 10a and 10b of the Merger Directive have not been taken over by the Romanian legislation.	N/A.

How have the 'profits' of an <u>acquired</u> company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
<u>**10a.2 Tax base for notional tax credit**</u> N/A.	N/A.

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an <u>acquired</u> company?	Reference
<u>**10a.3 Determination of notional tax credit**</u> N/A.	N/A.

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
<u>**10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders**</u> N/A.	N/A.

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
<u>**10a.5 Comparison with a resident fiscally transparent company**</u> N/A.	N/A.

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation As mentioned at 10a.1, Article 10b of the Merger Directive has not been taken over in the Romanian legislation. We are not aware of any current intention of the lawmaker to transpose this Article in the domestic legislation. No exit taxes are provided by the Romanian legislation for the described case.	N/A.

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' The term has not been defined.	N/A.

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency A Romanian profits tax resident is defined as a company set up according to the Romanian legislation or a company having the place of management in Romania. In our view, the concept of 'head office' will be relevant for the discussed case only for companies set up according to Romanian laws, as they would have the head office in Romania.	FC Art. 7 point 24

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>10b.4 Assets and liabilities not effectively connected with a permanent establishment</u> The tax regime is not clearly provided. By interpretation of the law, transfer of such assets will be a taxable transfer, however, the mechanics of such taxation are not provided for (see 4.5).	N/A.

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the '*N*' case?	Reference
<u>10b.5 Tax deferral</u> N/A.	N/A.

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
<u>10c.1 The term 'comparable circumstances'</u> Article 10c of the Merger Directive has not been taken over by the Romanian legislation. Taxation of transfers of registered offices of SEs and/or SCEs is not clear.	N/A.

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
<u>10c.2 Loss recapture for permanent establishments</u> N/A.	N/A.

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>10d.1 Deemed liquidation</u> Article 10d has not been taken over by the Romanian legislation. Under the domestic legislation, shareholders of an SE or SCE should not be subject to tax when the company transfers its registered office. Only sale of shares in such company should trigger taxation.	FC Art. 14, Art. 30 and/or Art. 65 para. (1) c)

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>10d.2 Tax treatment of third country residents</u> The comments at 10d.1 apply.	N/A.

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> The Article was translated into the Romanian legislation. However, no further guidance is provided as regards its application.	FC Art. 27^1 para. (11) a)

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
<u>11.2 General anti-abuse provision</u> As mentioned above, Article 11(1)(a) of the Merger Directive has been transposed into the Romanian legislation. Apart from the specific anti-abuse provision of Article 11(1)(a) of the	FC Art. 11 para. (1)

Merger Directive, there is also a general anti-abuse provision in the Romanian Fiscal Code, which can be used as well, providing that the tax authorities can reconsider any transaction so that it reflects its real economic substance.	

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' No steps in this respect.	N/A.

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions No.	N/A.

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' No definitions are provided in this respect. In our view, 'valid commercial reasons' would have a similar meaning with the need for a transaction to reflect its 'real economic substance', referred to at 11.2.	N/A.

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof Normally the taxpayer.	N/A.

SLOVAKIA

Abbreviations

English	English	Slovak
ITA	Act no 595/2003 Coll. on Income Tax	Zákon o dani z príjmov
CC	Act no 513/1992 Coll. Commercial Code	Obchodný zákonník
AA	Act no 431/2002 Coll. on Accounting	Zákon o účtovníctve
ATA	Act no 511/1992 Coll. on Tax Administration	Zákon o správe daní
Civil Code	Act no 40/1964 Coll. Civil Code	Občiansky zákonník
AP	Decree 740/2002 Coll. Accounting Principles	Postupy účtovania
Merger Directive	Directive 90/434/EEC	Smernica o fúziách
PE	Permanent establishment	Stála prevádzkareň

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
<u>Overall state of implementation</u> In Slovakia, the Merger Directive is applicable as from 1 May 2004, i.e. the date when Slovakia joined the European Union. There is no specific implementation act (e.g. piece of law), which would transpose the Merger Directive into the Slovak law. The implementation is not systematic; the relevant parts of the Merger Directive are reflected in various provisions governing the accounting of entrepreneurs (AA and AP) and the ITA. Current AA and AP are valid as from 1 January 2003, current ITA is valid from 1 January 2004. However, both accounting as well as tax laws was subject to numerous amendments since they were enacted. No amendments were implemented after 31 January 2008. With respect to the Merger Directive, the ITA was amended by (a) Act No. 534/2005 implementing rules applicable in case of transfer of registered seat – carrying over of losses and tax base (Article 10c of the Merger Directive). (b) Act No. 621/2007 which clarified that the tax base of a company being dissolved without liquidation does not change in case when the legal successor is a tax payer with registered seat in EU who takes over the rights and liabilities relating to assets which are part of the permanent establishment in Slovakia. The reason for this change was the clarification of Section 17 (13) of ITA due to interpretation uncertainties. The AA were amended by Act No. 689/2004 stipulating that valuation differences in case of the merger defined in Article 2(a) of the Merger Directive first subparagraph will be accounted for in the same way as for other types of merger. This amendment should probably remove the accounting gap that existed before. Only very limited official guidelines exist and no draft legislation is in place with respect to the relevant provisions of the Slovak legislation implementing the Merger Directive.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> In the tax laws of Slovakia there is no specific implementation of the expression 'in which companies from two or more Member States are involved'. Only the general provisions apply. However, all the provisions	CC Section 69aa (1) AA Section 1 (1)

governing the mergers concern entities that 'are dissolved without liquidation' and have a legal successor. In addition, specific provisions apply to the transfer of assets. No other types of transactions are mentioned / regulated by the Slovak law, including tax laws (ITA). The definition of the company from a Member State is explicitly stipulated only in the Slovak Commercial Code. For the purposes of the Commercial Code, the company from a Member State is determined based on its seat. It is important to note that the Commercial Code does not allow any other cross-border mergers than mergers between the companies from the EEA Member States. The AA does not provide for any specific definition of the company from a Member State. Based on the AA, the companies with registered seat in Slovakia and branches of foreign companies registered in the Commercial Register that undertake or perform activities in Slovakia are subject to the Slovak accounting rules. ITA defines the taxpayers from EU Member States, as a taxpayer which is subject to the world-wide taxation in one of the other EU Member States and is a Slovak tax-non resident. The Slovak legislation does not recognize other than worldwide taxation for the determination of tax residency in other EU Member States. Thus, from a grammatical point of view, French companies may not be considered as falling within the scope of the Merger Directive. There is not a precise implementation of the expression 'companies involved'. Therefore, only general provisions apply.	a) CC Section 21 ITA Section 2 t)

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
<u>1.2 Foreign Member State and third state merger</u> The benefits of the Merger Directive are not directly conferred upon EU and third country merging companies. However, if the merging companies operate in Slovakia through a branch registered in the Slovak Commercial register ('*organizačná zložka*'), these will be obliged to keep books of accounts according to AP and AA. Also, if the activities/assets of the foreign taxpayers constitute a permanent establishment for income tax purposes in Slovakia, the tax regime applicable for Slovak taxpayers will generally be applicable also for the PE. Generally, the companies from EU Member States operating through a branch registered in the Slovak Commercial register should benefit from the same provisions of Merger Directive transposed in the Slovak law as Slovak taxpayers. Differences may occur, in particular if a PE is created	AA Section 1 (2) ITA Section 17 (7) ITA Section 17(7)

but not registered in the Commercial Register. The tax base is in such a case calculated on the basis of attributable costs/expenses; alternative methods are possible.	

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term 'securities' The term 'securities' as used in the Merger Directive has not been specifically defined in the Slovak legislation. The meaning of this term shall, based on the Commercial Code, be interpreted as capital participation of the shareholder on company's register capital. It is questionable, if also personal participation of general partners in unlimited and limited partnerships may be subject to exchange of securities as the general partner is personally connected to the partnership. Note that limited partnership ('*komanditná spoločnost*') is listed in the Annex to the Merger Directive. However, principally, it should be possible to execute an exchange of shares also in case of general partners in unlimited and limited partnerships. The legal uncertainty stems from the nature of the partnership, i.e. personal participation of a partner in a partnership and from lack of practical experience.	CC Section 114 (1) CC 155 (1)

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' The Slovak Commercial Code stipulates the 10% cap for cash payment for reorganization of companies. The aggregate compensation in cash shall not exceed 10% of the nominal value of all shares on an overall basis to be issued by the successor company to the shareholders of the companies to be dissolved.	CC Section 218a 1) b)

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger No other types of merger are recognized in the Slovak legislation. Moreover, the Slovak commercial law recognizes only specific types of mergers. It does not recognize a partial division as stipulated by the	CC Section 69a, 69aa

Merger Directive. It is doubtful if a Commercial Register will recognize a corporate transaction not directly envisaged by the CC. In practice, only business combinations that are specifically listed in the CC are being implemented, e.g. mergers except partial division.	

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares There is no specific implementation of the term 'exchange of shares' in the Slovak tax legislation. Thus only general principles apply, i.e. the tax treatment follows the accounting treatment. These apply irrespective of the fact whether a majority is acquired or consolidated. According to the Slovak accounting standards, such an operation at the moment of the exchange should not affect the accounting result (P&L) of the involved companies The exchange of shares would be considered as an equity operation and, consequently, would not have impact on their tax bases.	

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
2.5 Consolidation of qualifying holding As already mentioned, there are no specific provisions regarding the exchange of shares. Please refer to 2.4.	

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
2.6 The term 'branch of activity' The Slovak definition of 'enterprise' ('podnik' or 'časť podniku') in the Commercial Code meets the conditions of the term 'branch of activity' as defined in the Directive. The term 'enterprise' is defined as 'the whole of tangible, intangible and	CC Section 5

personnel assets, which are used in business. The enterprise comprises assets, rights and other valuables, which belong to the entrepreneur and are or, due to their characteristics, are aimed to be used for the operation of the enterprise.' However, from the tax perspective, the same treatment applies for all contributions of assets into the equity of another (receiving) company, i.e. individual assets as well as enterprises/branches of activity.	

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> The Slovak legislation does not have any specific implementation of the Merger Directive. Hence the general treatment of mergers is applicable to all merging companies (EU and third countries). Therefore, the Slovak legislation does not restrict the application of the Merger Directive only to those types of entities listed in the Annex. The provisions of the Commercial Code implementing the Merger Directive refer to 'commercial companies'. Among these are not only the companies listed in the Annex (joint-stock company, limited liability company, limited partnership), but also to general partnerships. However, as the legislation does not specifically treat the mergers of partnerships (both limited and general) therefore it is not clear whether the benefits of Merger Directive will apply also to these. The provisions of the CC on mergers are in general applicable also to cooperative societies.	CC Section 56 (1), Section 69aa, CC Section 255, 260

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>3.2 Transparent entities</u> The limited partnership is listed in the Annex of the Merger Directive ('*komanditná spoločnosť*'). According to the Income Tax Act, limited partnership is considered as partially transparent. The tax base of the company is allocated to the two categories of partners – general partners and limited partners. The tax base is allocated on the same basis as the profit of the limited partnership before taxation. The tax attributable to limited partners is levied at the level of the partnerships. General partner tax in their hands the portion of the tax base attributable to them. Based on current law, the foreign fiscally transparent entities are taxed as corporations (as PEs of foreign entities). However, the tax authorities recently expressed opinion that the profit	ITA Section 14(4) ITA Section 14(5)

generated by foreign fiscally transparent entities should be taxed in the hands of their partners. No specific guidance in this respect is available; an amendment to the ITA is planned in this respect. No details are available as of today (4 April 2008). Please note that no official guidance has been issued regarding this new approach and it is only a single case. Moreover, the Slovak legislation, at its current state, does not provide any legal background for this new approach. The tax loss shall be allocated on the same basis as the tax base.	

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
<u>**3.3 Qualification of tax residency**</u> According to the Slovak ITA, a company is considered as Slovak tax resident if its registered seat or its place of management is located in the Slovak Republic. The registered seat is the main and primary criterion. The most common tax residence criterion in the double tax treaties concluded by the Slovak Republic is the seat and place of effective management.	ITA Section 2 d) 2.

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>**3.4 Subject-to-tax clause**</u> There is no specific implementation of the subject-to-tax clause. The Corporate Income Tax (*'daň z príjmov právnických osôb'*) stipulated in the Article 3(c) of the Merger Directive is a general income tax defined by ITA covering all corporate bodies having any income taxable in the Slovak Republic. The Slovak legislation does not recognize other than world-wide tax basis principle for the determination of tax residency (for details see 1.1).	

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>**3.5 Shareholder requirements**</u> The Slovak legislation does not specify any requirements regarding persons owning or controlling companies that would limit the benefits of the Merger Directive.	

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
4.1 The concepts of 'real values' and 'value for tax purposes' The concept of real value is recognized by the AA and AP. As the result of a merger, the receiving company accounts for the real value, which is generally the market value, or valuation by an expert/appraiser if the market value is not available or cannot be determined. In principle, the market value is the value of assets on the market where such assets or comparable assets are traded. The term 'value for tax purposes' is neither clearly defined in the ITA nor in other Slovak law. It is calculated differently for different types of assets/liabilities. The ITA stipulates specifically the 'tax residual value' in case of tangible and intangible assets valued more than SKK 30,000 (ca. EUR 920) and economic life longer than one year. The tax residual value generally matches with the Merger Directive's concept of 'value for tax purposes'. The tax residual value is the difference between the price determined for depreciation purposes (e.g. acquisition cost, production cost, replacement cost) and the accumulated depreciation of the asset treated as tax expense. For other types of assets/liabilities the value for tax purposes is their accounting value and not necessarily matches the 'value for tax purposes'. This leads to possible step up/step down in tax value of other assets (stock, receivables, and small value assets). The accounting value is the difference between the input price (acquisition cost, production cost, nominal value, replacement cost, and real value) and the accumulated depreciation of an asset. The step up/down in tax value should have no effect on the tax position of the transferring company. Likewise, no immediate tax effect should occur on the side of the acquiring company; however, it effects its tax position at a later stage, e.g. depreciation. This deferred tax effect might not be in compliance with the Merger Directive.	AA Section 27(2) AA Section 27(1)d) ITA Section 25 (1) f ITA Article 26

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions No specific guidance has been issued in respect of divisions and partial divisions.	

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' No specific administrative guidance was issued. If the PE accounts in the Slovak Accounting Standards (i.e. pursuant to AA and AP), effectively connected means being recognized in the books of the PE. There is no definition of 'effectively connected assets' in place; however, in principle, it should cover assets which are being used by the PE for their local activities. The concept of a PE is a purely tax concept, i.e. not directly recognized by the CC, AA or AP. The Slovak PE definition generally follows the OECD Model Tax Convention's definition of a PE. In line with the ITA, a PE means a fixed place or facility through which tax non-residents carry out their activities, fully or in part, in the Slovak Republic. In particular, a fixed place or a facility is defined as an administration point, branch, office, workshop, sales-point, technical facility or a point of research or of extraction of natural resources. The fixed place or the facility is considered to be permanent if the activities are carried out continuously or repeatedly. In the case of one-off activities, the place or facility is considered to be permanent if the duration of the activities exceeds six months, either continuously or divided into two or more periods in the course of twelve consecutive calendar months. A building site, construction or assembly works-site is considered to be a permanent establishment only if the duration of the activities exceeds a period of six months. The term 'permanent establishment' also includes a person acting on behalf of an entity having its registered office abroad or being resident abroad, and who negotiates or enters into agreements on behalf of such an entity on a continuous or repeated basis, under a power of attorney.	ITA Section 16 (2)

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief No.	

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment Generally, the assets/liabilities not connected with the PE will not be part	

of the branch of activity taking part in the merger. These assets / liabilities are not excluded from scope of any provision implementing the Merger Directive. However, these need to be attributed to any other enterprise which is subject to the merger. No guidance setting criteria for allocation available in the local legislation. In case an asset/liability ceases to be effectively connected with a permanent establishment (irrespective if undergoing a merger), the tax authorities may try to seek the 'deemed taxable' income. Under the ITA the tax base of a PE cannot be lower as if the same activity would be performed by a separate entity (so called separate entity approach). Therefore, the tax authorities may seek to adjust the tax base of a PE by a 'deemed taxable' income, which basically should be similar to an income a separate entity would accrue due to a sale of the particular asset.	ITA Section 17(7)

Is a merger (under the condition of Section 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company Yes. There should be no taxation upon the merger.	AP Section 26, ITA Section 17 (18)

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral There is no exit taxation in Slovakia.	

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities The concept of foreign transparent entity is not expressly defined in the Slovak ITA. We anticipate the clarification of the concept in future. The Slovak legislation provides rules only for the taxation of domestic (Slovak) transparent entities (for details please refer to 3.2).	

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
<u>4.9 Further conditions for tax relief</u> No.	

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>5.1 The term 'provisions and reserves'</u> In Slovak law, the term 'provision' provides for a temporary impairment of the value of an asset. According to AP, provisions shall be created when it is reasonable to assume that the value of assets will decrease in comparison with the value showed in the accounting books. AP defines 'reserves' as liability of the accounting unit from the past events, it is presumable that in the future will decrease the economic gains of the accounting unit if the amount of the liability is not known. It shall be valued by the assessment sufficient for the fulfillment of the liability at the day of closing of the accounting books (e.g. end of the accounting period) considering potential risks. In case of a merger, the assets/liabilities are booked at current market value (an accounting rule) in the receiving entity. As a result, provisions should not be booked in the open books of the receiving companies. This causes uncertainty as to the tax treatment of provisions. Reserves, as other liabilities, should be booked in their real value by the receiving company. On the side of the transferring entity, with respect to mergers and divisions, provisions will be included in the tax base if not taken over by the legal successor, either with a seat in Slovakia or in EU Member States. In case the legal successor has a PE in Slovakia, provisions will not be taxed if they relate to assets attributable to that Slovak PE of the taxpayer with registered seat in the European Union. No specific tax provisions regarding the carry over of provisions and reserves (i.e. their tax treatment by the receiving company) were implemented. As a result, the tax exemption of provisions is generally not maintained. The exemption of transferred reserves is not specified in the Slovak ITA.	AP Section 18 (1), AP Section. 19 (1)

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments With respect to mergers and divisions, provisions and reserves and other items of accruals (deferred revenues, accrued revenues, deferred expenses, accrued expenses pursuant to Slovak AP) will be included in the tax base and taxed/deducted if these accounts of accruals are not taken over by the legal successor, either with a seat in Slovak Republic or in EU Member States; in case the legal successor has a permanent establishment in Slovakia, the above items of accruals will not be taxed/deducted if they relate to assets/liabilities attributable to that Slovak permanent establishment of taxpayer with registered seat in the European Union. No specific provisions to distinguish between provisions and reserves derived from a foreign permanent establishment or other permanent establishments or business divisions or the company as whole was implemented.	ITA Section 17 (13)

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves Allocation of provisions and reserves for tax purposes follows the accounting treatment of merger/division/transfer of assets. No specific provisions regarding the allocation method were implemented. No practical experience so we cannot comment on best practice in this respect.	AA Section 27

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry over of provisions and reserves The accounting treatment of the carry over of provisions by the receiving company is not clear. As indicated in 5.1, the reserves should be transferred in their real value. On the side of the transferring entity, with respect to mergers and divisions, provisions will be included in the tax base if not taken over by the legal successor, either with a seat in Slovakia or in EU Member States. In case the legal successor has a PE in Slovakia, provisions will not be taxed if they relate to assets attributable to that Slovak PE of the taxpayer with	ITA Section 17 (13)

registered seat in the European Union. No specific tax provisions regarding the carry over of provisions and reserves (i.e. their tax treatment by the receiving company) were implemented. As a result, the tax exemption of provisions is generally not maintained. The exemption of transferred reserves is not specified in the Slovak ITA.	

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry over of losses The term 'loss' is defined in the Income Tax Act as the amount, by which the tax expenses exceed the taxable income, taking into account the substantial and chronological correlation between the taxable income and the tax expenses in the relevant tax period. The losses can be carried over in five consecutive periods following the period in which it was incurred.	ITA Section 2 k) ITA Section 30

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment Allocation of losses of the transferring company to the receiving company's permanent establishment situated in the same Member State as the transferring company is allowed only if the permanent establishment is created as a result of the merger. If there is more than one legal successor the tax loss carried forward is divided according to the portion of equity assumed from the dissolved entity (please note that Slovak law does not define partial division).	ITA Section 17 (28) ITA Section 17 (27)

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets If there is more than one legal successor the tax loss carried forward is divided according to the portion of equity assumed from the dissolved entity (please note that Slovak law does not define partial division). There are no specific regulations for the transfer of assets. Hence, the tax losses carried forward are not transferred with the branches of activity if the entity is not dissolved.	ITA Section 30 (2)

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses The receiving company (legal successor) can carry forward the loss incurred by the transferring company if: (a) both companies are subjects to the Corporate Income Tax, and (b) purpose of the merger is not only minimization of tax base or tax avoidance. The above conditions apply to domestic as well as cross border situations.	ITA Sec. 30 (2)

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Amended holding threshold The Slovak ITA does not contain any such threshold restricting the application of the Merger Directive. The gain or loss from the cancellation of a holding (i.e. receiving company holds a shareholding in the transferring company) should crystallize into a equity fund (valuation difference) and should not impact the tax base. Please note that the tax treatment is not 100% clear. Due to lack of specific rules there is a risk that the Slovak tax authorities would insist on P&L accounting which would lead to the recognition of taxable revenue.	AP Section 26

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses Please see 7.1.	

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
<u>**8.1 Avoidance of economic double taxation at the level of the shareholder**</u> The concept of 'exchange of shares' is not expressly stipulated by the Slovak law. Therefore, the exchange of shares should rather be considered as a contribution of the shares in the acquired company into the registered share of the acquiring company. The shares should be booked at the real, i.e. market value. According to the Slovak accounting standards, such an operation at the moment of the exchange should not affect the accounting result (P&L) of the involved companies The exchange of shares would be considered as an equity operation and, consequently, would not have impact on their tax bases.	

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>**8.2 Computation of the capital gain**</u> No guidance was issued by the Slovak tax authorities. Based on the Slovak legislation, income arising from the exchange of shares in case of dissolution of the taxpayer without liquidation is exempt from taxation. However, in case of exchange of shares and partial division no dissolution of the taxpayer without liquidation occurs. Therefore, the respective cash payments should be subject to taxation.	

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>**8.3 Further conditions for tax relief**</u> The following conditions apply: (a) The aim or the substance of the transaction must not circumvent or contradict the law.	Civil Code Section 39 ATA Section (2)6

(b) When applying Slovak tax law, the substance of a transaction is taken into account for the correct assessment of the tax. Thus, the tax authorities should consider the substance of a transaction if it differs from its legal form.	

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>9.1 Avoidance of economic double taxation at the level of the transferring company</u> There will be no taxation of the inherent gain at the level of the transferring company, but only at the time of disposition of newly acquired shares. The capital gain is not taxable in case it relates to assets that are depreciated pursuant to the ITA (i.e. assets of useful life longer than 1 year and of value more than SKK 30,000). However, these assets do not realize a tax step-up in value on the merger, i.e. their value for tax purposes in the receiving entity is derived from the tax residual value (value for tax purposes) in the transferring entity. The limitation of relief only to depreciable assets is contrary to the Merger Directive.	AP Section 59(8) ITA Section 17(19)

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>9.2 Further conditions for tax relief</u> N/A, no relief is possible; capital gains are taxable except for assets depreciable according to the ITA (see 9.1).	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>9.3 Tax deferral</u> The case 'N' was not reflected by Slovak legislation or manifest change in interpretation of the Tax Authority.	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Loss recapture for permanent establishments in third Member States</u> Utilization of foreign PE losses against Slovak profits is seriously restricted. Under the Slovak legislation, the tax base of a tax payer subject to world wide taxation in Slovakia includes also the tax base of a foreign PE with the exception when the tax loss of a foreign PE may be utilized in the state where the income of the PE is sourced. However, it is not clear whether the option to utilize the losses relates only to the respective tax year or also to future tax periods.	ITA Section 17 (14)

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> <u>10.2.1 General treatment</u> There is no specific implementation in this respect. If the PE is registered in the Commercial Register, general AP and AA rules apply and the tax base is calculated based on the accounting result further adjusted by similar items as for the Slovak tax residents. If the PE is not registered in the Commercial Register, the tax base should be determined on a specific basis (difference between profits and costs or any other basis respecting transfer pricing provisions). No specific implementation of the Article 10(1) of the Merger Directive in this respect. <u>10.2.2 Losses</u> Based on ITA, the losses of a company dissolved without liquidation can be utilized by its legal successors. Based on this general rule it should be possible for the tax loss generated by a PE in a state in which the receiving entity is established to be further utilized by this receiving entity. This principle cannot be used, if the transferring company is not dissolved (transfer of assets, partial division). The Slovak legislation does not provide for any mechanism governing the conversion of a PE into a subsidiary. Therefore, the answer of tax deferral in this case is not clear.	ITA Section 17 (1) b) ITA Section 30 (2)

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
10.3 Concept of worldwide taxation/tax credit system There should be no taxation of unrealized capital gains.	

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
10.4 Tax deferral The case '*N*' was not reflected by Slovak legislation nor a change in interpretation of the Tax Authority has been noticed. There is no exit taxation in Slovakia. The use of the separate entity approach (see 4.5) of taxation of a PE is not clear. If assets are being moved outside of Slovakia as part of the reorganization process, it might be possible to conclude, based on the general rules of taxation and the separate entity approach, that a taxable disposal of asset takes place. However, no guidance covering such a situation is in place.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies There is neither implementation nor administrative guidance in this respect. Based on current law, the foreign fiscally transparent entities are taxed as corporations (as PEs of foreign entities). However, the tax authorities recently expressed opinion that the profit generated by foreign fiscally transparent entities should be taxed in the hands of their partners. No specific guidance in this respect is available; an amendment to the ITA is planned in this respect. No details are available as of today (4 April 2008). Please note that no official guidance has been issued regarding this new approach and it is only a single case. Moreover, the Slovak legislation, at its current state, does not provide any legal background for this new approach.	

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit See 10a.1.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit There is no system of notional tax credits.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders Please See 10a.1. The legislation currently does not recognize non-resident fiscally transparent entities. Change in administrative practice is unclear in this respect and proposals are planned to the ITA. No details yet.	

What does that 'same treatment for tax purposes' (Article 10a (4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company Please see 10a.4.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation No exit taxation should be realized, Slovak tax legislation does not stipulate any specific exit tax provisions.	

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term 'head office' The Slovak version of Regulation 2157/2001 uses the term 'head office'('*ústredie*'), which is defined as the place from which the activity of the European Society is managed. The term is not defined in any relevant law (i.e. AA, AP, CC or ITA). It is questionable, whether it differs from the term 'place of effective management' ('*miesto skutočného vedenia*') used by the Slovak ITA and majority of Double Tax Treaties concluded by Slovakia. There is no specific implementation of Article 10b of the Merger Directive.	Act 562/2004 Coll. Section 2 a) ITA Section 2 d) (2)

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency The term 'head office' is not clearly defined in the law. Different terms are used (see 10b.2). No relevant administrative practice is available.	

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>**10b.4 Assets and liabilities not effectively connected with a permanent establishment**</u> No specific guidance in this respect. Slovak legislation specifies only some type of assets and liabilities which will influence the tax base in case of not being connected with a PE. However, in general, a separate entity approach applies (see 4.5 above). The tax base may be adjusted with assets not connected to permanent establishment. No specific administrative guidance or practice of tax authorities known in this respect. The use of the separate entity approach (see 4.5) of taxation of a PE is not clear. If assets are being moved outside of Slovakia as part of the reorganization process, it might be possible to conclude, based on the general rules of taxation and the separate entity approach, that a taxable disposal of asset takes place. However, no guidance covering such a situation is in place.	ITA Section 17(7) ITA Section 17 (13)

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the '*N*' case?	Reference
<u>**10b.5 Tax deferral**</u> The 'N' case was not reflected in Slovak legislation. No exit taxation provisions.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
<u>**10c.1 The term 'comparable circumstances'**</u> In case that by transfer of registered seat or head office of a SE or SCE from Slovak Republic to other Member State arises that company's PE, the tax loss generated before the transfer can be utilized by that PE.	ITA Section 17 (28)

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
<u>10c.2 Loss recapture for permanent establishments</u> The losses generated by a PEs of Slovak companies may be utilized by that companies if that tax loss cannot be utilized in the respective Member State by the PE. The interpretation of this provision remains unclear.	ITA Section 17 (14)

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>10d.1 Deemed liquidation</u> From tax respective, no deemed liquidation is applicable in Slovakia. Therefore, no exit taxation will be realized in Slovakia.	

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>10d.2 Tax treatment of third country residents</u> As Slovak tax legislation does not provide any provisions as regards the exit taxation, Slovakia will not tax the respective capital gain on shares as it will not be realized.	

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> No, the Article 11(1)(a) of the Merger Directive has not been specifically transposed into Slovak national law.	

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
11.2 General anti-abuse provision Slovak Civil Code provides general law anti-abuse principle stipulating that the transaction, which in substance contradict or circumvent the law or is against the 'good moral (practice)' is not valid. There is not an exact definition of 'good practice', but it can be characterized as generally accepted conduct in legal relations in the society, e.g. honesty, no n-misuse of rights, respecting equality of parties). However, the courts are rather reluctant to use this reason to invalidate a transaction and try to seek other grounds to find a transaction invalid. The tax laws contain a so called 'substance over form' provision, based on which for determination of the tax treatment of a transaction its substance has prevalence over its legal form. This provision means that a transaction is assessed based on its economic merit (substance) rather than its legal form. However, its application in practice is not very clear due to non-unified interpretation and non-existing case law. We have not seen this principle to be applied in practice.	Civil Code Section 39 ATA Section 2 (6)

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' The 'Cadbury' case has not been yet reflected by the Slovak tax law. Similarly, the Slovak tax authorities have not tried to apply the principles established by the 'Cadbury' in practice.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions The Slovak tax authorities have not sought to rely on Article 11(1)a of the Merger Directive (see also 11(1)a and 11(2)). As from 1 January 2008, the carry over of losses in case of merger may be utilized by the receiving entity, only if the aim of the merger is not minimization of tax base or tax avoidance.	ITA Section 17 (13) ITA Section 30 (2)

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' Technically, the substance over form principle (see 11.2) applies. Based on this, the transaction is treated according to its real purpose and aim. There is very little practical application to date. In addition, the Section 30 (2) ITA may be interpreted that 'valid commercial reasons' means having the aim of the merger other than minimization or avoidance of tax liability. No specific guidelines were issued in this respect.	ITA Section 30 (2)

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof The initial burden of proof has the taxpayer, as he is generally supposed to be able to document all the items reported in the tax return. There is no special provision with respect to the Merger Directive.	

SLOVENIA

Abbreviations

English	Slovene	English	Slovene
CITA	ZDDPO-2	Corporate Income Tax Act	Zakon o davku od dohodkov pravnih oseb
OG	UL	Official Gazette	Uradni List
CA	ZGD-1	Companies Act	Zakon o gospodarskih družbah
OECD	OGSR	Organisation for Economic Co-operation and Development	Organizacija za gospodarsko sodelovanje in razvoj
Para.	Odst.	Paragraph	Odstavek
No.	Št.	Number	Številka
EU	EU	European Union	Evropska unija
FIMA	ZTFI	Financial Instruments Market Act	Zakon o trgu finančnih inštrumentov
TPA	ZDavP-2	Tax Procedure Act	Zakon o davčnem postopku

Survey of the Implementation of Council Directive 90/434/EEC

(The Merger Directive, as amended)

SLOVENIA

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
<u>Overall state of implementation</u> The Merger Directive was implemented by the Corporate Income Tax Act which came into force on 1 January 2005 (Official Gazette of the Republic of Slovenia No 40/04 from 20 April 2004). At that time the law implemented the EC Directive 90/434 from 23 July 1990 and which was published in the OJ L 225 (20 August 1990). The national provisions implementing the Merger Directive were applicable to operations occurring subsequent to 1 May 2004 (the date of Slovenia's entry into the EU). The subsequent changes of the Merger Directive – the last one being the 2005/19/EC (OJ L 58, 4 March 2005) – were implemented with the adoption of the new Corporate Income Tax Act (Official Gazette of the Republic of Slovenia, No. 111/07 and 90/07), which came into effect as of January 1, 2007. The substantive issues regulated by the Merger Directive, are comprised in Chapter 7 (Taxation Applicable to Mergers, Divisions and Exchanges of Shares) of the Corporate Income Tax Act. Additional guidance is issued by the Ministry of Finance with adoption of the Regulation on the Execution of the Corporate Income Tax Act (Official Gazette of the Republic of Slovenia, No. 60/2007), dated July 7, 2007. The Regulation provides a list of the EU companies (legal forms) which are entitled to the benefits of the Merger Directive and a list of the corporate taxes in EU Member States to which it relates.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> The expression 'in which companies from two or more Member States are involved' has been interpreted and implemented separately for mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States respectively, as follows: (a) In the case of a transfer of assets, 'companies involved' refers to companies, which are residents of Slovenia and / or a resident of another EU Member State, provided that; • The transferor and transferee of an operation (assets) are residents of Slovenia, and the subject of the transfer must be	Article 41(I) 1, 2, and 3 of the Corporate Income Tax Act.

transferred within Slovenia or to another EU Member State. • The operation transferred between a transferor of an EU Member State (excluding Slovenia) and a transferee, which is a resident of Slovenia, must be actually transferred to Slovenia and not to another state in which the Slovene resident has a permanent establishment. • The operation transferred between a transferee of an EU Member State (excluding Slovenia) and a transferor, which is a resident of Slovenia or another EU Member State, must be actually transferred to a permanent establishment of the transferee in Slovenia.	Article 46 (I) 1, 2, and 3 of the Corporate Income Tax Act.
(b) In the case of an exchange of shares, 'companies involved' refers to companies, which are a resident of Slovenia (and/or) a resident of another EU Member State, provided that: • the acquiring and acquired entities are residents of Slovenia and/or residents of another EU Member State; and • the shareholder is a resident of Slovenia, or is not a resident of Slovenia but is the holder of securities of the acquired and acquiring entity via a permanent establishment in Slovenia.	Article 50(I) 1, 2, and 3 of the Corporate Income Tax Act.
(c) In the case of mergers and divisions, 'companies involved' refers to companies, which are residents of Slovenia (and/or) a resident of another EU Member State provided that: • both companies are considered residents of Slovenia, regardless of whether the operations of the transferring company are in Slovenia or in another EU Member State or; • the acquired company is not a resident of Slovenia, yet is an EU resident, and the acquiring company is a resident of Slovenia, under the condition that the subject of transfer (assets, operations, reservations etc) is not transferred to a permanent establishment outside of Slovenia after the merger or division or; • the acquiring company is not a resident of Slovenia, yet a resident of an EU Member State and the acquired company is a resident of Slovenia or another EU Member State, under the condition that the subject of transfer (assets, operations, reservations etc) is transferred to the acquiring entity's permanent establishment in Slovenia. Based on the Corporate Income Tax Act, the term 'companies involved' should be interpreted as the companies which are actually directly taking part in the transaction (e.g. the two companies which are merging/exchanging shares). The term 'companies involved' has not been interpreted as encompassing parent companies.	

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
1.2 Foreign Member State and third state merger N/A.	

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term 'securities' The tax law does not define the term 'securities'. Nor has it been defined in other Tax Authority guidance. For general purposes, the term 'securities' is defined in the Financial Instruments Market Act. It defines securities as all instruments that can be traded on the financial market including the following: (a) Shares of stock companies, other securities that are substantively equated with such shares, that represent a share in the capital of a company or membership rights, and certificates of deposit concerning these shares; (b) bonds and other securities, which define the duty of the issuer and certificates of deposit concerning these securities; (c) every other security, which includes: (d) an unilateral right of the holder to obtain or sell a security or (e) the right of the holder to request a monetary payment, which is defined in accordance with the value of securities, the relevant foreign exchange rate, interest rate or yield, or given the value of the index.	Article 7 (3) of the Financial Instrumemts Market Act

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' 2.2.1 Concept The Corporate Income Tax Act specifically provides for the possibility of allowing a 10% cash payment for reorganization at book value with regards to the exchange of shares. Specifically, regulations state that the receiving company may issue a cash payment to the shareholders of the transferred company in an amount, that does not exceed 10% of the nominal value of the transferred shares. If the nominal value has not been determined, the cash payment must not exceed 10% of the amount of the smallest total shares issued or transferred. Moreover, a monetary payment may be made to minority shareholders, however, such payment should not exceed 5% of the nominal value of the transferred shares. If the nominal value has not been determined, the cash payment must not exceed 5% of the amount of the smallest total shares issued or transferred.	Article 44/II of the Corporate Income Tax Act

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger The Corporate Income Tax Act of Slovenia refers to the Companies Act when defining the term merger. The definition found in the Companies Act does not provide for any additional or other types of mergers, which are not covered by the Merger Directive.	Article 48/I of the Corporate Income Act; Articles 580/ II and III of the Companies Act.

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares The condition where successive acquirements of shares must be carried over a period of six months in order for such transactions to be treated for tax purposes as one transaction, applies to situations where an acquiring	Article 44/I of the Corporate Income Tax Act

company obtains a majority in the acquired company through more than one transaction (exchanges of shares).	

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>2.5 Consolidation of qualifying holding</u> Should the acquiring company already hold a majority of shares in the acquired company, any further exchange of shares should also be considered as an exchange of shares which qualifies for the tax relief granted in accordance with the Merger Directive. Such relief is not subject to any further conditions, except that it must not be solely tax motivated.	Article 44/I of the Corporate Income Tax Act

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>2.6 The term 'branch of activity'</u> Similarly to the definition encompassed in the Merger Directive, the Slovene Corporate Income Act defines a 'branch of activity' as a certain part of an entity, including all assets and liabilities, which is, from a business organizational perspective, competent of constituting an independent business and a subject capable of conducting business with its own means. No administrative guidance has been issued in this regard.	Article 39 and 48/IV of the Corporate Income Tax Act

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> The national legislation does not apply the Merger Directive to more types of entities than those listed in the Annex.	Article 10 of the Regulation on the execution of the Corporate Income Tax Act

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
3.2 Transparent entities Slovene legislation does not provide for transparent entities. Generally, in order to apply the relief, one should be able to prove that an entity, established in a legal form included in the annex is also subject to a tax included in the annex.	

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency	
3.3.1 Tax residency under domestic law A corporation is a tax resident in Slovenia if it is seated (registered seat) in Slovenia or if its effective place of management is in Slovenia.	Article 5/I (1,2) of the Corporate Income Tax Act
3.3.2. Tax residency under Double Taxation Treaties In various double tax conventions concluded between Slovenia and other countries, the tiebreaker criterion to determine the tax residency of corporations is the place of effective management.	Article 4 (3) of various Slovene double tax conventions
3.3.3. Statutory seat under domestic company law The statutory seat of an entity, as defined by the Companies Act, is the location entered as such into the court registry. The seat of a company may also be determined as the place in which the entity carries out its activities, or as the predominant place of management.	Articles 29 and 30 of the Companies Act

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject-to-tax clause The subject-to-tax clause has been implemented in Slovene legislation as follows: the relevant Articles implementing the Merger Directives shall apply to entities that are EU residents, and not residents of Slovenia, provided that they are a taxable entity subject to one of the taxes, to which the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of	Article 41 (II), 3 of the Corporate Income Tax Act.

different EU Member States or to the transfer of the statutory seat of an European company or cooperative society between EU Member States applies. The tax, to which the entities involved in the aforementioned transactions are subject to, under this provision, was additionally determined by the Regulation for the Execution of the Corporate Income Tax Act. An entity which is tax exempt or has the right to opt is not considered a taxable entity under the subject-to-tax clause. Slovenian residents for the purposes of the Corporate Income Tax Act are legal entities subject to corporate income tax and should be per se eligible for the relief.	

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>3.5 Shareholder requirements</u> The citizenship or residency of shareholders of a company should not be relevant for the application of the benefits arising from the Merger Directive.	Articles 38 to 54 of the Corporate Income Tax Act

Article 4 – Carry over of balance sheet value

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>4.1 The concepts of 'real values' and 'value for tax purposes'</u> Slovene regulations define 'real values' (directly translated as the 'fair value') as the value at which a transferred value good/stock may be sold or otherwise exchanged for an equity instrument or other asset, or at which it may settle an obligation, between two parties that are well informed, willing, mutually independent and equal. 'Value for tax purposes' is an amount attributable to a certain asset or liability when calculating the tax or based on which income, expenditures, profits of losses are calculated when determining the tax liability.	Article 38/IV of the Corporate Income Tax Act Article 38/V of the Corporate Income Tax Act

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
<u>4.2 Specific guidance for divisions/partial divisions</u> <u>4.2.1. Concept</u> For the purpose of the implementation of the Merger Directive, divisions follow the same rules of common taxation applicable to mergers.	Article 48 of the Corporate Income Tax Act

The Merger Directive requires that in the case of a division, all assets and liabilities of a company are transferred to two or more existing or new companies. The Corporate Income Tax Act additionally provides however, that the relevant provisions, implementing the Merger Directive, are applicable only to such partial divisions, whereby at least one branch of activity remains in the transferring company. A 'branch of activity' is defined as the assets of a company which, from an organizational point of view, are competent of constituting an independent business and a subject capable of conducting business with its own means. The valuation of assets in the case of divisions and partial divisions follows the same rules applicable to mergers, namely, the acquiring entity is obliged to assess the value of the acquired assets and liabilities transferred from the acquired entity, by taking into consideration the tax values. Moreover, it must depreciate their value and evaluate possible gains or losses arising from the merger or division on the day of the relevant transaction. The purpose of this provision is that the tax basis is carried forward from the previous company. There is no specific guidance outside the law on the interpretation of these provisions.	Article 48/III, IV of the Corporate Income Tax Act

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' 4.3.1. Effectively connected The Slovene term is *'pripadajo'* and can be translated as 'belonging to'. The term is not further defined and there is no practice or case law in this respect. 4.3.2. Permanent establishment Pursuant to Slovene legislation, the term 'Permanent establishment' has been implemented as 'stalna poslovna enota nerezidenta' which is the fixed place of business in Slovenia, through which activities of an organization are wholly or partially carried out. A permanent establishment includes a place of management, a branch, an office, a factory, a workshop, and a mine, oil or gas well, quarry or other place of extraction of natural resources residing in a foreign jurisdiction. It also includes a building site, a building project or assembly project, or the erection or supervision thereof, if the business activity exceeds a 12 month period. The concept of permanent establishment extends to dependent agents. The interpretation and practical application of permanent establishments should generally closely follow the OECD Model Convention Concept.	Article 50/ I (3) of the Corporate Income Tax Act Article 6/I, II of the Corporate Income Tax Act Article 6/III of the Corporate Income Tax Act

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief 4.4.1 Concept No, there is no recapture of depreciation on the assets transferred. The Corporate Income Tax Act completely incorporates the provisions of Article 4(2) of the Merger Directive. where it provides that the receiving entity must value the acquired assets and liabilities and compute any gains or losses and any new depreciation in respect of the assets and liabilities transferred by taking into account their tax values and according to the rules that would have applied to the transferring company if the merger or division had not taken place.	Article 49/II of the Corporate Income Tax Act

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment The Corporate Income Tax Act incorporated the term from the directive 'effectively connected with a permanent establishment' as 'belonging to a permanent establishment'. The latter however, is not further defined or elaborated and no official guidance has been issued yet. Moreover, 'assets and liabilities' were implemented into the national legislation as 'assets, liabilities, provisions, reserves and losses'. The tax treatment of these assets and liabilities that are not effectively connected with permanent establishment is not clear from law and practice. The current tax regime provides for the system where the transaction qualifies for the EC Merger Directive benefits if the assets and liabilities, provisions, reserves and losses generate income in Slovenia either through a permanent establishment or through a Slovene resident acquiring company. If the acquiring company is not resident in Slovenia, but it is however a resident of another EU Member State, the provisions, reserves, losses, assets and liabilities should be effectively connected (belong to) with the permanent establishment of that acquiring company in Slovenia. The provisions, reserves, losses, assets and liabilities should not be effectively connected (belong to) with a permanent establishment of the Slovene resident acquiring company in another Member State.	Article 50/I (2,3) of the Corporate Income Tax Act.

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company Pursuant to the Corporate Income Tax Act, a merger should be profit tax exempt at the level of the receiving company, even if the profit can be allocated to the cancellation of a holding in shares of the receiving company in the transferring company.	Article 49/I - 2 (c) of the Corporate Income Tax Act

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral We are not aware of the practical application of the C-470/04*'N'* case in Slovenia. However tax payers can rely on ECJ decisions in their claims or submissions before the tax authorities. Therefore, it should be possible to claim that no taxation should apply to gains derived from assets and liabilities which are not connected to a permanent establishment. Moreover, the requirement of obtaining the prior approval of the tax administration before carrying out an operation falling within the scope of relief under the directive was applicable from 1 January 2005 to 1 January 2007. The new Corporate Income Tax Act, no longer provides for such a requirement. Therefore, it may be construed that such a restriction may conflict with the decision of the ECJ and the amendment to the Corporate Income Tax Act is in accordance with the ECJ decision. Furthermore, the fact that assets and liabilities which are not effectively connected to a permanent establishment are not subject to tax relief granted by the Merger Directive, may be considered to conflict with the Case C-470/04, as it may be assessed to be too restrictive.	

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities Slovene tax law does not recognize the transparent entity concept. All legal entities are considered as non-transparent and in general should be subject to corporate income tax.	

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief Pursuant to regulations, relief is granted on the basis of a notification of the anticipated merger to the tax authorities. The tax authorities issue a decision on whether the foreseen merger will be granted tax relief arising from the Merger Directive, provided that the conditions set out in the Merger Directive are met and provided that the transaction is not solely tax motivated. Such notification is not a substantive requirement, but merely a procedural one. Therefore if a procedural error occurs in the notification process or a failure of such notification does not preclude the relief arising from the Merger Directive from being granted. For this reason, it is maintained that the relevant provision is in accordance with the Merger Directive. The purpose of such notification is to provide entities anticipating a merger, to receive advance confirmation from the tax authorities that the merger will indeed will be granted by the authorities. Please see 11.1 for a detailed outline of the procedure.	Article 53/I of the Corporate Income Tax Act

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
5.1 The term 'provisions and reserves' A general definition of reserves is provided in the Companies Act, which divides reserves into capital reserves, reserves from profits and statutory reserves. These are further regulated by Slovenian and international accounting standards. The tax definition of reserves follows the accounting definition. 5.1.1 Capital reserves The three abovementioned reserves are defined as follow: (a) Amounts which the company obtains from payments exceeding the smallest issue amounts of the shares issued or the founding stakes (paid-up capital surplus); (b) amounts which the company obtains from the issuing of convertible bonds or bonds with a share option above the nominal value of the bonds; (c) amounts additionally paid in by members for the acquisition of additional rights arising from their shares;	Article 64 of the Companies Act Article 20 of the

(d) amounts of other payments by members on the basis of the Articles of association (for example, subsequent payments by members); (e) amounts based on a simplified reduction in the subscribed capital or a reduction in the subscribed capital through a withdrawal of shares; (f) amounts arising from general capital revaluation adjustments. <u>5.1.2 Profit reserves</u> Profit reserves may only be created from the net profit for the financial year and the net profit brought forward from previous years. Profit reserves shall be divided into: (a) statutory reserves (third paragraph of this Article; liabilities item A.III.1.); (b) reserves for own share (fifth paragraph of this Article; liabilities item A.III.2.); (c) own shares (as deductible item A.III.3); (d) reserves under Articles of association (seventh paragraph of this Article; liabilities item A.III.4.). (e) other profit reserves With regards to the provisions, these should be formed in line with the applicable accounting standards. However, not all the provisions are considered tax deductible at the time when they are formed. Should the provisions not be 100% tax deductible at the time of formation, 50% of the provision is deductible at the time of formation and the other 50% is deductible at the time when it is used.	Corporate Income Tax Act

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
<u>5.2 Exclusion of 'provisions and reserves' from permanent establishments</u> We are not aware of any guidelines that have been issued with regards to this matter.	

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation method for provisions and reserves There is no guidance provided as to the allocation of provisions and reserves in the case of a division, a partial division and a transfer of assets.	

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Further conditions for carry-over of provisions and reserves A notification of the transaction must be submitted to the tax authorities in order for the carry-over of provisions and reserves to be possible.	Articles 43, 47 and 53 of the Corporate Income Tax Act

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 The concept of carry-over of losses Pursuant to the Slovene Corporate Income Tax Act, a tax loss is defined as the difference between the expenditure and income of an entity. In general, tax losses from previous fiscal periods may be carried forward indefinitely. The receiving company has the right to take over the tax losses of the transferring company, under the same conditions that would apply to the transferring company, had the transfer not been carried out. However, they are subject to the ownership and business activity test. This test is further elaborated in 6.4. In the case of a merger or a division, the carry-over does not apply to the entire loss incurred by the company, however merely to the loss, which may be attributed to the activity or the asset, which is subject of transfer (i.e. the business, assets, liabilities).	Article 36/I of the Corporate Income Tax Act Article 49/II (b) of the Corporate Income Tax Act

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment No guidance is issued as to the allocation of losses to the permanent establishment.	

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets No specific legislation has been enacted regarding the carry-over of tax loss concerning divisions, partial divisions, and transfer of assets, therefore general regulations are applicable. Divisions, partial divisions and the transfer of assets do not qualify as transactions that preclude taxpayers from applying past tax losses.	Article 49/II of the Corporate Income Tax Act.

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses A notification of the transaction must be submitted to the tax authorities in order for the carry-over of losses to be possible. Moreover, as a general rule, the carry over of losses is not possible in the following events: (a) if the ownership of shares in capital or capital share or voting rights of the taxable entity directly or indirectly changes for more than 50%, in comparison to the ownership situation at the beginning of the fiscal period, and (b) if the taxable person had not carried out its business activity for the past two years or fundamentally changes its business activity two years prior to or after the change in ownership structure. However this condition does not apply to entities that have fundamentally changed their business activity in order to maintain positions of employment or to rehabilitate or reorganize the entity.	Articles 43, 47 and 53 of the Corporate Income Tax Act Article 36/ V (1,2) and VI of the Corporate Income Tax Act.

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Amended holding threshold Slovene regulations provide that the acquiring company is granted complete tax relief for capital gain arising from the cancellation of its holding in capital that it had in the transferring company. Slovene regulations do not stipulate any minimal holding percentage requirements.	49/I (2c) of the Corporate Income Tax Act.

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Treatment of losses The provisions of the national legislation implementing the merger directive do not specifically regulate losses incurred on the cancellation of a holding. We consider that it is likely that the tax losses related to a cancellation of a holding may not be deductible.	

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Avoidance of economic double taxation at the level of the shareholder In the case of an exchange of shares, the acquired company is obliged to evaluate the exchange of shares received of the acquiring company in accordance with their market value on the day of the transfer.	Articles 45

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
8.2 Computation of the capital gain Any cash payment for shares that a shareholder of a transferred company may receive during a merger or division is not tax exempt. We are not aware of any additional official guidance on this topic.	Article 49/III, IV of the Corporate Income Tax Act

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>8.3 Further conditions for tax relief</u> Slovene legislation does not provide for any further requirements in order for tax relief to be granted under Article 8 of the Directive, except for the general requirement of notification of the tax authorities of the transfer, as relief is granted on the basis of such notification. The notification is merely a tool with which the government ensures legal predictability, as parties to a transaction notify the tax authorities before the relevant transaction is carried out. The transferred entity is obliged to notify the relevant tax before the anticipated date of the transaction. It is important to note however, that the tax relief is not conditional upon such notification. Therefore, even if an entity fails to submit a notification to the tax authorities, it may claim the relevant tax relief in its tax return. By submitting a claim for relief without a preliminary decision from the tax authorities, the entity risks refusal of tax relief, even though the transaction has already been carried out. Please see 11.1 for a more detailed outline of the procedure.	Articles 43, 47 and 53 of the Corporate Income Tax Act

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>9.1 Avoidance of economic double taxation at the level of the transferring company</u> The national legislation stipulates that the transferring company is obligated to evaluate the received securities from the acquiring company by taking their market value on the day of the transaction, into consideration.	Article 40/I (3) of the Corporate Income Tax Act

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>9.2 Further conditions for tax relief</u> A notification of the transfer should be submitted to the tax authorities in order for the transferring and receiving company to be conferred the relevant rights and obligations arising from the Merger Directive. Such notification is not a substantive requirement, but merely a procedural one. Therefore, a procedural error, which occurred during the notification was	Articles 43 of the Corporate Income Tax Act

carried out or failure of such notification does not preclude the relief arising from the Merger Directive from being granted. For this reason, it is maintained that the relevant provision is in accordance with the Merger Directive. The purpose of such notification is to provide entities anticipating a merger, to receive advance confirmation from the tax authorities that the merger will indeed will be granted by the authorities. Please see 11.1 for a detailed outline of the procedure.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
<u>9.3 Tax deferral</u> The case law of the ECJ has not been directly transposed into Slovene legislation, however it should be considered when interpreting the law and applying its benefits. The requirement of obtaining the prior approval of the tax administration before carrying out an operation falling within the scope of relief under the directive was applicable from 1 January 2005 to 1 January 2007. The new Corporate Income Tax Act, no longer provides for such a requirement. Therefore, it may be construed that such a restriction may conflict with the decision of the ECJ and the amendment to the Corporate Income Tax Act is in accordance with the ECJ decision.	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Loss recapture for permanent establishments in third Member States</u> The national legislation does not provide for loss recapture as envisaged by Article 10(1).	

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Permanent establishment in the Member State of the receiving company</u> Paragraph one of Article 10 is not implemented into Slovenian tax law. Paragraph two, of the same Article however, is implemented into Slovenian legislation and is applicable to the transfer of assets, mergers and divisions.	

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
10.3 Concept of worldwide taxation/tax credit system 10.3.1 Concept The national legislation implemented Article 10 (2) of the Directive into the Corporate Income Tax Act, which includes the possibility of applying a system of world-wide profits taxation. According to the relevant provision, any profits or capital gains of the permanent establishment resulting from a merger, division or transfer of assets may be taxed in Slovenia, if the transferring company is a Slovene resident. The possibility to tax is subject to the condition that the Slovene authorities give relief for the tax that would have been charged, if the Merger Directive was not in place, in the Member State in which that permanent establishment is situated.	Article 42 of the Corporate Income Tax Act

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
10.4 Tax deferral The case law of the ECJ has not been directly transposed into Slovene legislation, however it should be considered when interpreting the law and applying its benefits. The requirement of obtaining the prior approval of the tax administration before carrying out an operation falling within the scope of relief under the directive was applicable from 1 January 2005 to 1 January 2007. Although it was not explicitly stated that the new Corporate Income Tax Act, no longer provides for such a requirement due to the *'N'* judgment, it may be derived that this judgment was implemented into the Corporate Income Tax Act via such modification.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies Article 10a of the Directive has not been implemented into national legislation as yet. Slovene national regulations do not recognize the	

institute of 'transparent entities'. Please refer to 3.2.	

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit N/A.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit N/A.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders N/A.	

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company N/A.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
<u>10b.1 Exit taxation</u> No, Slovenia does not impose an exit taxation regime. Furthermore, an SE or SCE should be entitled to the benefits provided by the Merger Directive upon transfer of the registered office if the profits, losses, devaluation estimates and provisions arise from or are associated with the assets and liabilities, which actually remain with interlinked with the permanent entity of the SE and SCE in Slovenia or an EU Member State.	Article 54/II of the Corporate Income Tax Act.

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
<u>10b.2 The term 'head office'</u> The EC Regulation 2157/2001 was implemented in the Companies Act. The term 'head office' was translated as place of effective management. The tax law does not provide for a special translation or definition of this term. The term 'registered office' was translated as 'seat' or 'statutory seat'.	Article 433 of the Companies Act.

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
<u>10b.3 Head office and tax residency</u> The effective place of management is in fact a criterion to determine the tax residency of the entity liable to pay corporate income tax and is also a common tiebreaker criterion found in Slovenia's double tax treaties.	Article 5 of the Corporate Income Tax Act

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>**10b.4 Assets and liabilities not effectively connected with a permanent establishment**</u> The law is silent on the situation where the assets and liabilities are assessed not to be effectively connected with the permanent establishment. Due to the lack of case law on this field it is not certain how the tax authorities would decide, nevertheless taxpayers should be able to rely on the EU law, including the ECJ case law.	

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the '*N*' case?	Reference
<u>**10b.5 Tax deferral**</u> The case law of the ECJ has not been directly transposed into Slovene legislation, however it should be considered when interpreting the law and applying its benefits. It may be considered that the requirement of obtaining the prior approval of the tax administration before carrying out an operation falling within the scope of relief under the directive was applicable from 1 January 2005 to 1 January 2007, is a restrictive requirement breaching the principle of the freedom of establishment, as noted in the '*N*' case. The new Corporate Income Tax Act however, no longer provides for such a requirement.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
<u>**10c.1 The term 'comparable circumstances'**</u> The term 'comparable circumstances' has not been transposed into national legislature, nor have guidelines been issued with regards to this term.	

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
<u>10c.2 Loss recapture for permanent establishments</u> The receiving company has the right to take over the tax losses of the transferring company, under the same conditions that would apply to the transferring company, had the transfer not been carried out. However, they are subject to the ownership and business activity test. This test states that the carry over of losses is not possible in the following events: (a) if the ownership of shares in capital or capital share or voting rights of the taxable entity directly or indirectly changes for more than 50%, in comparison to the ownership situation at the beginning of the fiscal period, and (b) if the taxable person had not carried out its business activity for the past two years or fundamentally changes its business activity two years prior to or after the change in ownership structure. However this condition does not apply to entities that have fundamentally changed their business activity in order to maintain positions of employment or to rehabilitate or reorganize the entity. A notification of the transaction must be submitted to the tax authorities in order for the carry-over of losses to be possible. In the case of a merger or a division, the carry-over does not apply to the entire loss incurred by the company, however merely to the loss, which may be attributed to the activity or the asset, which is subject of transfer (i.e. the business, assets, liabilities).	Article 54 of the Corporate Income Tax Act

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>10d.1 Deemed liquidation</u> The transfer of registered office of an SE/SCE should not give rise to a deemed liquidation, however no explicit guidelines are issued with regards to this matter.	

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>**10d.2 Tax treatment of third country residents**</u> We are not aware of any tax consequences for third country residents that could arise due to the transfer of the registered office.	

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>**11.1 Transposition of anti-abuse provisions**</u> <u>11.1.1 Concept</u> The statutory reasons supporting the refusal of tax relief are directly implemented from the directive into the Corporate Income Tax Act. Tax relief is granted if the relevant transaction fulfils the formal statutory conditions transposed from the Directive into national law, such as the definition of the transaction, residency of the involved parties, the legal form of the entity etc. The general presumption that the primary goal of a transaction is tax evasion or tax avoidance if the transaction is not carried out in accordance with a valid business purpose, such as the restructuring or rationalization of an entity, is applied by the tax authorities upon assessment of the transaction. <u>11.1.2 Notification of the Tax Authorities</u> The underlying anti-abuse measure is encompassed in the condition of notification in the Corporate Income Tax Act. Tax relief arising from the merger directive is conditional upon a notification to the tax authorities of the transfer, merger, division or exchange of shares, subject to the aforementioned relief. The authorities have the possibility of assessing the transaction and refusing the relevant tax relief. Such refusal must be issued in the form of an administrative act, which must be issued within 45 days for entities involved which fall within the local standards of 'middle, small and micro sized companies' and within 90 days for entities involved that fall within the definition of a large company. The deadline elapses within 45/90 days from the notification of the tax authorities. Relief is refused if the	Article 381/VII of the Tax Procedure Act Article 47/IV of the Corporate Income Tax Act Article 379/V of the Tax Procedure Act Article 381 of the Tax Procedure Act

authorities determine the main goal of the transaction to be the decrease of tax liabilities or tax evasion. The notification is merely a tool with which the government ensures legal predictability, as parties to a transaction notify the tax authorities before the relevant transaction is carried out. The transferred entity is obliged to notify the relevant tax before the anticipated date of the transaction. It is important to note however, that the tax relief is not conditional upon such notification. Therefore, even if an entity fails to submit a notification to the tax authorities, it may claim the relevant tax relief in its tax return. By submitting a claim for relief without a preliminary decision from the tax authorities, the entity risks refusal of tax relief, even though the transaction has already been carried out. Tax payers can apply the benefits without the prior approval of the tax authorities. This may be regarded as merely an administrative mechanism, which provides the tax payer with a degree of security and the tax authorities with a control mechanism. Lack of business and financial grounds may be a reason for the tax authorities to deny the benefits of the EC Merger Directive. The sole purpose of this rule is to ensure that a transaction is not solely tax motivated. As an example of business and financial reasons the tax law stipulates that the reorganization or rationalization of business should be in line with Article 11/1 point a, of the EC Merger Directive.	

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' (*'Kofoed'*, paragraph 46)?	Reference
<u>**11.2 General anti-abuse provision**</u> N/A. Article 11(1)(a) of the Merger Directive has been transposed into national law.	Article 43, 47 and 53

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
<u>**11.3 The concept of 'wholly artificial arrangement'**</u> The concept of 'wholly artificial arrangements' is not transposed into the national Corporate Income Tax Act as such. National regulations do not place restrictions on the freedom of establishment and do not refuse tax relief, transposed from the merger directive into national law, on the grounds that an entity sought to profit from tax advantages in force in a Member State other than his State of residence.	Para. 55 of Case-196/04 *'Cadbury'*

Paragraph 55 of the '*Cadbury*' judgment which states that 'in order for a restriction on the freedom of establishment to be justified on the ground of prevention of abusive practices, the specific objective of such a restriction must be to prevent conduct involving the creation of wholly artificial arrangements which do not reflect economic reality with a view to escaping the tax normally due on the profits generated by activities carried out on national territory' is indirectly implemented into the national Tax Procedure Act, whereby the tax authorities may issue a decision refusing tax relief for profits arising from the transfer of assets, exchange of shares, divisions and mergers, should the authorities assess that the activity was carried out for the purpose of tax avoidance or evasion, thus the transaction was not carried out in order achieve the reorganization or rationalization of activities of the transferring or receiving company, or for the fulfillment of other justifiable business or financial goals. From this it may be derived that the concept of a 'wholly artificial arrangement' is implemented into national law as an arrangement with the primary goal of tax evasion or avoidance.	Article 381/VII of the Tax Procedure Act

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
<u>**11.4 Specific anti-abuse provisions**</u> The requirement of obtaining the prior approval of the tax administration before carrying out an operation falling within the scope of relief under the directive was applicable from 1 January 2005 to 1 January 2007. The new Corporate Income Tax Act, no longer provides for such a requirement.	

How have the concepts of ‘valid commercial reasons’, ‘restructuring’ and ‘rationalization’ been interpreted in your national legislation?	Reference
11.5 The concept of ‘valid commercial reasons’ The concepts ‘valid commercial reasons’, ‘restructuring’ and ‘rationalization’ have been interpreted in the national Tax Procedure Act, where it follows that tax relief may be refused if the statutory requirements are not fulfilled or if it is assessed that the main, or one of the main goals of the transaction, is tax avoidance or tax evasion, especially in the event that the transaction is not supported by valid business or financial reasons, such as the reorganization or rationalization of business activities of the transferred or acquired entity, or other justified business or financial reasons. Therefore, the term ‘valid commercial reasons’ involves financial and business reasons, which include rationalization and restructuring of the entity involved. Unfortunately, these terms are not further elaborated and should be assessed on a case by case basis. Currently, there is very limited practice available.	Article 381/VII of the Tax Procedure Act

Which party has the initial burden of proof to establish the existence or absence of ‘valid commercial reasons’?	Reference
11.6 Burden of proof Pursuant to the Tax Procedure Act, a party to the procedure is obligated to support its submissions with evidence. From this it may be inferred that the party notifying the tax authorities carries the burden of establishing the existence of ‘valid commercial reasons’.	Article 76 of the Tax Procedure Act

SPAIN

Abbreviations

English	Spanish	English	Spanish
CITA	TRLIS	Corporate Income Tax Act	Real Decreto Legislativo 4/2004, por el que se aprueba el Texto Refundido de la Ley del Impuesto sobre Sociedades.
GTL	LGT	General Tax Law	Ley 58/2003, de 17 de diciembre, General Tributaria.
LLCA	LSL	Limited Liability Companies Act	Ley 2/1995, de 23 de marzo, de Sociedades de Responsabilidad Limitada
NRITA	TRIRNR	Non Residents' Income Tax Act	Real Decreto Legislativo 5/2004, de 5 de marzo, por el que se aprueba el Texto Refundido de la Ley del Impuesto sobre la Renta de No Residentes.
PITA	LIRPF	Personal Income Tax Act	Ley 35/2006, de 28 de noviembre, del Impuesto sobre la Renta de las Personas Físicas y de modificación parcial de las Leyes de los Impuestos sobre Sociedades, sobre la Renta de No Residentes y sobre el Patrimonio.
SCA	LSA	Stock Corporations Act	Real Decreto Legislativo 1564/1989, de 22 de diciembre, por el que se aprueba el Texto Refundido de la Ley de Sociedades Anónimas

Survey of the Implementation of Council Directive 90/434/EEC

(The Merger Directive, as amended)

SPAIN

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.

Overall state of implementation

Implementation process of the Directive

The 1990 Merger Directive has been implemented in Spain through the following pieces of legislation:

(a) Law 29/1991 of December 16th ("Ley de adecuación de determinados conceptos impositivos a las Directivas y Reglamentos de las Comunidades Europeas") that came into forth on January 1st, 1992, January.

(b) The tax regime introduced by Law 29/1991 was later included in the Corporate Income Tax Act number 43/1995 which came into force on 1st January 1996. This initial CITA was revoked and substituted for technical reasons, -such as the renumbering of Articles-, by the CITA that is presently in force (approved by Royal Decree 4/2004, of 5th of March).

(c) Law 29/1991 modified the Stamp Duty Act to introduce the Capital Duty tax exemptions applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares (the Stamp Duty Act presently in force was approved by Royal Decree 1/1993 of 24th September). Law 29/1991 also modified the VAT Act to introduce the non subjection to VAT of mergers, divisions, partial divisions, transfers of assets and exchanges of shares under certain conditions.

(d) The amendments made by the Directive 2005/19 of 17th of February were implemented by Law 25/2006, of July 17th, ("Ley por la que se modifica el regimen fiscal de las reorganizaciones empresariales y el sistema portuario y se aprueban medidas tributarias para la financiación sanitaria y para el sector de transporte por carretera".), which introduced these amendments into the CITA.

The Spanish General Directorate of Taxes has issued numerous binding and non binding rulings, upon request from taxpayers, on the interpretation of the above legislation, that are generally relied upon as an indication of the tax authorities' criterion. There are also several resolutions from the Tax Courts and judgments from judicial Courts on these provisions.

Article 1 – Scope

Please describe how the expression "in which companies from two or more Member States are involved" has been interpreted and implemented. Has the term "companies involved" been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> No definition of the term "companies involved" has been provided in the implementing legislation. There are general references to the types of companies that may be eligible for the regime as contained in the relevant Annex of the Directive. Rather, a definition of transactions that may be carried out under the tax free regime is provided. Further, rules clarifying when the option not to tax is available are provided, These rules establish when a merger may be carried out under the option not to tax and when the shareholders (e.g. parent companies) of the merged entities may also benefit from the option not to tax. Generally speaking, the criteria is that the option not to tax may be applied to transactions that fall under the definition of mergers, spin offs, etc provided that, after the transaction, there continues to be a connection point with Spain. For instance, domestic mergers and mergers where the receiving entity is not an EU resident may elect for the regime (in the latter case in respect of elements that are connected to a Spanish permanent establishment). Also, there is a general exclusion from the regime of "tax haven" (blacklisted) entities that includes Malta, Cyprus, The Netherlands Antilles and certain Luxembourg entities. The first three jurisdictions however have signed or are in the process of signing agreements with Spain that have or will terminate their consideration as "tax haven" entities for Spanish tax purposes, and thus their non-eligibility for the special reorganization tax deferral regime. In relation to Luxembourg, it is mainly (now in the process of being phased out) "1929" holding companies that are affected, although certain Luxembourg collective investment entities could also be affected (generally, Spanish collective investment entities may be entitled to the reorganizations tax deferral regime, which could, in certain cases, mean a different treatment for Luxembourg and for Spanish collective investment entities).	Articles 83 to 96 of the CITA

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
<u>1.2 Foreign Member State and third state merger</u> The Spanish option not to tax as implemented in the CITA can be applied to transactions where a Spanish resident entity transfers assets located in Spain. In this case if the acquiring entity is not resident in Spain the assets transferred must remain connected to a permanent establishment in the Spanish territory for the option not to tax to be applicable. The same treatment applies to transfers by Spanish companies of permanent establishments located in non EU States to other Spanish entities. Under Article 84.1 b CITA, the option not to tax also applies to transfers among Spanish companies of permanent establishments located in non EU States to other Spanish entities. We consider that this provision would not be in direct conflict with Directive 90/434/EEC, but rather may be contrary to the EC Treaty (restriction of both the free movement of capital and the freedom of establishment), insofar as the option not to tax (deferral) is afforded only to transfers taking place between Spanish entities. The question arises whether this difference in treatment could be justified on the basis of the principle of territorial taxation and on adequate allocation of taxation rights between Member States, since if, after the transaction there is no permanent establishment left behind in Spain, normally tax treaties signed by Spain would exclude the possibility for Spain to tax the gain arising upon transfer of the non-Spanish permanent establishment once it is owned by a non-Spanish taxpayer. Commentators have pointed out that a less restrictive solution to this issue could be to allow a deferral of payment of the tax until the moment in which the assets are transferred out of the group. It should also be taken into account that, pursuant to Article 22 of CITA, Spain normally exempts from tax the gain arising upon a transfer of a foreign PE of a Spanish company, therefore, the possible discrimination for non-application of the option not to tax would only arise, as a matter of practice, in cases in which the conditions to apply said Article 22 are not met. The Spanish option not to tax is also applicable to the shareholders of the companies involved. For instance, in the case of share exchanges, Spanish legislation requires that the shareholders be resident in Spain, in another EU Member State or in a third country provided that, in this latter case, the shares received in exchange are issued by a Spanish resident entity. We consider that in the case where the contributing shareholders are not resident in a EU Member State, the restriction that the contributee company must be resident in Spain for the option not to tax to apply (therefore excluding other EU Member State resident recipient entities)	Articles 84, 87 and 88 of the CITA

could potentially be contrary to EC Treaty, as such difference in treatment may restrict both the free movement of capital and the freedom of establishment. Again, the question arises as to whether the discrimination could be justified on the basis that otherwise Spain would lose the right to tax the gain embedded in a subsidiary that was previously held by a non-EU resident. Also on this regard, note that Article 21.2.d) CITA establishes that in the case of contributions of shares or assets by a Spanish company to a foreign entity (whether resident in the EU or not), where the transaction has been made pursuant to the special reorganizations (tax deferral) regime (i.e. assuming that there is no entitlement to the Spanish participation exemption regime either on the transfer of foreign shares or foreign permanent establishments), a future gain on the transfer of such shares (received on the contribution of the foreign shares or assets to the capital of a foreign entity) will be subject to Spanish taxation up to the amount of the deferred gain (pursuant to the option not to tax contained in the special reorganizations regime). Whereas domestic asset-for-share and share-for-share transactions are not subject to a participation exemption system (such as the one applicable for international transactions, under certain conditions), there is a difference in treatment in the domestic and the foreign transactions in that, in the domestic transaction, there is a roll-over of the cost (so that a future gain will be higher than if a step up in value had occurred), and in the international transaction there is an actual gain 'freezing' of the deferred gain. This means that if a future gain on the foreign shares received in exchange for the contribution of the assets the tax on which was deferred were to correspond not to the relevant contributed assets or shares (which could have even gone down in value underneath the foreign company whose shares were issued in exchange for the contribution) but to other assets that would qualify for the participation exemption, there would still be a taxation of the 'frozen' gain above referred to. Although the mechanism in itself would seem to be in line with the rationale under the '*N*' case and the position of the Commission in its Communication 'Exit taxation and the need for co-ordination of Member States' tax policies' (except for the potential double taxation of the same gain, or for the fact that taxation could occur in respect of an asset that has gone down in value), ascertaining whether or not the difference in treatment (internal versus cross-border contributions) may be contrary to EU primary law is a complex matter which should also be analyzed in the context of the proper allocation of taxing rights held by Spain over such assets.	

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term "securities": When describing the transactions that may benefit from the special regime, the reference is made to the term "securities". However, the term "securities" is not interpreted or defined in the implementing legislation, nor are there administrative guidelines on this interpretation. From a strict point of view, under the SCA the term "securities" only refers to the shares of the so-called Stock Corporations (Sociedades Anónimas). The Limited Liability Companies Act expressly states that the term "securities" cannot be understood to comprise the participations (shares) of Limited Liability Companies (Sociedad de Responsabilidad Limitada). Notwithstanding the forgoing it is broadly accepted by the Spanish tax authorities and tax and judicial courts that the term "securities" contained in the CITA refers to both Stock Corporations' shares and Limited Liability Companies' participations. Also, in Articles other than those containing the definition of transactions that may be executed under the special regime, the reference is made to "acciones" (securitiess representing the stock of Sociedades Anónimas) and "participaciones" (securities representing the stock of Sociedades de Responsabilidad Limitada).	Articles 47 and 48 of the SCA Article 5 of the LLCA Aricle 86 of the CITA

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term "cash payments". Yes, the possibility to allow 10% cash payment for reorganization in merger, division/partial divisions and exchange of shares has been implemented in the CITA. However this piece of legislation does not clarify whether it applies on a per shareholder basis or overall basis. There are no rulings or decisions on this latter point, but the majority of authors are of the view that it should apply on a per shareholder basis. The SCA allows a maximum cash payment of 10% of the face value of the securities allocated to each shareholder.	Article 83 CITA Chapter 8th SCA (Article 247)

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger. The national implementation covers the three types of mergers but does not include further types. There has in past years been controversy as to whether an upstream simplified liquidation procedure may fit the definition of merger given by the CITA but recent rulings indicate that if a liquidation takes place –regardless of whether it is simplified or not- this falls outside the definition. The upstream simplified liquidation procedure is one of the alternatives to wind up a Company, with a sole shareholder, without a formal liquidation (however a simplified liquidation procedure takes place). The following procedure must be completed: (a) the decision to transfer all assets and liabilites must be taken by the General Shareholders' Meeting; (b) this resolution must be published in the Official Gazette of the Commercial Registry and in a local newspaper; (c) the creditors will have the right to challenge the transfer, within one month since the last publication of such announcements; and (d) once the one month period is completed, the Public Deed executing the transaction is granted and must thereafter be registered with the Commercial Registry.	Article 117 LLCA Article 266 SCA Article 83.1 CITA

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares. The Spanish legislation grants relief in respect of successive exchange of shares that contribute to the build-up of a state in the company after a majority holding has already been obtained.	Article 83.5 of the CITA

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
2.5 Consolidation of qualifying holding The relief is subject to the transaction being carried out for bona fide commercial reasons.	Article 96.2 of the CITA

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
2.6 The term "branch of activity" Spanish tax law provides the following definition of the term "branch of activity: The set of assets which can form, by themselves, an autonomous economic unit defining an economic activity, namely an overall unit capable of functioning by its own means. The debts arising from the organization or functioning of the items that are transferred may be also attributed to the acquiring company. The tax authorities have issued numerous rulings where they dictate whether or not a branch of activity exists in a given situation, based upon the description provided by the taxpayer. The point that must be highlighted is that it is the tax authorities´ criteria that the branch of activity must exist as such –albeit internally-prior to the transfer of the same to another company and that the assets that are transferred to the acquiring company must be sufficient for the activity to continue to be carried out with these resources after the transaction takes place. For instance, in a ruling dated 4 October 1999: "The tax definition does mean not that there is not a need for the economic activity to exist prior to the de-merger in the transferring company; it is however the case that it is sufficient if the economic activity exists only from an internal point of view, provided it is possible to identify a set of assets allocated or destined to the same. This is independent of the fact that the human and material resources needed to manage this activity may be internal or external, that is to say, the management of the activity may be outsourced. " Although after the 2001 amendment of the definition of branch of activity, it is possible to argue that a branch exists where the assets allocated to that branch form an economic unit capable of functioning by its own means in the receiving company, the Spanish tax authorities continue to require that the branch of activity exists in the transferring company. Thereafter the branch of activity as such must be found not only in the receiving entity but also in the transferrring entity before the contribution.	Article 83.4 of the CITA

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
3.1 Types of entities Spanish legislation extends the application of the Merger Directive to more types of Spanish entities than those listed in the Annex. The option not to tax is limited to the non-Spanish entities that are mentioned in the Directive (there is an express reference to the Annex of the Directive) and to the Spanish entities that are subject to Spanish CITA. It is doubtful that the extension of the Spanish list of entities that may be entitled to the tax deferral regime is contrary to the Directive, as it seems that the aim of the Directive is not to limit the number of entities that may be entitled to its benefits (and, as such, certain Member States have chosen to include in the Annex to the Directive all entities subject to the local corporate income tax). A different issue is whether under EU primary law Spain should grant Merger Directive benefits to all EU resident entities that are subject to a corporate income tax, but this would seem to go beyond of what has been agreed in the context of the Directive itself.	Article 87.6 of the CITA

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
3.2 Transparent entities No, the national legislation does not regard any of the Spanish entities listed in the Annex as being transparent, as these entities are not included in the list provided under the GTL. Please see 3.4. As regards non-Spanish entities, it is possible that some of the entities listed in the Annex to the Directive are considered as transparent for Spanish tax purposes. There is not a list of foreign transparent entities under Spanish tax law. In accordance with Spanish tax legislation, whether or not a particular entity should be treated as transparent must be determined on a case-by-case basis, after a thorough examination of the legal and tax attributes of the said entity in its domestic jurisdiction. Please see 3.1.	

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency Companies qualify as tax resident in Spain in any of the following cases: (a) where they have been incorporated under Spanish Company	Article 8 of the CITA

legislation, (b) when they have their domicile in Spain, or (c) when they have their place of effective management in Spain. The most common residence tiebreaker criterion in the double tax conventions concluded by Spain is effective place of management.	

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
<u>**3.4 Subject-to-tax clause**</u> Deferral of the taxable income deriving from the transactions that fall under the scope of this tax regime is not allowed it the acquiring entity is exempt or is a transparent entity as defined under Spanish tax law.	Article 84.1 of the CITA

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
<u>**3.5 Shareholder requirements**</u> There are limitations where the shareholders are resident in tax havens: tax haven shareholders may not benefit from the option not to tax in mergers or spin offs or exchange of share transactions. The limitation is drafted broadly, to include all cases where a tax haven resident shareholder intervenes.	

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>**4.1 The concepts of "real values" and "value for tax purposes"**</u> <u>4.1.1 General points</u> Spanish legislation provides a general principle which is that a company's assets and liabilities must be valued in accordance with the provisions of the Commercial Code and that variations in value that originate due to the application of the 'reasonable value' criteria are only given tax effects when the variation is recorded in the company's Profit and Loss Account. Special rules dictate that the following elements must be valued at fair market value, thus determining that the transferor is taxed on the	Article 15 of the CITA

difference between the value resulting from the above rule and the fair market value of the element at the date of transfer: (a) Assets transferred or acquired for no consideration. (b) Assets contributed to companies and the value received in exchange for the contribution. (c) Elements transferred to a company's shareholders or partners in the company's dissolution, in a separation of shareholders from the company, in a share capital reduction with refund of contributions to shareholders, in a share premium distribution or in a dividend distribution. (d) Elements transferred by virtue of a merger, absorption or total or partial de-merger.	
(e) Elements acquired in exchange for other elements. (f) Elements acquired by exchange or conversion.	Articles 84, 85, 86 and 87 of the CITA
Fair market value is defined as the value that would have been agreed upon by non related parties under normal market conditions. Spanish law relies on the OECD valuation methods to determine fair market value. <u>4.1.2 Reorganizations regime</u> The Chapter governing the application of the tax-free regime, provides the following rules in respect of elements that are transferred or acquired under a tax free transaction. <u>4.1.3 Tax value of the elements acquired in a tax-free transaction</u>	Article 85 of the CITA
Article 86 provides that assets and rights acquired by virtue of a transfer derived from the transactions to which the special regime has been applied are valued, for tax purposes, at the same value they had in the transferring entity before the transaction took place. The acquisition date of the transferring entity is also maintained for tax purposes. This tax value is corrected (increased) in an amount equal to that which has been effectively taxed.	Article 86 of the CITA
This latter provision refers to cases where the part of the transfer is taxable either (a) because the assets do not, for instance, remain connected to a permanent establishment of the receiving company in Spain and the transferring entity cannot apply for the regime in respect of their transfer or (b) because the transferring entity elects to be taxed on the capital gain deriving from the transfer of part or all of the assets and rights. This election can be made by the transferring entity when filing the tax return corresponding to the transaction and makes it possible to apply the	Article 87 of the CITA

tax free regime only partially in respect of capital gains or to apply the regime exclusively for indirect tax purposes. The election to be partially or totally taxed cannot be made in an exchange of shares transaction. Lastly, this provision clarifies that in those cases where the special regime is not applicable, the values to be used are those agreed upon by the parties intervening in the transaction, with the limit of fair market value. <u>4.1.4 Tax value of the shares or participations received by the company transferring a branch of activity</u> The tax value of the shares received by the company transferring a branch of activity is equal to the accounting value of the branch of activity, corrected (increased) in the amount of the gain that is included in the transferring entity's tax base (see above as to when this may occur). <u>4.1.5 Exchange of shares</u> The receiving entity must value the shares at the value these had for the shareholders under the CITA or PITA rules prior to the transaction, except in those cases where the fair market value of these shares is lower than the value resulting from the application of these rules, in which case they must be valued by the receiving entity at fair market value. In those cases where the shareholders are not taxable in Spain on the capital gain resulting from the transfer of shares (by application of Tax Treaty benefits or domestic exemptions), the shares must be valued by the receiving entity at the value agreed upon by the parties executing the transaction, subject to it not exceeding fair market value. Shareholders shall value the shares received, for tax purposes, at the same value the shares that are exchanged had under the CITA or PITA rules. This value must be increased or reduced in the cash contribution that is made or received by the shareholder. It is explicitly stated that these securities maintain the acquisition date the securities transferred had prior to the transaction. If a share-for-share transaction is carried out under the tax free regime, where the shareholders are taxable in Spain, they cannot compute a loss. In the case of mergers, spin offs, etc, they may compute such a loss as they may waive the application of the tax free regime for direct tax purposes.	

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
<u>4.2 Specific guidance for divisions/partial divisions</u> There are no specific rules for divisions/partial divisions –other than those explained under 4.1.	

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How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of "effectively connected" and "permanent establishment" **4.3.1 Effectively connected** The NRITA provides that "patrimonial elements" are effectively connected with a permanent establishment when they are functionally connected to the development of the permanent establishment's activity. Securities or other assets representing the participation in the equity of a company are only 'effectively connected' to a permanent establishment when the permanent establishment is a branch that has had access to the Company Registry (has been registered with the Company Registry) are recorded in the branch's accounts and the branch has the human and material resources required to manage this shareholding. **4.3.2 Permanent establishment** A permanent establishment is deemed to exist under the definition that is provided by Spanish NRITL when the following conditions concur: (a) a business activity is undertaken in the Spanish territory on a habitual basis through a fixed place of business (physical permanent establishment), or (b) a business activity is carried out in Spain through a dependent agent (legal permanent establishment) which would be authorized to make up/conclude binding contracts. In particular, it shall be understood that places of management, branches, offices, premises, warehouses, amongst others, constitute a permanent establishment. Installation works in Spain constitute a permanent establishment if they last for more than 6 months. Although this definition is imported from the OECD definition it does not include exceptions provided under the definition given by Tax Treaties entered into by Spain of the term permanent establishment. To be noted that where a Tax Treaty is in place, whether or not a permanent establishment exists must be determined by reference to the Treaty definition.	Article 16 of the NRITA Article 13.1a) of the NRITA

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief Where legislation seeks to treat transfers as being not subject to tax, there is no attempt to claw back relief claimed in respect of prior periods.	

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment Where the acquiring entity is not a Spanish tax resident and the transferred assets and liabilities are not effectively connected with a permanent establishment in Spain after the transaction, the transferring entity is taxable on the gain (or loss) deriving from these assets and liabilities under the normal rules governing transfers. It is further provided that if assets and liabilities that have been transferred on a tax free basis under the Directive cease to be effectively connected with that permanent establishment, the transferring company shall be taxed on the difference between the fair market value of the assets at the date of transfer and the tax value of these assets (that derives from the application of the above described rules), reduced by the depreciation and write down of the same that has been recorded for accounting purposes and has been allowed for tax purposes. Taxation occurs in the year the assets cease to be connected to the permanent establishment. It would seem that if the Directive entitles Member States to require the effective connection of the transferred assets with a permanent establishment, then when that effective connection ceases to exist, the Member State should be entitled to tax the deferred gain. Whether or not such mechanism may be contrary to EU primary law is a more complex matter. Transfers of permanent establishments located in a non EU Member State from a Spanish company to another Spanish company can be eligible for tax deferral (or, under certain circumstances, as exempt), irrespective of the fact that they are not effectively connected with a Spanish permanent establishment (please see above answer to 1.2).	Article 84.1 of the CITA

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company Yes, it is profit tax exempt even in this case.	Article 84 of the CITA

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral Spain imposes an "exit tax" upon migration of companies or individuals from Spain and has not amended the legislation implementing the Mergers Directive as a result of Case Law. If shareholders that have benefited from tax-free transaction lose their Spanish tax resident condition, taxation occurs. Payment of the tax due can be deferred to the date the shares are transferred provided that a guarantee to secure payment is made available. Requiring a guarantee of payment is a less restrictive method (thus, it would seem, more proportionate with the objective of not losing taxing power, which it would seem an objective at least not contrary to the Directive) than requiring immediate payment of the tax, although it could in certain cases it could be quite burdensome and therefore, disproportionate (e.g., for high amounts). Again, under the '*Lasteyrie*' and '*N*' cases, this type of guarantees would seem to be contrary to EC primary law (free movement).	Article 88.3 of the CITA

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities GTL provides a list of entities that are treated as tax transparent and also provides that all entities that have no legal personality but form a business unit or separate patrimony that may be subject to taxation, should be treated as tax transparent. The CITA further describes how this type of entities must be treated for direct tax purposes. Further guidelines are provided under the NRITA, with reference to tax transparent entities that are incorporated in Spain or elsewhere.	Article 35.4 of the GTL Article 6 of the CITA Article 7, 35, 36 and 37 of the NRITA

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief That the transaction is carried out for bona fide commercial reasons.	Article 96.2 of the CITA

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
5.1 The term "provisions and reserves" "Provisions and reserves" are generally understood to be accounting principles and, as such, defined under Spanish accounting legislation. No specific definition exists for tax purposes. Provisions that are recorded for accounting purposes are only allowed for tax purposes if they meet the requirements set out in the CITA. For instance, provisions to reflect the decline in value of a subsidiary's shares are only allowed for tax purposes up to an amount equal to the negative difference in the subsidiary's equity from the beginning to the end of the financial year; provisions for future risks are generally not allowed as a tax expense; provisions for bad debts are only allowed if the debt is overdue by at least six months and the debtor is not a public entity, the State, the amount due is not guaranteed, etc. The CITA establishes that in the case of mergers or total divisions where a universal succession takes place, the tax rights and obligations are transferred to the receiving company. This entity must comply with the relevant requirements to continue to apply the tax benefits that are transferred to it. In the case of a transfer of assets or partial division only the tax rights and obligations linked to the assets transferred are allocated to the acquiring entity. As in the cases of universal succession, this entity will have to comply with the requirements to continue the application of the tax benefits transferred.	Article 90 of the CITA

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
<u>**5.2 Exclusion of "provisions and reserves" from permanent establishments**</u> There is no specific regulation in the Spanish CITA on this point so the answer to 5.1 is not relevant. Please refer to 6.2 on the allocation of tax losses to permanent establishments.	

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
<u>**5.3 Allocation method for provisions and reserves**</u> The CITA does not provide specific guidelines or methods, although generally tax will follow the method applied for accounting purposes, the general rule being that the provision follows the asset to which it refers. For instance, where a credit is transferred, the bad debt provision would follow such credit. Please also note that, as explained under 5.1, provisions and reserves are accounting criteria.	

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
<u>**5.4 Further conditions for carry-over of provisions and reserves**</u> There are no specific rules to cover this situation.	

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
<u>**6.1 The concept of carry-over of losses**</u> There is no specific definition of loss for the purposes of implementing Article 6. Rather, the implementation relies on the general definition of tax loss existing under the CITA, which is the loss resulting after making the applicable book-to-tax adjustments to the accounting profit or loss recorded by a company or permanent establishment. Losses may generally be carried forward for a 15 year period.	Article 10.3 of the CITA Article 25 of the CITA

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment There is no method covering this situation. Rulings describe when losses may be transferred by or to a permanent establishment, this being when the transferring entity has no other presence in Spain, as explained under 6.3.	

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets Tax losses may only be transferred to the receiving company where the transferring company ceases to exist, that is, in total divisions and mergers and, as explained above in 6.2, in certain cases where losses correspond to a permanent establishment and there is no other presence in Spain of the transferring entity. There is no specific guidance as to how losses must be allocated when there is more than one receiving company, other that they should be allocated to the company receiving the activity to which they correspond. When this identification cannot be made (for example, where there is no clear distinction as to the activity from which the losses have originated) other allocation criteria may be used. There is no list of these allocation criteria, but provided they are reasonable and given the lack of guidelines, they should be allowed (for instance, based on the proportion the assets transferred represent over total assets, percentage in which business transferred has historically contributed to the creation of losses, etc.).	Article 90 of the CITA

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Further conditions for carry over of losses Losses cannot be transferred in transactions, such as mergers, that are carried out under the "general" regime. In other words, losses and other tax attributes can only be transferred by a company or permanent establishment to another company or permanent establishment when the transaction qualifies for the tax free regime and subject to compliance with the above requirements and the general requirement that the transaction be carried out for bona fide commercial reasons (please see 11.1). Spanish tax law provides that when a merger is carried out under the tax-free reorganizations regime, the losses of the transferring entity may be transferred to the receiving company subject to certain limitations. The	Article 90.3 of the CITA

aim of the restrictions on the transfer of losses in tax-free mergers is to avoid double relief for tax losses in cases where the transferring and receiving companies belong to the same group of companies as defined in Sec. 42 of the Commercial Code. These restrictions are as follows. (a) First restriction: The transferring company's tax losses must be reduced by an amount equal to the positive difference between the contributions made by the present or prior shareholders of this company to the company's equity and the value of the investment in this company in its parent company's books. (b) Second restriction: The second restriction is that the transferring company's tax losses may not be "transferred" to the receiving company if the losses have caused a group company to reflect an expense or loss derived from the decline in value of the shares in the transferring company. This second restriction only applies in respect of carried forward tax losses reported after the transferring company's shares are purchased by the receiving company's group.	

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
<u>7.1 Amended holding threshold</u> Spanish legislation has historically required a 5% holding threshold in this respect. As such, no amendment has been introduced recently.	Article 89 of the CITA

Article 7(1) covers <u>gains</u> accruing on the cancellation of a holding. It does not cover <u>losses</u> that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
<u>7.2 Treatment of losses</u> Yes, Spanish legislation deals with losses that may be realized upon the cancellation of a holding by providing that the loss shall not be tax deductible to the extent the holding company has a holding of at least 5% in the transferring company and the loss corresponds to existing or in built losses of the transferring company.	Article 89.1 of the CITA

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
<u>8.1 Avoidance of economic double taxation at the level of the shareholder</u> Securities issued under a merger, division or partial division are treated in the hands of the recipient shareholders as if they formed part of their original shareholding in the transferring company. Hence there is no taxation of capital gains and the value for tax purposes of the new shareholding is equal to the value the securities exchanged had immediately before the merger, division or partial division. The assets that are transferred are treated in the hands of the receiving company as inheriting the same tax basis they had when they were held by the transferring entity. Hence there is no market value step up. Please refer to 4.1 for a more detailed explanation on the above. The CITA foresees a mechanism to avoid the economic double taxation which is common for the exchange of shares and for the transfers of assets or shares received in exchange for a branch of activity.	Article 85, 87 and 88 of the CITA

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
<u>8.2 Computation of the capital gain</u> According to the CITA, cash receipts reduce the value for tax purposes of the securities received in the case of a merger, division, partial division or exchange of shares. Conversely if the shareholders have to make cash payments, these increase the tax basis of the securities received.	Article 88.2 of the CITA

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
<u>8.3 Further conditions for tax relief</u> The transaction must have been for bona fide commercial reasons.	Article 96 of the CITA

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
<u>9.1 Avoidance of economic double taxation at the level of the transferring company</u> In the case of a transfer of assets or exchange of shares, the newly received shares are valued at the tax value the assets had prior to the transfer and the assets or shares received are also valued at their prior value (please refer to 4.1 for a more detailed explanation) Therefore, there is no step-up of the value of the assets and/or of the shares received in exchange. The CITA establishes a mechanism to avoid the economic double taxation that applies only to transfers of assets and exchange of shares (e.g., not in the case of mergers, partial or total divisions, etc.): (a) If the assets/shares transferred are recorded for accounting purposes by the receiving entity at the same value they had in the transferring entity, a full dividend tax credit applies to the distribution of profits retained earnings that derive from the sale of these assets (if the same occurs). The right to benefit from this tax credit is granted even where the general requirements for its application (minimum holding period, and minimum shareholding) are not met. The tax credit can be applied when dividends are distributed out of the retained earnings deriving from the sale of the assets. The deductibility of the decline in value of the shares, caused by the distribution of the retained earnings, is only allowed for tax purposes when an amount equal to this amount has been taxed in Spain in a transfer of the shares received in the tax-free transaction. (b) If the value of the assets/shares has been stepped up for accounting purposes by the receiving entity, this entity is entitled to make negative book-to-tax adjustments equal to the positive book-to-tax adjustments made in the past (in respect of these assets), at the moment it is extinguished. These negative book-to-tax adjustments may also be made if the shares in this entity are sold, the limit in this second case being the amount on which the shareholders have been taxed on the sale of the shares.	Article 86 of the CITA Article 95 of the CITA

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
9.2 Conditions for tax relief The transaction must have been for bona fide commercial reasons.	Article 96 of the CITL

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
9.3 Tax deferral No changes have been introduced as a consequence of the above.	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
10.1 Loss recapture for permanent establishments in third Member States Where a permanent establishment in an EU Member State is transferred, the taxable base of the Spanish transferring company must be increased by the amount in which losses have exceeded profits allocated by the permanent establishment to its taxable base. This reinstatement of taxable profits is limited to the amount of the capital gain deriving from the transfer of the permanent establishment.	Article 92 of the CITA

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
10.2 Permanent establishment in the Member State of the receiving company There is no special reference to this situation. Therefore the same rule described under 10.1 above applies.	Article 92 of the CITA

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Concept of worldwide taxation/tax credit system</u> If the taxable profits mentioned under 10.1 do not meet the requirements for the application of the exemption to avoid international double taxation, the transferring entity is entitled to a relief for the tax that, but for the provisions of this Directive, would have been charged on those profits in the Member Sate in which that permanent establishment is situated. The relief is limited to the amount of the tax that had actually been charged and paid by the transferring company. This relief can be applied automatically.	Article 92 of the CITA

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
<u>10.4 Tax deferral</u> No changes have been introduced as a consequence of the above.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
<u>10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies</u> Spain has opted not to transpose Article 10a of the MD.	

How have the 'profits' of an <u>acquired</u> company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
<u>10a.2 Tax base for notional tax credit</u> N/A.	

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit N/A.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders Spain has opted to implement Article 10a(3) of the MD, as the option not to tax cannot be exercised where the receiving or acquiring company is fiscally transparent.	Article 84 of the CITA

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Comparison with a resident fiscally transparent company N/A.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ("the SE Statute") requires that the "registered office" be located in the same Member State as the "head office". It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b.1 Exit taxation The CITA provides that a Spanish company suffers exit taxation only when it transfers its tax residence to another State. Exit taxation only arises in respect of elements that do not remain connected to a permanent establishment in Spain.	Article 17 of the CITA

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 The term "head office" This term has not been defined.	

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Head office and tax residency Companies are deemed to be Spanish tax residents under any of the following circumstances: (a) they have been incorporated in accordance with Spanish legislation, (b) their domicile is located in Spain, or (c) their effective place of management is situated in Spain. The tiebreaker rule is generally the effective place of management.	Article 8 of the CITA

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
10b.4 Assets and liabilities not effectively connected with a permanent establishment The option not to tax cannot be effected if assets and liabilities are not connected with a permanent establishment in Spain and taxation occurs as if a deemed disposal had taken place.	Article 17.1.a) of the CITA Article 83.7 of the CITA

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the '*N*' case?	Reference
10b.5 Tax deferral Spain appears to take the position that the principles outlined by the ECJ in the case C-470/04 '*N*' only apply to individuals and have no impact on the interpretation of the Merger Directive. See comments to previous question. Spain requires the connection of the assets of a migrating company with a Spanish permanent establishment in order not to tax the embedded gain. See also comments elsewhere in this survey regarding the	

potential incompatibility of the Spanish exit taxation rules with the '*N*' Case (migration of residence of shareholders).	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
<u>**10c.1 The term "comparable circumstances"**</u> It has not been defined in this particular case. However, there are rulings providing guidance as to how to allocate losses to permanent establishments in other tax free transactions that should apply to these cases. The rulings describe how to apply the limitations to the transfer of tax losses when a permanent establishment in lieu of a company is involved in the transaction.	

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
<u>**10c.2 Loss recapture for permanent establishments**</u> Please refer to 10.3 above.	

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
<u>**10d.1 Deemed liquidation**</u> Companies are only taxable on a deemed disposal of assets that do not remain connected to a permanent establishment in Spain. No taxation for shareholders in this case.	Article 17.1 a) of the CITA

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
<u>10d.2 Tax treatment of third country residents</u> Please see 10d.1.	

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 *Leur-Bloem* and C321/05 *Kofoed*. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> Yes it has been transposed as follows: 'The regime governed in this Chapter shall not be applicable when the transaction's main purpose is fraud or tax evasion. In particular, the regime will not be applicable when the transaction is not carried out for valid commercial reasons, such as the restructuring or rationalization of the activities of the companies, but rather with the mere finality of obtaining a tax advantage.'	Article 96 of the CITA

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on "a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance" (*Kofoed*, paragraph 46)?	Reference
<u>11.2 General anti-abuse provision</u> As noted in 11.1, Article 11(1)(a) of the Merger Directive has been transposed into Spanish law.	Article 96 of the CITA

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *Cadbury* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
<u>11.3 The concept of "wholly artificial arrangement"</u> Spain's legislation has not been amended specifically in respect of the findings of in the 'Cadbury' judgment. Although the question as to what tax	Article 96 of the CITA

constitutes "tax avoidance" has been considered in respect of other situations, existing judgments in respect of the application of the reorganizations regime determine that there is no business purposes – other than obtaining tax advantages- in the situations that are discussed and disallow the application of the regime. These judgments refer to situations where the receiving company is a pure holding company and carried out no business activities prior to the merger. Moreover, the cases to which the judgments refer are situations in which the result of the merger is the step up the tax value of the assets of the transferring company (including goodwill) and the transfer of the tax losses of the transferring company.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
<u>11.4 Specific anti-abuse provisions</u> No such restrictions have been imposed. Taxpayers may file for rulings in advance of executing a tax-free reorganization to obtain the tax authorities' opinion as to whether the transaction may qualify for the application of the regime. Provided the factual description given in the filing for the ruling fits the facts that occur thereafter, the taxpayer that obtains a positive ruling is protected by the same.	Article 96.2 of the CITA

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
<u>11.5 The concept of "valid commercial reasons"</u> No specific interpretation, other than the reference contained in the general anti-avoidance clause, is made in Spanish legislation. Rulings, decisions from the tax courts and judgments from judicial courts take the approach that whether or not valid commercial reasons exist is a matter that must be assessed on a case-by-case basis. Existing rulings, decision and judgments provide guidelines as to when this is deemed to be the case and there is a fairly high amount of rulings. These rulings, decisions and judgments generally take the position that valid commercial reasons do not exist when the receiving company in a merger carried out does not have any business activity prior to the merger and/or was incorporated to purchase the shares of the transferring entity, where the merger allows to step up the tax value of the assets of the transferring company (including goodwill). Nevertheless, there are rulings allowing the application of the regime in cases of this type where there are bona fide commercial reasons (such as a complicated structure being "inherited" from the vendor, the reduction of interest on loans when the merger is imposed by banks, etc). The tax authorities are also generally reluctant to allow the application of the regime to spin offs where the shareholders would not be taxed on the	

future transfer of the shares of the receiving entities. There are numerous rulings that refer to a vast number of different situations.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof When a tax audit takes place, the inspector may ask that the taxpayer explains, demonstrates and proves the "valid commercial reasons" that support the application of the regime. If these are deemed insufficient, the inspector may then disallow the application of the regime and raise the corresponding assessment. The assessment may be appealed with the tax courts, where the taxpayer may provide evidence and arguments sustaining the existence of "valid commercial reasons". Resolutions from the tax courts may be appealed with the judicial Courts. The general rule is that the burden of proof is the taxpayer's.	

SWEDEN

Abbreviations

English	English
ITA	Income Tax Act (1999:1229)
SOU	Official reports
Swedish GAAP	Generally accepted accounting principles in Sweden

Survey of the Implementation of Council Directive 90/434/EEC

(The Merger Directive, as amended)

SWEDEN

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 31 January 2008 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued. In the event that relevant national legislation was implemented after 31 January 2008, please comment on the status occurring between 31 January 2008 and the date of implementation of the legislation.
<u>Overall state of implementation</u> <u>Tax law</u> The 1990 Merger Directive (hereinafter the Directive) was implemented in Sweden in 1995(Sweden entered the EU the same year) through a new provision, ITA. In 1999 this act was amended and the rules were transferred to a number of different tax acts. Currently the rules are included in the Swedish Income Tax Act (1999:1229) in the following sections: (a) 37 merger and division; (b) 38 transfer of assets (*'Sw verksamhetsöverlåtelse'*); (c) 38 a partial division; (d) 48a and 49 exchange of shares. The rules have been amended several times after the implementation in to the ITA, the latest amendment came into force on 1 January 2008. <u>Company law</u> Merger between two Swedish limited liability companies have been possible for several years. As regards cross-border mergers a new legislation came into force on 15 February 2008.

Article 1 – Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies?	Reference
<u>1.1 Involved companies</u> The definition of 'company' in the Swedish legislation is as follows: (a) Swedish limited liability company (SW AB), Swedish economic association, Swedish savings bank and Swedish mutual insurance company; (b) foreign company;	37:9, 38:3,38 a:4, 49:9 ITA

(c) another foreign company if it is a foreign legal person that is tax resident within the EU and is listed on the annex to the Directive and is tax liable to the taxes in Article 3 without any option or exception. The legislation enacting the Directive only covers the companies directly involved and does not refer to the parent companies.	

If so, would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single (foreign) Member State or a from a third (non-EU) state or states? If not, would you apply the benefits of the Merger Directive under domestic law if the merging companies were from a single (foreign) Member State or from a third state or states?	Reference
1.2 Foreign Member State and third state merger According to Swedish tax law the benefits of the Directive should apply even if a merging company is not resident within the EU if the company qualifies as a *foreign company*. The definition of a foreign company is a foreign legal entity whose taxation is similar to a Swedish limited liability company (*'Sw AB'*). A company is always considered to be a foreign company if the company is resident in a treaty country and is liable to income tax.	37:9 and 2:5a ITA

Article 2 – Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 The term 'securities' In the Swedish legislation, the term has been interpreted as 'shares' and the term shares is defined in the Company Law Act as a share in a company's share capital.	Company Law Act 1:6

Has the possibility to allow a 10% cash payment for reorganization at book value (merger, division/partial division, exchange of shares) been implemented in your national law and if so whether it applies on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 The term 'cash payments' There is no 10% limitation in the Swedish legislation – cash payments may be unlimited.	37:13, 40 a:2 and 49:2 ITA

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Further types of merger No further types of merger are covered by the national implementing legislation.	

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
2.4 Qualifying exchange of shares Under the Swedish legislation, the acquiring company should hold more than 50 percent of the shares in the acquired company at the end of the transaction year. This means that if the acquiring company sells shares in the acquired company during the transfer year and does not hold 50 percent of the shares at the end of the year (although it has held 50 percent or more during the year), the company is not benefiting from the Directive. However, if particular reasons are at hand the transaction could qualify as an exchange of shares. According to the preparatory works to the tax rules, 'particular reasons' can be at hand in case a foreign acquiring company does not manage to acquire all shares of a Swedish company but more than 90 % of the shares and votes. For a compulsory redemption of the remaining shares the foreign company must transfer its shares to a Swedish subsidiary. According to the preparatory works this situation could take place the same year the exchange of shares take place.	48 a:8, 49:12 ITA

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>2.5 Consolidation of qualifying holding</u> The grant of relief is not subject to any conditions.	

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>2.6 The term 'branch of activity'</u> The definition of the term branch of activity has been implemented in 2:24 ITA and differs from the Directive in some cases. According to the Swedish law, the branch of activity should be 'a part of a business activity that is suited to be separated to an independent business'. The term business is defined as other business activity than holding of cash, securities and similar assets. There is no requirement in Swedish tax law that *all* assets and liabilities of a division of a company should constitute a branch of activity. According to the preparatory works to the tax rules, owning and managing of a single real estate could qualify as 'branch of activity'. No guidelines from the tax authority have been published.	2:24 and 2:25 ITA

Article 3 – Companies

Does your national legislation apply the Merger Directive to more types of entities than those listed in the Annex?	Reference
<u>3.1 Types of entities</u> See above under 1.1.	2:5a ITA

Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
<u>3.2 Transparent entities</u> In the preparatory work to the Swedish legislation enacting the amended Directive the Finance Department has commented on whether there are any entities that should be considered to be transparent from a Swedish perspective. However, the Department concluded that is was neither possible nor meaningful to investigate this question further. The solution was instead to interpret if the entity at hand is considered to be a legal person according to general provisions in the ITA.	SOU 2005:19

What is the tax residence criterion applied in domestic law? What is the most common tax residence tiebreaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Qualification of tax residency Under Swedish law a limited liability company is tax resident in Sweden due to its incorporation in Sweden. A foreign company can be limited liable to tax in Sweden if the company has a permanent establishment or a property in Sweden. The most common tie breaker rule in Double Tax Conventions is that a company's tax residence is determined by where the central management and control is situated.	Chaper 6 ITA

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject-to-tax clause Yes, the Article is listed in the annex to the ITA.	Annex 37.1 ITA

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
3.5 Shareholder requirements There are no shareholders requirements in the Swedish legislation.	

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
4.1 The concepts of 'real values' and 'value for tax purposes' The term real value has not directly been defined. Under Swedish GAAP real value is equal to 'fair market value'. The term is not used in the legislation enacting the Directive. As regards 'value for tax purposes' the following applies in the legislation enacting the Directive: If the assets are capital assets such as shares, the value for tax purposes is	2:31-33 ITA

the acquisition price for the shares plus contributions. For other assets than capital assets the value of tax purposes is the acquisition price minus depreciations.	

Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific guidance for divisions/partial divisions No guidance has been issued.	Chapter 37 and 38 a ITA

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 The concepts of 'effectively connected' and 'permanent establishment' There is no specific definition of 'effectively connected' in the Swedish legislation. The definition of permanent establishment under Swedish domestic law corresponds in principle with the definition under the OECD Model Tax Convention. Therefore the commentaries to the OECD Model Tax Convention may serve as guidance when interpreting domestic law.	37:30 and 2:29 ITA

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of the scope of relief The assets are considered to be transferred at book value, not fair market value and the assets can be depreciated on the book value and not the fair market value.	37:14

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with a permanent establishment No notional tax credit is allowed if the assets and liabilities are not effectively connected with a permanent establishment in Sweden. Taxation could be triggered in Sweden when the transfer of assets and	37:30

liabilities take place.	

Is a merger (under the condition of Article 7 Merger Directive) profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Tax treatment of shares of the receiving company The receiving company assuming the transferring company's tax position.	

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Tax deferral No specific amendments due to the ECJ case.	

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Criteria to determine tax transparent entities The definition of a *transparent entity* is given in Chapter 6 ITA where a foreign legal person is defined. If the requirements given in the section are not fulfilled the entity is considered to be transparent for tax purposes. The requirements are as follows: (a) the entity can acquire rights and liabilities; (b) the entity has the right to plead before a court; (c) the owners of the entity do not have the right to dispose over the entity's assets and liabilities. The definition of a *foreign company* is a foreign legal entity which taxation is similarly to a Swedish limited liability company ('Sw AB'). A company is always considered to be a foreign company if the company is resident in a treaty country and is liable to income tax.	6:8 and 2:5a ITA

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Further conditions for tax relief The transferring company shall immediately before the transaction be liable to tax in Sweden for at least a part of the transferred business or line of business. The income shall not be tax exempt under a double tax convention. The acquiring company shall immediately after the transaction be liable to tax in Sweden for at least a part of the transferred business that the transferring company was liable to tax for. The income shall not be tax exempt under a Double Tax Convention.	37:11-12 ITA 38:6-7 ITA 38 a:7-8 ITA

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
5.1 The term 'provisions and reserves' According to Swedish tax law, the provisions and reserves that are covered by the Directive are: (a) tax allocation reserve; (b) replacement reserve. However, there is no specific definition of the term 'provisions and reserves' in the Swedish tax legislation.	Chapter 30 and 31 ITA

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Exclusion of 'provisions and reserves' from permanent establishments The exclusion of provisions and reserves has not been implemented.	

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
<u>5.3 Allocation method for provisions and reserves</u> An allocation should be made which means that the value of the transferred provisions and reserves corresponds to the value for tax purposes of the transferred assets compared with the value of all assets in the transferring company at the time of the transaction.	37:28 and 38 a:15

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
<u>5.4 Further conditions for carry-over of provisions and reserves</u> No specific conditions are required, however, the acquiring company has to request to have the reserves transferred. The transfer does not occur automatically.	38:15

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
<u>6.1 The concept of carry-over of losses</u> The term loss has not been specifically defined in the legislation enacting the Directive. Under general Swedish tax provisions tax loss carry forward can be set off against group contribution if certain requirements are met. However, if the company making the loss is subject to a change of ownership restrictions regarding the possibility to utilize the losses might be triggered. Restrictions can also be triggered in connection with a merger, division, transfer of assets, etc. The rules are rather complicated and technical but it can be mentioned that under certain conditions (for example, where the companies distribute a group contribution before the transaction) the restrictions should not be triggered. A group contribution is deductible for the giver and taxable for the receiver. Group contribution can be distributed if the following requirements are met: (a) The parent company holds more than 90% of the shares in the subsidiary; (b) the qualifying relationship shall have existed during the whole fiscal year or since the subsidiary first started its business;	37:21 38:17a17b 38a a:18-19

(c) both the payer and the recipient shall report the contribution openly in their tax returns for the same assessment year; (d) the recipient must not be considered as a resident of a foreign state under a tax treaty, except when the recipient is a Swedish company that, under a double tax treaty, shall be deemed to be resident of a country within the EEA and is taxable in Sweden on the business from which the group contribution is deriving; (e) the business that the contribution is deriving from must not be exempt from Swedish taxation under a double tax treaty; (f) as regards contributions made by a subsidiary to a parent company, any dividends received by the parent company shall be tax exempt in the hands of the parent company. Group contributions can be given in order to set off losses. Tax losses may be carried forward indefinitely, but not carried back. There are no limits regarding the amount of losses that can be applied against group contributions. If a company with old tax losses is subject to a transfer of ownership or if a company with old losses acquires another company, restrictions could be triggered under two different rules which limit the right to use the losses after the transfer. (a) Losses exceeding 200 % of the amount paid for the acquired company may not be carried forward any more (Permanent restriction). (b) If a company with old losses obtains the decisive control of another company the old losses may not be set off against group contributions (see 3.2.2) from the acquired company during the acquisition year and the five years following the acquisition (Temporary restriction).	

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of losses to the permanent establishment The losses attributed to a permanent establishment are those derived from its activity. No special method exists to allocate losses.	

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Specific legislation for divisions/partial divisions/transfer of assets See above 6.1.	37:21 38:17a17b, 38a a:18-19

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
<u>6.4 Further conditions for carry over of losses</u> See above 6.1.	37:21 38:17a17b, 38a a:18-19

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
<u>7.1 Amended holding threshold</u> There is no such restriction.	

Article 7(1) covers <u>gains</u> accruing on the cancellation of a holding. It does not cover <u>losses</u> that may be realized on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
<u>7.2 Treatment of losses</u> The latter situation has not been dealt with in the Swedish tax legislation.	

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
<u>8.1 Avoidance of economic double taxation at the level of the shareholder</u> If the shareholder is an individual the received shares should be considered to be acquired for the value for tax purposes (see definition above). If the shareholder is a company the taxable gain is computed at the time of the transaction but the actual taxation will occur at the time the shares are sold. This method implies a kind of 'deferred taxation'.	Chapter 48 a and 49

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
8.2 Computation of the capital gain Cash payments should be taxed the year in which the transaction takes place.	48 a :9 ITA

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
8.3 Further conditions for tax relief If the seller is an individual he or she should be tax resident in Sweden (please also see above in 2.4).	48 a:5

Article 9 – Transfer of assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the 'real' or 'market' value of the assets transferred?	Reference
9.1 Avoidance of economic double taxation at the level of the transferring company The payment for the transfer should not be taxed in the hands of the transferring company. Other assets than capital assets should be considered to be disposed of at the value for tax purposes. Capital gains and losses should not be taxed/deducted. The received shares in the hands of the transferring company should be considered to be acquired for the net value of the transferred business or line of business.	Chapter 38 ITA

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
9.2 Further conditions for tax relief The rules are applicable at the company request which means that the rules do not apply automatically. However, this is not an application but a request that the rules should be applicable. See above regarding the tax liability requirement in Sweden.	Chapter 38 ITA

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
9.3 Tax deferral No specific amendments have been made after the ECJ case.	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
10.1 Loss recapture for permanent establishments in third Member States There is no legislation regarding loss recapture in the Sweden.	

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
10.2 Permanent establishment in the Member State of the receiving company A notional credit can be allowed if the following requirements are met: (a) the assets, liabilities and other obligations are transferred by a re-organization that should have been a merger or a division if the transferring company had been a foreign legal entity (see definition above); (b) the transferring company is a foreign entity that is tax resident within the EU;	37:30

(c) the acquired company carries on business in any of the legal forms as stated in Annex 37.1; and (d) the acquired company is liable to tax as stated in Annex 37.2. The notional credit implies that the company is allowed to credit an amount corresponding to the tax that should have been paid in the foreign country if the Directive was not implemented.	

Does your national legislation provide for the taxation of unrealized capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
10.3 Concept of worldwide taxation/tax credit system? No.	

Please also describe how account has been taken of ECJ case law, and in particular of the 'N' judgment, in the legislation implementing Article 10(2).	Reference
10.4 Tax deferral No amendments have been done due to the ECJ case.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
10a.1 Option right for the application of the Merger Directive to deemed fiscally transparent transferring or acquired companies Sweden has not implemented Article 10a.1 of the Merger Directive. The reason for this is, according to the preparatory work, that it should be rather unusual that entities covered by this Article should be part of a transaction covered by the Directive. According to the Finance department in case an entity does not qualify as a legal person under Swedish law, it is not suitable that this entity should benefit from the Directive. Taxation should instead follow the general rules.	SOU 2005:19

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Tax base for notional tax credit No definition in the Swedish tax legislation.	37:30

How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Determination of notional tax credit If the following requirements are met a notional tax credit should apply: (a) the assets, liabilities and other obligations are transferred by a re-organization that should have been a merger or a division if the transferring company had been a foreign legal entity (see definition above); (b) the transferring company is a foreign entity that is tax resident within the EU; (c) the acquired company carries on business in any of the legal forms as stated in Annex 37.1; and (d) the acquired company is liable to tax as stated in Annex 37.2. The notional credit implies that the company is allowed to credit an amount corresponding to the tax that should have been paid in the foreign country if the Directive was not implemented. It is not expressly stated in the tax legislation if notional tax credit system is applicable for the shareholders of a transparent company.	37:30a

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Option right for the application of the Merger Directive to deemed fiscally transparent acquiring/receiving companies and their shareholders Sweden has not implemented Article 10a of the Merger Directive.	

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What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
<u>10a.5 Comparison with a resident fiscally transparent company</u> The company is compared to a non-transparent company for tax purposes.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when a SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of the registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
<u>10b.1 Exit taxation</u> There is no specific implementation of the Article According to the preparatory works, the Swedish tax legislation already covers this situation and does not require implementation. The main rule in Sweden is that an exit tax should occur in case the head office is transferred to another country (this can be the case when the management is considered to be in another country due to a tax treaty). However, according to the '*Finance department*' no exit taxation should occur in case a SE transfer its head office to another Member State under the condition that the SE carries on business in Sweden through a permanent establishment here. The income from the permanent should be taxed in Sweden and no exit taxation is levied. The Swedish Supreme Administrative Court on 24 April 2008 (case 6639-06) rendered a verdict regarding exit taxation and the taxation of tax allocation reserves when a Swedish company changes its country of tax residence. The Court reached a verdict that the exit taxation of assets, as well as the rule on reversal of profit allocation reserves, hindered the company's exercise of freedom of establishment under Article 43 of the EC treaty. This would imply that if the SE transfers all its business i.e. no permanent establishment in Sweden, no exit taxation should be triggered on the transfer of head office.	SOU 2005:19

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
<u>**10b.2 The term 'head office'**</u> No definition exists in the Swedish legislation.	

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tiebreaker clauses of DTCs concluded by the Member State in question?	Reference
<u>**10b.3 Head office and tax residency**</u> See above under 10b.2.	

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
<u>**10b.4 Assets and liabilities not effectively connected with a permanent establishment**</u> An exit taxation could be triggered (please see 4.5).	Chapter 22 ITA

What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the '*N*' case?	Reference
<u>**10b.5 Tax deferral**</u> No amendments have been made due to the ECJ case.	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 The term 'comparable circumstances' The term has not been defined.	

Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Loss recapture for permanent establishments Sweden has not implemented rules regarding loss recapture for permanent establishments.	

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE/SCE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
10d.1 Deemed liquidation The rule is not applicable.	

What applies in respect of shareholders that are third (non-EU) country residents?	Reference
10d.2 Tax treatment of third country residents The rule is not applicable.	

Article 11 – Anti-abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Transposition of anti-abuse provisions</u> The Article has not been transposed into Swedish tax law, however, see below regarding the Swedish Tax Avoidance Act.	

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
<u>11.2 General anti-abuse provision</u> Under the Swedish anti-avoidance legislation a transaction may be adjusted for tax purposes if *all* of the following conditions are met (Tax Avoidance Act): (a) The transaction, alone or together with other transactions, is part of a procedure that provides a substantial tax advantage to the tax payer. (b) The taxpayer, directly or indirectly, has participated in the transactions. (c) The tax advantage, considering all circumstances, can be considered as the predominant reason for the procedure. (d) A tax assessment based on the procedure would be in conflict with the purpose of the tax legislation, as it can be concluded from the general design of the tax rules, and those rules that are directly applicable or have been circumvented through the procedure. (The current legislation came into force on January 1, 2008.) In case law a substance over form method has developed which entails that the tax court can perform a re-characterization of a transaction.	Swedish Anti Avoidance Act (1995:575).

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 The concept of 'wholly artificial arrangement' See above section 11.2.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Specific anti-abuse provisions No specific anti-abuse provisions exist.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalization' been interpreted in your national legislation?	Reference
11.5 The concept of 'valid commercial reasons' See above 11.2.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
11.6 Burden of proof The burden of proof lies with the Tax Agency	

UNITED KINGDOM

Abbreviations

English	English
FA 1986	Finance Act 1986
ICTA 1988	Income and Corporation Taxes Act 1988
TCGA 1992	Taxation of Chargeable Gains Act 1992
FA 1996	Finance Act 1996
CAA 2001	Capital Allowances Act 2001
FA 2002	Finance Act 2002
FA 2003	Finance Act 2003
CA 2006	Companies Act 2006
FA 2007	Finance Act 2007
IHT	International Taxes Handbook (part of Inspectors Manuals)
HMRC	Her Majesty's Revenue & Customs
ECJ	European Court of Justice

Introduction

Please describe the overall state of implementation of the original 1990 Directive and of all amendments to the Directive with an implementation deadline of 1 January 2007 or earlier, together with dates upon which the relevant law became effective. Please also describe, in general terms, any administrative guidance that may have been issued.

State of Implementation of the Legislation

The original 1990 Mergers Directive (referred to from hereon as the 'Directive', a term that will be applied to both the original legislation and the amended legislation as appropriate) was implemented through new provisions included in Finance Act (No 2) 1992 which took effect from 1 January 1992. The scope of these rules was limited to:

(a) the transfer of a UK trade, or part trade, between companies resident in two different Member States; and

(b) the transfer of a non-UK trade from a UK company to a company resident in another Member State.

The rationale for limiting the implementation to these two situations was that Her Majesty's Revenue and Customs (HMRC) did not consider that mergers, divisions and partial divisions were possible under UK Company Law as it existed at the time.

Furthermore, specific legislation was not brought in to account for share for share exchanges on the basis that the UK already had legislation in place that governed the taxation of share for share exchanges and that this legislation was already compliant with the Directive.

In response, to Regulation 2157/01 that introduced the Societas Europea (SE), the UK introduced legislation in Finance Act (No 2) 2005 which amended the legislation that originally implemented the Directive to take into account the existence of the new legal entity.

Legislation was incorporated at FA 2007 s110 to give the Treasury power to introduce regulations to fully implement the Directive, as amended by Directive 2005/19/EC of 17 February 2005 at some future point without the need to formally enact further legislation. These regulations were implemented via a Statutory Instrument SI2007/3186 with effect from 29 November 2007. This Statutory Instrument implemented the remaining elements of the Directive that had not been previously been enacted given the changes in UK Companies Act legislation that now specifically allow all of the types of transaction that are envisaged within the Directive. As a result, HMRC now believe that UK tax law is compliant with the Directive.

Method of Implementation

UK Tax law is made up if a number of different statutory acts and instruments which, when taken together, make up the rules that describe the UK tax system. However, the rules that impact corporate taxation are scattered among these acts and are not consolidated into a single legislative code.

Specific Areas of UK Tax Law

The specific areas of UK tax legislation that implement the Directive are contained in the following areas:

Taxation of Capital Gains Act 1992 ('TCGA 1992'):

(a) Share for share exchanges – Sections 135-138;

(b) Capital Gains arising on divisions, partial divisions and mergers – Sections 140A-140L.

Finance Act 1992 ('FA 1992'):

(a) Taxation of Loan Relationships (special computational provisions) – Schedule 9 paragraphs 12B-12J.

Capital Allowances Act 2001 ('CAA 2001'):

(a) Transfer of assets qualifying for capital allowances between legal entities on the transfer of a UK trade – Section 561.

(b) Transfer of assets qualifying for capital allowances between legal entities on the formation of an SE by merger – Section 561A.

Finance Act 2002 ('FA 2002'):

(a) Taxation of Derivative Contracts – Schedule 26 paragraphs 30B-30I;

(b) Taxation of Intangible Assets – Schedule 29 paragraphs 85-88.

As a result, the rules implementing the Mergers Directive are not included as a single body of legislation. Instead, they are scattered through the legislation in the same places where the rules describing the taxation of the assets impacted by the Mergers Directive are located, and this, as the survey demonstrates, has resulted in technical inconsistencies between the treatment of certain assets within a transaction covered by the Directive.

Definition of 'Member State'

There is no specific definition of the term 'Member State' in UK legislation. Therefore, the term 'Member State' should take its ordinary meaning i.e. being a Member State of the European Community.

HMRC Guidance

HMRC Issue guidance to taxpayers through a number of sources.

(a) Inland Revenue Manuals – these provide practical guidance to HMRC Officers who administer the tax law on a day to day basis and set out HMRC view on how the law applies to specific areas. These manuals are made available to the public through the HMRC website.

(b) Tax Bulletins – these are issued every two to three months and provide the HMRC view on specific technical topics and are written by leading specialists within the organization.

(c) Press releases – these are issued on an ad hoc basis when points of note arise and require comment on by HMRC.

(d) Technical Notes that accompany the publication of draft or final legislation.

HMRC Manuals

Given the newness of the updated legislation, the published guidance is limited to the enacted legislation that was in place before the update in November 2007. The main focus of the guidance within the Manuals has been to cover the treatment of capital gains on share for share exchanges and [divisions]. Virtually no guidance has been given in respect of the knock on impact of these transactions on loan relationships, assets qualifying for capital allowances, derivative contracts or intangible assets.

In terms of providing practical guidance to taxpayers on specific scenarios that may come up, there is little guidance. One possible reason for this is that, to date, there has been relatively little in the way of merger activity in the UK. This might be partly explained by the fact that there was a general consensus held by many bodies, including HMRC, that mergers were not permitted under UK Company Law.

Technical Notes

In November 2006 HMRC issued a detailed technical note as part of the consultation process for the issue of new legislation to take into account of the amendment to the Directive. In this document, a detailed explanation was given for each new section of proposed legislation referring back to the Directive and how the proposed legislation implemented it.

In this technical note HMRC specifically commented that an extremely small number of companies in the UK have sought to take advantage of the Directive and that other transactions that attempt to achieve some of the same aims as a merger (e.g., share for share exchanges) have proved far more popular.

When the new legislation was eventually issued in November 2007, HMRC published a short explanatory memorandum indicating how certain areas of the Directive had been incorporated into UK tax law.

Status of Gibraltar

Gibraltar is understood to be part of the United Kingdom for the purposes of the EC Treaty and hence, is would be understood to be part of the United Kingdom for the purposes of the Directive. However, for the purposes of this review, we have only considered how the directive is applied in Great Britain and Northern Ireland.

Article 1 - Scope

Please describe how the expression 'in which companies from two or more Member States are involved' has been interpreted and implemented. Has the term 'companies involved' been interpreted as encompassing not only the merging companies but also any parent companies.	Reference
1.1 Involved Companies 1.1.1 Definition of Company The definition of 'company' is inconsistent between the various areas of legislation that implement the Directive. (a) Mergers, Divisions and Partial Divisions In general, the legislation enacting the Directive in the above areas has defined the terms 'company' as being an entity that is listed on the annex to the Directive. Therefore it is reasonable to assume that the relief given under UK law in respect of mergers, divisions and partial divisions is	TCGA 1992 s140A, 140C, 140E, 140F, 140G FA 1996 Sch 9 para. 12B, 12C, 12D, 12E, CAA 2001 s561, 561A FA 2002 Sch 26 para. 30B, 30C, 30D, 30E FA 2002 Sch 29

limited to those types of entity. There is an exception to this within the legislation covering the transfer of intangible assets under one of the above operations. In this legislation, no specific definition of a 'company' has been given. Therefore, it is reasonable to conclude that the term 'company' takes on its normal meaning as applied in the rest of tax legislation, being 'any body corporate or unincorporated association, but does not include a partnership, local authority or a local authority association'. This definition potentially covers more entities than are included within the Annex and thus, although is inconsistent with other enacting legislation, is compliant with the Directive. (b) Share for share exchanges The definition of 'company' for share for share exchanges is not defined and hence, as for the example with respect to intangible assets above, the general definition of a company as described above should be used. In addition, specialist entities such as Industrial Provident Societies are also included. As discussed, this would appear to be compliant with the Directive as it goes beyond the minimum relief that must be given. <u>1.1.2 Two or more Member States are involved</u> (a) Mergers The implementing legislation in respect of mergers refers to two circumstances that must be in place for the transaction to qualify for the relief given in the enacting legislation: Each of the companies involved must be resident in a Member State; and Not all of the companies can be resident in the same Member State. What is meant by 'resident' is considered elsewhere. However, under UK legislation: In the case of a merger between two or more companies all from the same Member State relief is not available. This appears consistent with the Directive. In the case of a merger between two or more companies all resident in Member States but not all resident in the same Member State relief is available. This also appears consistent with the Directive. In the case of a merger between three or more companies, at least two of which are resident in Member States, albeit different ones, and one not resident in a Member State relief is not available. This appears inconsistent with the Directive. (b) Divisions and Partial Divisions The requirements regarding the location of companies involved in a partial division are that: The transferring company is located in one Member State; and	para. 85, 85A, 87, 87A

At least one of the receiving companies is located in a Member State other than the one in which the transferring company is located. This area of legislation appears to be less restrictive than that applying to mergers and also appears to be consistent with the Directive. (c) Share for Share exchanges There is no territorial restriction within this area of legislation that would block the application of the relevant relief. This is goes beyond the minimum requirements of the Directive and hence appears to be in compliance. <u>1.1.3 Companies Involved</u> The legislation enacting the Directive only covers the companies directly involved in the merger, division, partial division or share for share exchange, and does not refer to the shareholders or parent companies.	

If the expression 'companies involved' has been interpreted as encompassing both merging companies and parent companies, then would the fact that the parent companies were from two different Member States suffice to bring the merger within the scope of the national implementing legislation, even if the merging companies were from a single Member State or a from a third (non-EU) state or states?	Reference
<u>1.2 Application of term 'companies involved' to Parent Companies</u> UK legislation enacting the Merger Directive does not interpret 'companies involved' as including parent companies.	N/A.

Is relief available to resident shareholders in the event that the exchange of shares, merger, division, partial division or transfer of assets occurs between companies located in Member States other than your own?	Reference
<u>1.3 Impact on resident shareholders of transactions taking place entirely in other Member States</u> <u>1.3.1. Exchanges of Shares</u> This is a relief that is granted to shareholders on a specific corporate transaction that does not rely on the residence of the companies involved in the exchange. Therefore, in this situation, relief should be available to UK shareholders in the event that the companies involved are all outside of the UK.	TCGA 1992 s136, TCGA 1992 Sch 5AA.

1.3.2 Divisions, Partial Divisions and Transfers of Assets The relief granted to shareholders specifically covers two situations: (a) a company located in a Member State transferring a business located in the UK to another company located in another Member State wholly in exchange for an issue of shares or debentures to the shareholders of the transferring company; and (b) a company located in the UK transferring a business located outside of the UK to another company located in another Member State wholly or partly in exchange for an issue of shares or debentures to the shareholders of the transferring company. The rules therefore would not cover a situation where a company located in a Member State transfers a business located outside of the UK to a company located in another Member State which is not the UK. Therefore, unless the standard rules relating to shareholder relief under the rules covering either a share for share exchange or a corporate reorganisation apply, no shareholder relief would be due. This may be incompliant with the Directive since the UK legislation imposes conditions that may be more onerous than the Directive although whether this is a practical issue remains to be seen. 1.3.3 Mergers The rules regarding mergers, as above, cover the situations where: (a) two or more companies, all resident in Member States, at least one of which has assets used in a permanent establishment in the UK, merge into a single entity in exchange for shares and debentures issued to the shareholders of the transferring companies; and (b) a company resident in the UK with assets located outside of the UK merges with one or more companies all located in Member States, albeit not the same Member State in exchange for shares and debentures issued to the shareholders of the transferring companies. Again, the situation where two non-UK entities located in Member States without any assets located in the UK merge is not covered and, therefore, again, unless the standard rules covering shareholder relief in the case of a share for share exchange or a corporate reorganisation apply, no shareholder relief would be due. This may be incompliant with the Directive since the UK legislation imposes conditions that may be more onerous than the Directive although whether this is a practical issue remains to be seen. 1.3.4 Implications In the absence of the relief accorded under the legislation implementing the Directive, there exists relief in the case of a transaction which is deemed to be a 'scheme of reconstruction'.	

For a scheme to qualify the following conditions must be in place: (a) the receiving company must issue ordinary share capital to the shareholders of the transferring company in proportion to their shareholding in the transferring company; (b) the business of the transferring company must be continued by the receiving company; and (c) no part of the business is transferred to any other person other than the receiving company. In this instance, in the event that the original shares held by the shareholders of the transferring company are cancelled, the new shares received are deemed to inherit the tax attributes of the original shares. The transaction is ignored for tax purposes and hence no tax arises. This gives the relief required. The situation where relief would not be granted would be where shares, other than ordinary shares were issued, or that the shares issued were not in proportion to the original shareholdings. It is unclear whether this means that, in the event of a merger where a minority shareholder received cash rather than shares (with the cash being less than 10% of the nominal value of the shares being issued) this would make the transaction fall outside of the scope of the relief. If it were the case that such a payment would invalidate the relief, then the liquidation may create a tax charge on the shareholders which would be incompliant with the Directive. This is described in more detail in 2.2 below.	

Article 2 - Operations

The definitions provided by Article 2 (a)-(d) contain a reference to an exchange of 'securities'. How has the latter term been defined or interpreted in implementing legislation and/or administrative guidelines?	Reference
2.1 Definition of Securities 2.1.1 'Securities' (a) Tax legislation The term 'securities' as used in the Directive has been transcribed into all areas of UK tax legislation covering, mergers, divisions, partial divisions and asset transfers as 'shares or debentures'. In interpreting the meaning of these terms, tax legislation refers the reader to the relevant areas of company law for definition. (b) Company Law - shares Shares are defined in company Law as a 'share in a company's share capital'. No further guidance is offered as to the meaning of this term.	CA 2006 s540(1), CA 2006 s738, Levy v Abercorris Slate and Slab Company ((1887) 37 Ch D. 260)

(c) Company Law - Debentures Debentures are defined as including 'debenture stock, bonds, and any other security of a company'. Although, again, HMRC offers no further guidance on the subject, there is guidance from UK Case law where a Debenture was taken to mean a document '… which either creates a debt or acknowledges it…' The transcription of these terms into UK law appears to be in compliance with the Directive.	

Has the 10% cap on cash payments been interpreted and implemented as applying on a per shareholder basis or on an overall basis (i.e. as allowing a cash buy-out of minority shareholders)?	Reference
2.2 Cash Payments 2.2.1 Mergers Under UK legislation, in order for a merger to qualify for the relief outlined in the legislation implementing the Directive, the merger must be carried out by way of a transfer of assets and liabilities to the company into which they are to be merged in exchange for an issue of shares or debentures by the receiving company to the shareholders of the transferring company. UK legislation does not consider the situation where cash is offered as part of the consideration and thus, in the absence of any non-statutory relief granted by HMRC any merger where an element of the consideration was paid in cash would not qualify for the relief and this may be incompliant with the Directive. Given the newness of the legislation, there is no guidance from HMRC on this point and no precedent on how this situation would be treated in practice. In this situation, a tax payer could refer back to the Directive to determine what relief they should be due. However, from the wording in the Directive, there are different possible interpretations of what the 10% cash element actually refers to as it could be interpreted to mean that: (a) a cash payment is permitted to ensure that the receiving company does not have to issue fractions of shares in order to ensure that shareholders in the transferring company receive consideration in proportion to their shareholdings; (b) a cash payment is permitted to enable minority shareholders in the transferring company to be removed under the transaction; or (c) shareholders in the transferring company may be permitted to realize value from their shareholdings provided this realization is minimal compared with the overall transaction.	TCGA 1992 s140E, 140F, 140G FA 1996 Sch 9 para. 12B, 12C, 12D, 12E, CAA 2001 s561A FA 2002 Sch 26 para. 30B, 30C FA 2002 Sch 29 para. 85A, 87A TCGA 1992 s135 Inland Revenue Inspectors Manuals – Capital Gains Manual 52587, 52592, 57835

2.2.2 Asset transfers, Divisions, Partial Divisions (a) Assets left within UK charge to tax through a permanent establishment post transaction In this instance, in order for the relief under the implementing legislation to be available, the transfer must be carried out, wholly in exchange for the issue by the receiving company of shares or debentures to the transferring company. As above, this seems to specifically preclude any transaction which includes the payment of a cash sum to the shareholders of the transferring company from qualifying to the relief permitted under the Directive and, therefore, may be incompliant. (b) Assets leaving UK charge Where, after the transaction, there is no UK presence because no overseas company runs a UK trade through a permanent establishment and no UK company ends up owning assets, then the transaction can be 'wholly or partly' in exchange for the relevant relief to apply. This would appear to be compliant with the Directive. 2.2.3 Share Exchanges In order to qualify for the relief under the legislation covering share for share exchanges, the transaction must consist of a paper for paper transaction. Any amounts received for cash are not specifically covered in this legislation and hence this area of the legislation may not be compliant with the wording of the Directive. However, HMRC guidance states that, in the event that consideration is made up of shares or debentures, and cash, that the cash element is treated as a capital distribution in respect of the shares in the hands of the shareholder of the . In other words, the transaction is split into two elements: a share for share element that, provided it qualifies for relief as a share for share exchange in its own right, is covered by the legislation; and a cash sale which is subject to UK corporation tax in the normal way. The base cost of the share upon which any such gain would be calculated is allocated between the two transactions on a just and reasonable basis. It would appear that while HMRC practice is compliant with the Directive the wording of the legislation is unclear or incompliant.	

Article 2(a) lists three types of merger. Does the national implementing legislation cover other or further types of merger?	Reference
2.3 Other Types of Merger No other forms of merger are contemplated.	N/A.

The definition of exchange of shares contained in Article 2(d), as amended by Directive 2005/19/EC, covers not only an exchange of shares leading to the obtaining of a majority of the voting rights, but also any further exchange that may consolidate that majority. In the case of a gradual increase in the stake in the target company, does the national implementing legislation grant relief in respect of each successive exchange of shares that contributes to the build-up of a stake in the target, or only in respect of the exchange that finally leads to the acquisition of a majority holding?	Reference
<u>**2.4 Build up of shareholdings in Share for Share Exchanges**</u> Relief is granted for any share for share exchange where, after the transaction, the receiving company owns either more than 25% of the ordinary share capital or the majority of the voting power. This means that, for any transaction that does not achieve either of these conditions, no relief is due and the exchange is subject to tax in the normal way. However, for any transaction where either of these criteria are achieved, relief is given on that transaction in full. Any subsequent share for share exchanges would qualify for relief, provided that, after the transaction, the receiving company still held either more than 25% of the ordinary share capital or the majority of the voting power. This would appear to be compliant with the Directive.	TGCA 1992 s135(2)

With regard to an exchange of shares that consolidates an existing majority holding, is the grant of relief subject to any conditions?	Reference
<u>**2.5 Consolidations of existing holdings**</u> The relief is subject to the transaction being carried out for bona fide commercial purposes and not part of a scheme or arrangements where the main purpose, or one of the main purposes, is the avoidance of tax.	TCGA 1992 s137

'Branch of activity' is defined in Article 2(i) and has been further clarified by Case C-43/00 '*Andersen og Jensen*'. Please describe how this concept has been implemented in national law and any administrative guidance that may have been issued.	Reference
<u>**2.6 Branch of Activity**</u> The UK legislation implementing the Directive was amended in November 2007. Before the amendments the UK legislation required that a company transfer a trade or part of a trade carried on by it. Arguably this may have been too restrictive as companies may have wished to transfer activity that did not amount to a trade but was a business e.g. investment activity. The amendment has broadened the relief by changing the requirement to	ICTA 1988 s 834 (1); Inland Revenue Manuals ITH 842-850 FA 2003 s148

transfer a business or part of business rather than a trade. We regard this to be complaint with the Directive.	

Article 3 - Companies

Does your national legislation apply the Directive to more types of entities than those listed in the Annex?	Reference
3.1 Companies to which the Directive applies See the analysis at question 1.1.	TCGA 1992 s140H, 140L ICTA 1988 s832(1)

3.2 Does your national legislation regard any of the entities listed in the Annex as being transparent and, if so, on what grounds?	Reference
3.2 Transparent Entities The definition of what is a transparent entity varies depending upon which area of legislation that is being considered. 3.2.1 TCGA 1992 – s135-139 (Share for share exchanges) In this area, the term 'transparent entity' is not defined and there is no general legislative guidance. As far as administrative guidance is concerned HMRC have issued a list of factors that they consider when responding to such rulings as follows: (a) Does the foreign entity have a legal existence separate from that of the persons who have an interest in it? (b) Does the entity issue share capital or something else, which serves the same function as share capital? (c) Is the business carried on by the entity itself or jointly by the persons who have an interest in it that is separate and distinct from the entity? (d) Are the persons who have an interest in the entity entitled to share in its profits as they arise; or does the amount of profits to which they are entitled depend on a decision of the entity or its members, after the period in which the profits have arisen, to make a distribution of its profits. (e) Who is responsible for debts incurred as a result of the carrying on of the business: the entity or the persons who have an interest in it? (f) Do the assets used for carrying on the business belong beneficially to the entity or to the persons who have an interest in it?	TCGA 1992 s140L, CA 2006 1(1), HMRC Tax Bulletin 83. Inland Revenue Manual: Double Taxation Relief 180010.

These tests are not cumulative but have to be weighed together based on the particular facts of a case. Furthermore, HMRC have issued a list of entities upon which they have been asked to provide a ruling as to whether they would treat that entity as transparent or opaque. From the list in the Annex, the following entities were considered transparent:

Société en nom collectif (Belgium), Coöperatie (Netherlands).

3.2.2 TCGA 1992 – s140A-140L (Treatment of capital gains on a merger, division or partial division)

In this area of legislation a transparent entity is one:

(a) listed on the Annex to the Mergers Directive;

(b) which is resident in a state other than the United Kingdom;

(c) does not have ordinary share capital, and

(d) were it resident in the UK, would not be capable of being a company under UK Company Law (please see 1.1).

HMRC has not issued guidance on whether this definition would exclude any of the entities listed in the Annex to the Directive.

3.2.3 FA 1992 – Sch 9 paragraphs 12B-12J (Treatment of gains and losses on loan relationships on a merger, division or partial division)

Here, a transparent entity is one:

(a) resident in a state in a Member State other than the United Kingdom; and

(b) does not have a share capital.

It has not yet been determined whether this definition would exclude any of the entities listed in the Annex to the Directive.

3.2.4 CAA 2001 s561-561A (Treatment of capital allowances on a transfer of assets or Merger to form an SE)

Here there is no definition of a transparent entity and hence, to the extent that one became necessary, the general principles as stated above would be used.

3.2.5 FA 2002 Sch 26 paragraphs 30B-30I (Treatment of gains or losses on derivative contracts on a merger, division or partial division)

Here the same definition of a transparent entity is used as in FA 1992 Schedule 9.

3.2.6 FA 2002 Sch 29 paragraphs 85-88 (Treatment of gains or losses on intangible assets on a merger, division or partial division) Here the same definition of a transparent entity is used as in FA 1992 Schedule 9. It is conceivable that certain entities may be treated as transparent for certain parts of the legislation that enacts the Directive but not for others. However, it is too early to tell whether the inconsistencies referred to above will have a practical impact upon the operation of the Directive.	

What is the tax residence criterion applied in domestic law? What is the most common tax residence tie-breaker criterion in the double tax conventions concluded by your national tax authority?	Reference
3.3 Residence 3.3.1 UK Law Companies can be tax resident in the UK either (a) by incorporation in the UK or, (b) if they are incorporated outside the UK, if 'Central management and control' are located in the UK. Central management and control is a matter of judgment but takes into account a wide range of facts and circumstances. However, UK case law has established that the most important factor when determining where a company is managed and controlled is the answer to the question of where the meetings of directors who control the company take place. 3.3.2 Double Tax Treaties Where a company could be treated as being tax resident in both the UK and another country, then, where a double tax treaty is in place between the UK and that other tax authority, the most common tie breaker is to determine where central management and control is habitually operated.	FA 1986 s66(1), De Beers Consolidated Mines Ltd vs Howe.

How is the subject-to-tax clause of Article 3(c) implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
3.4 Subject to tax 3.4.1 TCGA 1992 s135-138 There is no specific requirement that, for a share for share exchange to qualify for the relief, either of the companies must be subject to tax.	TCGA 1992 s140L (2),

3.4.2 TCGA 1992 s140A-140L Under implementing legislation a company is 'subject to tax' if they are within a charge to tax under the law of the State in which they are resident and they are not regarded as being resident outside the EU for the purposes of any Double Taxation Agreement. It is a requirement that the companies involved in the transaction are subject to tax within a Member State in order for them to qualify for the relief. 3.4.3 FA 1996 Sch 9 The same requirements apply here as they do for TCGA 1992 s140A-140L. 3.4.4 CAA 2001 s561-561A A transaction does not qualify for relief unless TCGA 1992 140A or TCGA 1992 140E apply to the transaction. In order for this condition to be satisfied, it is necessary for the companies to be subject to tax according to the rules stated above. 3.4.5 FA 2002 Sch 26 paragraphs 30B-30I The same requirements apply here as they do for TCGA 1992 s140A-140L. 3.4.6 FA 2002 Sch 29 paragraphs 85-88 The same requirements apply here as they do for TCGA 1992 s140A-140L.	

Does your national legislation limit the benefits of the Directive to companies owned or controlled by EU or EEA nationals or residents and, if so, on what grounds?	Reference
3.5 Residence of shareholders The benefits of the Directive are not restricted in respect of the identity of the owner of the company.	N/A.

Article 4 – Carry over of balance sheet values

How have the Article 4(1) concepts of 'real values' and 'value for tax purposes' (the latter concept is defined in Article 4(1)(a)) been interpreted and transposed into your national legislation?	Reference
<u>4.1 'Real values' and 'Values for tax purposes'</u> <u>4.1.1 General points</u> Before responding to this point, it is interesting to note is that, in UK legislation, the term 'capital gains' has a specific meaning inasmuch as it refers specifically to the taxation of gains and losses on the disposal of certain assets. However, it has been assumed that, for the purposes of this review, the term 'Capital Gains' refers to tax on the transfer of all assets within a company or branch included as part of a merger, division, or partial division. It should also be noted that the UK authorities, in enacting the Directive, have taken advantage of the derogations in Articles 10(2) (permanent establishment in a third Member State) and Article 10a (transparent entities). Hence, the analysis below refers to mergers, divisions and partial divisions between opaque companies where there remains presence in the UK after the transaction through a permanent establishment continuing to be located there. <u>4.1.2 Real Values and Values for Tax purposes</u> Within each of the following sections, the concepts of 'real value' and 'value for tax purposes' have not been directly defined. Instead, the rules have sought to apply the Directive by defining the gain or loss that arises on such a transfer. It can be argued that by using this approach, the concepts of 'real value' and 'value for tax purposes' have been implicitly defined as, in the absence of the Directive, gains or losses would be calculated with reference to these terms. UK legislation does not specify how to calculate 'real values'. The concept applies to each individual transaction as being what a third party purchaser would buy the assets at if it were taking part in an arms length transaction under the same or similar circumstances to the one that actually took place. For example, in the case that a business is being transferred as a going concern, the comparative transaction would be a third party purchaser buying the assets of the business as a going concern with the deemed proceeds being allocated accordingly amongst the assets transferred. It should be noted that the United Kingdom has adopted the derogation from Article 4 as permitted in Article 10(2) in the case where either the United Kingdom loses the taxation rights of a permanent establishment located outside of the UK transferred to a non-UK company (except in the case of a transfer of assets where, after the transaction, the transferring company owns at least 25% of the share capital of the receiving company) and the transfer of assets by a transparent entity as permitted in Article	TCGA 1992 s56(2) TCGA 1992 s140A-140L FA 1996 Sch 9 paragraph 12B-12J

10a(1). <u>4.1.3 Capital assets</u> The relief required by the Directive has been provided by stating that the transfer of assets from transferring company to receiving company is deemed to take place at a value that would generate neither a gain nor a loss on transfer. The value of the deemed transfer is calculated, therefore, by adding together the cost of the relevant asset (the 'base cost') plus an allowance to reflect the time value of money that is provided for under general capital gains calculation principles (the 'indexation allowance'). It would appear that this is compliant with the Directive.	CAA 1992 s561-561A
<u>4.1.4 Loan relationships</u> The value at which a loan relationship is deemed to transfer under merger, division or partial division is the 'notional carrying value'. This is defined as being the amount that would have been the carrying value of the asset or liability in the accounts of the transferring company if a period of account had ended immediately before the date when the transfer took place. So, for example, a company may be party to a loan relationship reflected as a debtor in its balance sheet that is recognised in the accounts at fair value under normal accounting principles. At the start of the period, the fair value of the loan is 100. However, when the loan balance is transferred to another company as part of a merger it has a fair value of 110. Had a set of accounts been produced at the date of the merger, the loan would have been shown at 110 in the balance sheet of the transferring company. Therefore, the notional carrying value of that balance in the hands of the transferring company is 110 and it is deemed to transfer that balance to the receiving company for 110, thus recognizing a taxable gain of 10 (110 – 100) in the hands of the transferring company. As can be seen from the example above, it is possible that a gain or loss would be taxable in the hands of the transferring company as a result of the transfer. On the other hand, it could be argued that these rules simply allocate the overall gain or loss on the loan relationship between different legal entities and the transfer itself does not trigger a gain or loss. It is not clear whether or not this area of legislation is in compliance with the Directive.	ICTA 1988 s815A
<u>4.1.5 Capital allowances</u> In the cases of: (a) a division or partial division, or (b) a merger which results in a SE where the United Kingdom retains taxation rights after the transaction the relief required by the Directive has been provided by stating that the transfer of assets from transferring company to receiving company is	

deemed to take place at a value that would generate neither a gain nor a loss on transfer.

In the event that not all of the assets of a company are transferred to another legal entity under the transaction, then the tax values of the assets being transferred and not being transferred will be allocated in a 'just and reasonable manner'. Whilst this does not provide absolute certainty to the taxpayer, since the HMRC version of 'just and reasonable' may be different to the view that a taxpayer might ascribe, it should provide the relief described in the Directive.

However, there are two cases where the legislation may not give the relief required in the Directive or, where the derogation in Article 10(2) has been applied, it may not have been implemented in a manner consistent with the Directive.

(c) Merger of a UK-trade where the receiving company is not an SE

This situation has been specifically addressed in UK legislation and hence relief on the transfer of assets in this situation would not be due. Therefore, assets that qualify for capital allowances being transferred in this situation would be deemed to be transferred to the receiving company at market value. Therefore, to the extent that market value is different from the value of the assets for tax purposes (known as 'tax written down value' or 'TWDV') there will be a gain or a loss in the hands of the transferring company on transfer. This appears to be incompliant with the Directive.

(d) Division, Partial Division or Merger of a non-UK trade

As described elsewhere, UK legislation has taken advantage of the derogation to Directive permitted in Article 10(2) in respect of transactions involving permanent establishments located in Member States outside of the UK. Therefore, in this instance, assets are deemed to be transferred at market value rather than their TWDV.

In implementing the derogation, UK legislation permits a notional credit for any overseas tax arising on gains accruing to a transferring company under a transaction covered by the Directive. However, any differences between market value and TWDV on a transfer of assets covered by the directive generates a difference know as balancing charge or a balancing allowance depending on whether there is an excess or deficit. In the absence of a definition of the term 'gain' in the legislation, is it not clear whether a balancing charge would qualify as a gain. In the event that it was not then a notional tax credit would not be available and therefore UK legislation would be incompliant with the Directive in this regard.

<u>4.1.6 FA 2002 Sch 26 paragraphs 30B-30I</u>

The value at which a derivative contract is deemed to transfer under merger, division or partial division is the 'notional carrying value'. This is defined as being the amount that would have been the carrying value of the asset or liability in the accounts of the company if a period of account had ended immediately before the date when the transfer took place.

The same points exist regarding the transfer of derivative contracts as they do for loan relationships above. Therefore, it is not clear whether the

rules are in compliance with the Directive. 4.1.7 FA 2002 Sch 29 paragraphs 85B-88 Transfers of intangible assets between legal entities as part of a merger, division or partial division where the assets remain within the UK tax net will be treated as 'tax neutral'. The term tax-neutral means that the receiving company will be treated as taking on all of the tax attributes of the intangible asset as if it had always owned the asset. No gain or loss arises. This appears to be compliant with the Directive. 4.1.8 Other items Whilst the legislation above covers the treatment of the transfer of many items connected with a merger, division or partial division, there are a number of items upon which the legislation is silent e.g. stock in trade, trade creditors and debtors. Whilst it appears clear that the Directive should apply to these items, it is unclear what the treatment would be of these balances under UK law. It is therefore inconclusive whether or not the UK has complied with the Directive in these areas.	

4.2 Has specific guidance been issued in respect of divisions and partial divisions?	Reference
4.2 Specific Guidance for divisions and partial divisions Please see 4.1.	

How have the Article 4(1)(b) concepts of 'effectively connected' and 'permanent establishment' been interpreted and implemented in your national legislation? What, if any, administrative guidance has been issued?	Reference
4.3 'Effectively Connected' and 'Permanent Establishment' 4.3.1 Effectively Connected There is no specific definition of 'effectively connected' within UK legislation. Under first principles, assets are 'effectively connected' with a permanent establishment if they are used by the permanent establishment in a trade carried on by that permanent establishment to generate taxable profits. Whilst, in most cases, it should be relatively straightforward to determine whether or not an asset is used in the business which is being transferred. However, in cases where assets being transferred are used infrequently in the business, or used by more than one permanent establishment within the same legal entity (e.g., Intellectual property), the determination of whether that asset is effectively connected with that	FA 2003 s148, Inspectors Manuals – International Manual 153060, Double Tax Relief Manual 1710-1715.

permanent establishment will need to be done in a fair and reasonable manner. What constitutes a fair and reasonable manner will depend on the facts in that individual case. 4.3.2 Permanent Establishment The concept of 'permanent establishment' is defined in UK legislation and is imported from the OECD definition. The definition includes branches but also includes other establishments such as offices, mines and factories. Furthermore, the term permanent establishment is also defined within many double tax treaties that the UK has entered into. In general, these definitions are the same as the definition that is included within UK law. Guidance in HMRC Manuals is limited. Reference is made to OECD material with an instruction that any 'difficult cases' be referred to a specialist unit within HMRC for which guidance is not published.	

Do the tax authorities in your country seek to limit the scope of relief, for instance by seeking to recapture depreciation on the assets transferred?	Reference
4.4 Limitation of relief As noted above, where legislation seeks to treat transfers as being not subject to tax, there is no attempt to claw back relief claimed in respect of prior periods except where the United Kingdom has applied the derogations permitted in Article 10(2) (transactions where the United Kingdom loses taxing rights in a permanent establishment) and Article 10a(1) (transactions involving transparent entities).	

What applies in respect of transferred assets and liabilities that are not considered to be effectively connected with a permanent establishment?	Reference
4.5 Assets and liabilities not effectively connected with the permanent establishment The relief is only available where a business or part of a business is transferred in exchange for shares being issued by the receiving company to the shareholders of the transferring company. Therefore, if an asset is not able to be allocated to any permanent establishment that is being transferred, the relief that is available under the implementing legislation may not be available to the transfer of that asset. In that event it will be subject to the normal rules on transfers of assets between companies. The rules in respect of each different type of transfer are dependant on a number of factors e.g., whether the companies between which the assets are being transferred are deemed to be within a group. In general terms, the transfer will be deemed to take place at the market value of the item being transferred on the date of the transfer, with profits and losses calculated accordingly.	

Is a merger profit tax exempt at the level of the receiving company even if the profit can be allotted to shares of the receiving company in the transferring company?	Reference
4.6 Merger Profits Under UK law, 'merger profits' do not arise since, if the transaction is one that qualifies for relief under the implementing legislation, the receiving company is deemed to inherit the tax attributes of the assets being transferred in accordance set out in Section 4.1.	N/A.

What account has been taken of the case law of the ECJ, and in particular of the judgment in Case C-470/04 *'N'*?	Reference
4.7 Impact of ECJ Case Law There have been no specific amendments in respect of the legislation implementing the Mergers Directive as the result of Case Law. However, as discussed above, the UK still has an 'exit tax' upon migration of companies from the UK under certain circumstances. However, it is yet to be determined in the ECJ whether or not such exit tax provisions are contrary to the Article 56 of the EU Treaty (Freedom of Movement of Capital).	TCGA 1992 s185

Please describe the implementation of Article 4(2) in your national legislation and any administrative guidance that may have been issued, in particular the criteria by which an entity is defined as transparent.	Reference
4.8 Determination of tax transparent entities Please see 3.2.	See above

Has relief under Article 4 been made subject to conditions not set out in that Article?	Reference
4.9 Conditions to which Article 4 is subject to In each area of the legislation referred to previously, the conditions under which the relevant relief is given are that the transaction: (a) is effected for bona fide commercial purposes; and (b) does not for part of a scheme or arrangements of which the main purpose, or one of the main purposes, is the avoidance of UK tax. Whilst the concept of tax avoidance is not specifically discussed in the	

Directive, it is possible that the above restriction in respect of avoidance of UK tax may go beyond what is permitted under the EC Treaty (see '*Cadbury*'). Provided the arrangements are not 'wholly artificial' then it may be argued that the fact that such an arrangements results in a reduction of UK tax payables would still be permitted under the Directive and this is an area of developing law. So, for example, a group with a Dutch parent may consider disposing of part of a UK business located within a UK subsidiary. If the business was disposed of for cash to a third party, then this would be treated in the hands of the UK subsidiary as a disposal of the assets of the business and a gain or loss may accrue. However, an alternative way to dispose of the division might be to transfer the division to a non-UK subsidiary of the Dutch parent in a transaction that qualified as a partial division. Under the legislation that implements the Directive in the UK, this should not generate a gain in the hands of the UK company provided the business is still carried on in the UK as a permanent establishment of the receiving company. If that non-UK subsidiary were then disposed of then, provided the subsidiary being disposed of qualified for relief under the Dutch participation exemption, then that second disposal may not be subject either to UK or Dutch tax. However, if the partial division were only carried out in order to avoid the potential UK tax on the disposal of the UK business then the relief under the legislation implementing the Directive may be withdrawn. One further condition in the case of the transfer of Intangible assets under a merger, division, partial division or transfer of assets, is that the transferring company must obtain clearance from HMRC that that the transaction has been carried out for bona fide commercial purposes and does not form part of a scheme of arrangement of which the main purpose, or one of the main purposes of which was to avoid UK tax. This condition may place more restrictions upon the transferring company than are permitted under the Directive and, hence, may be incompatible with the Directive.	

Article 5 – Carry over of provisions and reserves

Is the term 'provisions and reserves' defined in your national legislation or in administrative guidelines?	Reference
<u>**5.1 Definition of 'provisions and reserves'**</u> There is no specific definition of the term in UK tax legislation and the UK does not allow tax free reserves or provisions.	ICTA 1988 s343

How has the exclusion of provisions and reserves 'derived from permanent establishments abroad' been implemented, i.e. how are provisions and reserves 'derived' from a foreign permanent establishment distinguished from provisions and reserves of other permanent establishments or business divisions, or of the company as a whole?	Reference
5.2 Allocation of provisions and reserves Please see 5.1 above.	ICTA 1988 s11, 11AA

What method is applied to allocate provisions and reserves in the case of a division, a partial division, or a transfer of assets?	Reference
5.3 Allocation of provisions and reserves on a division, partial division or transfer of assets Please see 5.1 above.	

Is the carry-over of provisions and reserves subject to conditions not set out in Article 5?	Reference
5.4 Conditions governing the relief There are no specific rules to cover this situation.	

Article 6 – Carry over of losses

How is the concept of 'loss' defined for the purposes of implementing Article 6?	Reference
6.1 Definition of 'loss' 6.1.1 Meaning of loss The concept of 'loss' has not been specifically defined for the purposes of implementing the Directive. Therefore, one has to return to first principles to determine the meaning of loss. In general terms in the UK, profits and losses are streamed with respect to the nature of the activity that generated them and a loss is deemed to arise when the expenses or debits arising in respect of one of those types of income exceeds the related income or credits. For any given classification of loss, the company or permanent establishment has a number of choices with respect how they can apply those losses against profits arising in that entity either in that period or in other periods, or against profits arising in other companies provided that they qualify under	ICTA 1988 s 343.

the UK's group relief rules. 6.1.2 Options Available in respect of losses With the exception of capital gains and losses, the choices available to a permanent establishment with respect to losses of a specific character arising in a particular period are as follows: (a) Use to offset against other types of income arising in the period. (b) Carry back one year against the income arising in the previous period. (c) Group relief against profits arising in other 'group' entities (subject to detailed anti avoidance rules). (d) Carry forward for offset against future income of the same nature arising in the future, there is no time limit on the carry forward of losses. However, as stated above, losses of a business are not transferred to the recipient company on the transfer of a trade (as opposed to the transfer of a legal entity) from one company to another except in the circumstance where the company owned 75% of the ordinary share capital of the receiving company after the transfer, or when the same shareholder owns 75% of the shares of both the receiving company and, either directly or indirectly at some point in the two years after the transfer.	

What method is applied to allocate losses to the permanent establishment?	Reference
6.2 Allocation of Losses to Permanent Establishment Only certain types of income and expenses are allocable to a permanent establishment, being: (a) trading income; (b) income from property or rights held for use by the permanent establishment; and (c) chargeable gains. The profits and losses of the trading activities of the permanent establishment are then calculated as if it were a separate enterprise trading with other permanent establishments within the same legal entity as if they were third parties. Furthermore, it is assumed that the permanent establishment has both the same credit rating as the legal entity in which it is located, and that is has the same debt to equity ratio as a distinct enterprise might reasonably be expected to have in the same circumstances. One point to note is that this precludes the allocation of certain types of interest cost incurred by the company that would ordinarily be treated as	ICTA 1988 s11, ICTA 1988 s11AA

'non-trade debits' rather than trading deductions (although interest incurred for general trading purposes, for example to fund working capital, would be deductible). In respect of gains and losses from rights and on capital gains, then losses on these items are calculated in the same way that they are for separate legal entities, provided the related asset 'belongs' to the permanent establishment.	

Has specific legislation been enacted for divisions, partial divisions, and transfers of assets?	Reference
6.3 Guidance in respect of divisions, partial divisions and transfers of assets The rules that are outlined in 6.1 & 6.2 above apply in all of the above scenarios.	

Has loss carryover been made subject to conditions not set out in Article 6? If so, do those conditions differ from any that may be applicable in a wholly domestic context?	Reference
6.4 Conditions governing relief under Article 6 Except in the case where the receiving company owns 75% of the equity of the transferring company, or the same shareholder owns 75% of the shares of both the receiving company and the transferring company either directly or indirectly at some point in the two years following the transaction, then loss transfers are not permitted on the transfer of a business from one legal entity to another by way of merger, division, partial division or transfer of assets. UK tax legislation does not discriminate between transactions in a wholly domestic situation and the cross border position as the same rules apply equally to both situations.	

Article 7 – Cancellation of holding

Has the amended holding threshold (15%) been implemented in your national legislation?	Reference
7.1 Holding threshold In respect of relevant legislation that enacts the Directive there is no such restriction.	TCGA 1992 s140G(4), TCGA 1992 s136(1)

Article 7(1) covers gains accruing on the cancellation of a holding. It does not cover losses that may be realised on such cancellation. Has the latter situation been dealt with your national legislation or administrative guidance?	Reference
7.2 Losses on cancellation of shares The legislation provides that no gain or loss arise on the cancellation.	TCGA 1992, s136(2)

Article 8 – Tax relief for shareholders

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the acquiring company from the shareholders of the acquired company should be considered to have been received at 'real' or 'market' value?	Reference
8.1 Prevention of Double Taxation 8.1.1 Share for Share exchanges Where a shareholder exchanges their shares in one company for shares in another, and the conditions for relief under the share for share exchange rules are met, then the newly received shares are treated as having the same tax attributes as the shares previously held. Economic double taxation on the shares transferred to the newly acquired company is avoided by deeming the shares to have been received by that other company at their market value. 8.1.2 Divisions and Partial Divisions and transfers of assets Securities issued under a division, partial division or transfer of assets are treated in the hands of the recipient shareholders, as if they formed part of their original shareholding in the transferring company. However, assets transferred to the receiving company are deemed to have been transferred at a value that would generate neither a gain nor a loss on the transfer. Therefore, effective double taxation is avoided since any disposal of the asset being transferred would not generate any more tax than would have been the case had the transaction not taken place. Furthermore, any disposal of the shares in the receiving company by the shareholders of the transferring company would generate no more tax than had the transaction not taken place and the shareholders disposed of an equivalent proportion of their original shareholding in the transferring company instead. Therefore, in the event that the receiving company subsequently sells the assets, any gain will be calculated with reference to the above valuation. However, in the event that the shares in the receiving company were sold, then the gain would be calculated by reference to the same value. Hence two gains may arise, one on the disposal of the assets and another on	TCGA 1992 s171(3), TCGA 1992,s140DA, TCGA 1992 s 136, TCGA 1992 Sch7AC

disposal of the shares and, hence there could be an element of economic double taxation on the two transactions combined.	

What guidance, if any, has your tax authority issued on the computation of the capital gain in the situation covered by Article 8(9)?	Reference
8.2 Treatment of cash receipts 8.2.1 Share for share exchanges Cash receipts are treated as though a part disposal of the securities in question had taken place under normal capital gains rules (see section 2.2 above). 8.2.3 Mergers, divisions and partial divisions As described in Section 2.2 above, except for the case where, after the transaction no assets remain subject to UK tax, in order to qualify for the relief, the transfer has to take place wholly in exchange for shares and debentures. To date, there has been insufficient activity in this area to know whether or not, by concession or otherwise, HMRC will allow relief to be given in respect of transactions where some cash (e.g., equal to or less than 10% of the value of the assets being transferred) is transferred to shareholders of the participating companies.	

Has relief under Article 8 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
8.3 Conditions governing Article 8 In general, the two restrictions in respect of relief are that: (a) The transaction must have been for bona fide commercial purposes and did not have tax avoidance as a main purpose or one of the main purposes. (b) In order for a merger, division or partial division to qualify for relief, then, in the event of a UK company merging into a non-UK entity, the non-UK entity must still remain subject to UK tax through a branch or permanent establishment in the UK.	

Article 9 – Transfer of Assets

Does your national legislation provide for the avoidance of economic double taxation, for instance by stipulating that the shares received by the transferring company should be considered to have been received at the ‘real’ or ‘market’ value of the assets transferred?	Reference
9.1 Avoidance of Double Taxation On a transfer of assets under United Kingdom legislation, except where the derogations under the Directive apply, the transaction is deemed to take place at a value that would generate neither a gain nor a loss on the transaction. Therefore, the assets transferred and the shares received are deemed to be held by the transferring company and the receiving company respectively at a value equal to the cost of the assets plus an indexation allowance as provided under UK legislation. Therefore, in the event that the receiving company subsequently sells the assets, any gain will be calculated with reference to the above valuation. However, in the event that the shares in the receiving company were sold, then the gain would be calculated by reference to the same value. Hence two gains may arise, one on the disposal of the assets and another on disposal of the shares and, hence there could be an element of economic double taxation on the two transactions combined.	TCGA 1992 s140DA. TCGA 1992 s171(3)

Has relief under Article 9 been made subject to conditions not set out in that Article, for instance holding period requirements, continuity of business requirements, nationality requirements?	Reference
9.2 Conditions governing Article 9 In general, the two restrictions in respect of relief are that: (a) The transaction must have been for bona fide commercial purposes and did not have tax avoidance as a main purpose or one of the main purposes. (b) In order for a merger, division or partial division to qualify for relief, then, in the event of a UK company merging into a non-UK entity, the non-UK entity must still remain subject to UK tax through a branch or permanent establishment in the UK. Furthermore, the restrictions regarding carryover of losses brought forward from one business to another remain in place on the transfer of a business from one legal entity to another. Example: A company located in the UK transfers a UK business to a subsidiary located in France and claims relief from tax on that transfer under the implementing legislation for the Directive. In the event that the French company was then subsequently sold, and this disposal qualified under the	

UK's substantial shareholding exemption as an exempt gain, then, prime facie, the UK parent could have avoided tax on the disposal of the assets within the business. However, in order to qualify for the benefit under the original asset transfer, the taxpayer would need to demonstrate that the transfer was not part of an arrangement, one of the main purposes of which was the avoidance of UK tax which, in the circumstances outlined above, could be seen as questionable.	

Article 10 – Permanent establishment in a third Member State

Does your national legislation provide for loss recapture as envisaged by Article 10(1)? If it does, please describe the conditions under which loss recapture occurs, the mechanism itself, and any administrative guidance that may have been issued.	Reference
<u>10.1 Provision of loss recapture</u> The United Kingdom does not consider loss recapture as stated in Article 10(1) as it applies the derogation available in Article 10(2) in respect of the transfer.	TCGA 1992 s140C(3-5), TCGA 1992 s140F(3-4)

Please describe your national legislation insofar as it deals with the situation described in the final sentence of Article 10(1).	Reference
<u>10.2 Loss recapture where permanent establishment is in the same country as the receiving company</u> The United Kingdom does not consider loss recapture as stated in Article 10(1) as it applies the derogation available in Article 10(2) in respect of the transfer.	TCGA 1992 s140C(3-5), TCGA 1992 s140F(3-4)

Does your national legislation provide for the taxation of unrealised capital gains as provided for by Article 10(2)? If so, please describe the legislation and any administrative guidance in detail, in particular as it may relate to the crediting of the tax that, but for the directive, would have been charged in the Member State of the permanent establishment.	Reference
<u>10.3 Taxation of unrealized gains</u> The specific rules are set out as follows: (a) in respect of divisions and partial divisions they are set out in TCGA 1992 s140C, and (b) in respect of mergers they are set out in TGCA 1992 s140F. However, where the transaction consists of a transfer of assets, the taxpayer has a choice of treatment. They can either claim the treatment set out in TCGA 1992 s140C that enacts the derogation to the Directive	TCGA 1992 s140C, TCGA 1992 s140F, ICTA 1988 s815A, Inspectors Manuals – Capital Gains Manual 45730-45739

set out in Article 10(2). However, an alternative treatment is offered in TCGA 1992 s140 which provides a different relief and is described below. <u>10.3.1 Divisions and Partial Divisions</u> Subsection 1 sets out the conditions under which the relief applies for transfers or part transfers of permanent establishment located outside of the UK between a company located in the UK and another one located in another Member State either wholly or partly in exchange for shares or debentures. It states that, for the relief to apply, an overall gain must arise on the transfer. As this relief is the alternative to a deferral type relief that may applies in similar circumstances but on a worldwide basis the relief is by way of making a claim so that the taxpayer choose between the taxation with deemed credit under the merger directive or for a deferral based claim. Subsection 1A extends the relief to partial divisions which occur when a company resident in the United Kingdom (the transferring company) transfers part of its business to a non-UK resident company in another Member State in exchange for the receiving company issuing shares to the shareholders of the transferring company(unless the receiving company is precluded from issuing shares under local company law). Subsection 3 states that the aggregate gains and losses from the transfer will be converted into a single gain. Subsection 4 then refers to ICTA 1988 s815A ICTA 1988 s815A(2) states that, where a gain accrues to a company in the above scenario and, but for the Merger Directive, tax would have been paid in the Member State that the permanent establishment was located in, that a deemed tax credit equal to the amount of tax that would have been paid in that Member State would be available in the UK to offset the UK tax due. In calculating that credit, the UK company must presume that: (a) as far as permitted locally, any losses arising in the Member State are offset against the gain arising; and (b) any relief available to that company in the Member State has been claimed. <u>10.3.2 Transfers of Assets</u> Under legislation in the United kingdom, two possible treatments are available in respect of transfers of assets where the United Kingdom loses the right to tax those assets. Under normal conditions, the rules for the transfers of assets mirror those for divisions and partial divisions described above. However, if the transferring company makes a claim to HMRC, an alternative relief is available. The conditions for this alternative relief are: (a) the assets which, together, form a trade located outside of the United Kingdom, are transferred to a company not resident in the United Kingdom; (b) the trade is transferred wholly or partly in exchange for shares and	

loan stock issued by the receiving company; (c) after the transaction, the transferring company owns at least 25% of the share capital of the receiving company; and (d) after the transaction, either no losses are available to offset any gains, or the amount of the total gain is greater than the amount of the losses. In this instance, the gain that would have arisen in the transferring company on transfer is deferred until the earlier of: (a) the receiving company disposes of the assets transferred (provided this happens within 6 years of transfer); or (b) the transferring company disposes of the securities received from the receiving company It should be noted that this relief was available before the legislation specifically implementing the Directive was enacted and, hence, provides additional relief in the case of transfers of assets where the United Kingdom loses taxing rights in the assets being transferred. <u>10.3.3 Mergers</u> Subsection 1 sets out the circumstances in which the relief is given which is where: (a) an SE is formed by a Merger of two or more companies; or (b) an SCE is formed by the merger of two or more co operative societies; or (c) the merger is effected by the transfer by a company of all its assets and liabilities to another company; or (d) the merger is effected by the transfer by two or more companies of all their assets and liabilities to a single new company in exchange for the issue of shares or debentures to the shareholders of the original companies. Subsection 2 then discusses various conditions that must be fulfilled for the relief to be available. Namely: (a) Each company must be resident in a Member State. (b) Not all of the merging companies can be in the same Member State. (c) During the course of the merger, a company resident in the UK transfers all assets and liabilities relating to a business carried on in another Member State through a permanent establishment, to a company resident in a Member State but not in the UK.	

(d) There must be a net gain accruing to the UK company.

(e) The transfer must be made in exchange for shares or debentures to the shareholders of the UK company (or if not, the reason being that the receiving company is precluded from doing so by local company law).

Where the above all holds true, the gains and losses arising on the transfer by the UK resident company of the assets and liabilities are all aggregated in to a single gain upon which tax is payable. However, a deemed credit for tax payable in the Member State in which the permanent establishment is situated is available as described in ICTA 1988 s815A (see above).

There is no written guidance from HMRC currently in respect of mergers since the legislation is still very new. Guidance does exist in the Inspectors Manuals in the case of the transfer of a non-UK trade. However, little additional guidance is given except to reiterate the rules as set out in legislation.

10.3.4 Additional Comments

There are a number of practical issues in respect of the operation of this relief that are not addressed by either legislation or in guidance issued by HMRC:

(a) In order to calculate the notional overseas tax credit available, it is unlikely to be a simple case of substituting the overseas tax rate for the United Kingdom tax rate on the gains arising from the transaction as the rules relating to the taxation of the transfer are likely to be different in the two jurisdictions, for example, in the calculation of any gains arising.

(b) It may not be straightforward to calculate the amount of overseas gain that would have existed 'but for the provisions of this Directive' as it may be difficult to envisage how the rules taxing the transaction in question would otherwise have operated, particularly where legislation enacting the Directive has replaced previously existing legislation.

(c) It is unclear what evidence is would be necessary to present to the UK tax authorities in order to demonstrate what tax would have been paid.

(d) It is unclear how a taxpayer could obtain confirmation from the overseas tax authority of the amount of tax that would have been due under the transaction 'but for the provisions of this Directive'.

Please also describe how account has been taken of ECJ case law, and in particular of the '*N*' judgment, in the legislation implementing Article 10(2)	Reference
<u>10.4 Impact of EU Case Law</u> The rules relating to transfers of assets and mergers were updated in November 2007 to take into account the amendments to the Directive. As such, no specific amendments have been made in respect of ECJ case law. With respect to '*N*' Case, the UK's implementation of the Mergers Directive has followed the wording of the directive closely, particularly the derogation from the Directive permitted in Article 10(2). Therefore, the points raised by '*N*' case with respect to how a Member State can seek to restrict the freedom of establishment of a person by imposing a form of exit taxation upon them is not addressed. It is, however, arguable that, by permitting authorities to tax a division, partial division or merger, albeit with full underlying credit for notional taxes paid elsewhere, this is a form of exit taxation that is contrary to the principles of the '*N*' case.	

Article 10a – Transparent entities

Please describe your national legislation implementing Article 10a, including any administrative guidance that may have been issued.	Reference
<u>10a.1 Derogation from Directive in respect of shareholders of transparent entities</u> The UK legislation has chosen to adopt Article 10a. In the instances where an entity is included in the Annex to the Directive as being covered by the directive but would be treated as a transparent entity then the following treatment applies: <u>10a.1.1 Share Exchanges</u> The treatment that the shares received by the shareholders in the company equate to their previous holdings in the receiving company is removed. Instead, such transfers are treated as normal sales and capital gains are calculated in the normal way. <u>10a.1.2 Divisions, Partial divisions and transfers of assets</u> If the transferring company is transparent then the transfer is treated as if were carried out at market value rather than at no-gain, no-loss. Furthermore, the issue of shares is not treated as a reorganisation of share capital but as a separate issue of shares. If the receiving company is treated as being transparent then it is only the reorganisation treatment that is denied in the hands of the shareholders.	TCGA 1992, s140H, TCGA 1992 s140I, TCGA 1992 s140K

10a.1.3 Mergers If the transferring company is transparent, then the gains arising on the transfer of assets to the receiving company will be subject to tax in the hands of the shareholders. Furthermore, the issue of the shares to the shareholders will not be treated as a reorganisation of the share capital of the receiving company and hence the reorganisation relief available in the case of an opaque company will not be available. If the receiving company is transparent, then it will just be the issue of shares to the shareholders of the transferring company that is not treated as a reorganisation. In all instances, tax on any gains that arise will be reduced by the deemed overseas tax credit that would have arisen in the Member State, but for the application of the merger Directive in that state.	

How have the 'profits' of an acquired company been defined in the context of your national legislation implementing Articles 10a(1) and 10a(2)?	Reference
10a.2 Definition of term 'profits' The term profits, under the implementing legislation of the Mergers Directive, refers to the deemed gain on the transfer of assets or shares from one entity to another. Trading profits and losses are not considered. In the case of an entity deemed to be transparent these will continue to be taxed in the hands of the shareholders in the ratio of their respective shareholdings in the company.	

10a.3 How does your national legislation indicate that the notional tax to be credited under Article 10a(2) should be determined in the case of an acquired company?	Reference
10a.3 Calculation of notional tax on transactions involving transparent entities In each case the mechanism is exactly the same. The first question to consider is whether the transfer that takes place would have been subject to tax in another Member State but for the operation of the Merger Directive (other than the United Kingdom). If such tax would have been due, the UK tax charge is reduced by the amount of that charge that would have been available for credit under the UK's double tax relief rules.	

How does your national legislation distinguish between Articles 10a(3) and 10a(4)?	Reference
10a.4 Distinction between Article 10a(3) and 10a(4) Article 10a(3) deals with the removal of shareholder relief in respect of divisions, partial divisions, asset transfers and share exchanges. The UK legislation has specifically applied that derogation from Article 8 within the implementing legislation. Article 10a(4) allows the United Kingdom to tax the shareholders of the transparent company as if it were resident in the UK on the transfer. However, this specific element of the derogation does not appear to have been transcribed into local law. However, as it is optional, this should not be treated as a breach of the terms of the implementation of the directive.	

What does that 'same treatment for tax purposes' (Article 10a(4)) entail in the case of your country?	Reference
10a.5 Meaning of 'same treatment for tax purposes' This element of the Article does not appear to have been transcribed into local law.	

Article 10b – Transfer of registered office - assets

Article 7 of Council Regulation (EC) 2157/2001 on the Statute for a European Company ('the SE Statute') requires that the 'registered office' be located in the same Member State as the 'head office'. It follows that when an SE transfers its registered office from one Member State to another, it must also transfer its head office to that other Member State. For Member States applying the siège réel doctrine, that may ensure that the tax residence of the SE is also transferred to the other Member State. Would the transfer of registered office of an SE, but for the application of Article 10b, give rise to exit taxation under your national law?	Reference
10b. 1 Exit taxes on transfer of registered office of SE in absence of Directive Under legislation that was pre-existing, this relief already existed. TCGA 1992 s185 states that, in the event of a UK tax resident company (including an SE) ceasing to be tax resident in the UK, then an exit charge arises on a deemed disposal of all of the assets in the company at market value. It is possible that this in incompatible with Article 56 of the EC Treaty (freedom of movement of capital) although this is yet to be tested in the courts.	TCGA 1992 s185

However, an exception to the general rule exists where those assets continue to be used in a trade carried on through a permanent establishment in the UK after the company has ceased to be UK tax resident. Therefore, provided the SE continues to operate a UK trade through a permanent establishment after the movement of its tax residence (see below how that coincides with movements of its head office) then there should be no tax in respect of any assets used in carrying on a trade in the UK through a permanent establishment. This provides the relief required in this Article.	

How, if at all, has the term 'head office' been defined in your national legislation implementing Article 10b, or in administrative guidance either on that Article or on Article 7 of Regulations 2157/2001?	Reference
10b.2 Definition of 'Head Office' The term 'head office' has not been defined in UK legislation. UK legislation, instead, refers to the term 'registered office' in the legislation implementing the Directive.	FA1988 s66A(1)

Does the concept of 'head office' coincide with the criterion used to determine tax residence under your national law or in the tie-breaker clauses of DTCs concluded by the Member State in question?	Reference
10b.3 Residence of Head Office In the case of a SE that transfers its 'registered office' to the United Kingdom, United Kingdom legislation deems the SE to automatically become UK tax resident. However, if the SE subsequently transfers its 'registered office' to another Member State, then this does not automatically mean that the SE will cease to be UK tax resident. Instead, it will be necessary to consider the operation of the double tax treaty between the United Kingdom and the country to where the company has transferred its registered office to determine where tax residency exists. Generally the SE will be resident where central management and control are deemed to be operated from.	

What applies in respect of assets not connected to a permanent establishment in the Member State from the registered office is transferred.	Reference
10b.4 Assets not connected to permanent establishment Assets not connected to a permanent establishment will not be covered by the exemption referred to above and hence a tax charge will apply on the transfer of the tax residence of the registered office from the UK.	

10b.5 What, if any account has been taken in your national legislation of ECJ case law, and in particular of the judgment in the 'N' case?	Reference
10b.5 Impact of ECJ Case Law No specific account has been taken of ECJ case law as the UK authorities believe that UK tax legislation is already compliant with the findings. However, UK law in respect of exit taxes may not be compliant with EC Freedoms (see section 10b.1).	

Article 10c Transfer of registered office – provisions/reserves/losses

Article 10c(2) refers to 'comparable circumstances'. How has this term been defined or developed in your national legislation or administrative guidelines?	Reference
10c.1 Definition of 'comparable circumstances' The term 'comparable circumstances' has not been specifically defined for the purposes of implementing the Directive. However, the concept is incorporated in UK legislation by the wording of the rules in respect of the use of losses carried forward. ICTA 1988 s393 states that a where a company carrying on a trade so as to be within the charge to corporation tax (either as a UK tax resident or a company that is not tax resident but subject to the charge to tax through a UK permanent establishment) incurs a loss, then it shall offset that loss against income from the same trade in a succeeding accounting period. Therefore, provided the SE is still within the charge to UK tax, losses are preserved in the UK in the event that it becomes non-UK resident, provided: (a) it carries on a trade in the UK through a permanent establishment; and	ICTA 1988 s11, ICTA 1988 s393. ICTA 1988 s768.

(b) losses are not deemed to be extinguished under rules that operate in the event of a change in the nature or conduct of a business within three years (either before or afterwards) of a change of ownership of the SE. This rules is a general rule under UK law and not specifically designed to implement or otherwise the Directive.	

10c.2 Article 10c(2) does not contain a loss recapture provision of the kind contained in Article 10(1). What applies under your national law in respect of losses attributable to a permanent establishment in a third Member State.	Reference
10c.2 Treatment of losses of non-resident permanent establishment The same treatment applies as set out in 10.3.3.	

Article 10d – Transfer of registered office - shareholders

In what circumstances, if at all, would the transfer of registered office of an SE be considered to give rise to a deemed liquidation from a tax perspective (even if not from a company law perspective), and to a deemed distribution of latent capital gains and retained earnings?	Reference
10d.1 Deemed liquidation on transfer of registered office of SE Provided there were no changes in the share capital of the SE, the change of registered office of the SE would, of itself, not trigger any deemed liquidation or distribution of assets within it.	

10d.2 What applies in respect of shareholders that are third (non-EU) country residents?	Reference
10d.2 Treatment of shareholders As 10.d.1 above.	

Article 11 – Anti-Abuse provisions

Article 11(1)(a) has been the subject of interpretation in the Courts judgments in Cases C-28/95 '*Leur-Bloem*' and C321/05 '*Kofoed*'. The Court has also provided considerable guidance on the parameters for anti-abuse legislation in the context of freedom of establishment in its judgment in Case-196/04 '*Cadbury*'. Has Article 11(1)(a) been transposed into your national law, and, if so, how?	Reference
<u>11.1 Interpretation of 'tax evasion' or 'tax avoidance'</u> Article 11a has been implemented by, in each instance where relief is available under the implementing legislation in respect of the Directive, making relief dependant upon the related transaction being carried out for bona fide commercial purposes and not for one where tax avoidance was the main purpose or one of the main purposes. There is no definition of bona fide commercial purposes and there is no guidance. It is a question that must be decided on the facts of individual cases. As an aside, the UK understandings of 'avoidance' and 'evasion' are different. Whereas 'avoidance' implies that the taxpayer has taken advantage of an aspect of legislation to reduce their tax burden that is generally seen as avoidance by the authorities (particularly when the relief taken advantage of becomes available in circumstances not originally envisaged by the draftsman). 'Evasion' however, implies that the taxpayer has used illegal or fraudulent means to reduce their tax burden. Furthermore, the doctrine of 'wholly artificial' as described in '*Cadbury Schweppes*' has not been specifically transcribed into the UK law governing the Directive, except as described above.	

If Article 11(1)(a) has not been transposed into your national law, is the tax administration likely to rely on 'a provision or general principle prohibiting abuse of rights or other provisions on tax evasion or tax avoidance' ('*Kofoed*', paragraph 46)?	Reference
<u>11.2 Reliance on general principles of abuse of rights</u> This is not applicable since the Article has been incorporated into UK legislation.	

If so, what, if any, steps has the tax authority in your country taken to bring your national provisions into line with the principles of the *'Cadbury'* judgment, and in particular those enunciated at paragraphs 36-37, 55, and 69-70?	Reference
11.3 Amendment of local legislation in the light of '*Cadbury Schweppes*' The UK's legislation has not been amended specifically in respect of the findings in *'Cadbury'*. Specifically, although the question as to what 'tax avoidance' is has been considered in the courts, with respect to the legislation implementing the Merger Directive the definition of 'wholly artificial' has not (although an attempt to transcribe such legislation has been made in the CFC legislation). Furthermore, the phrase 'wholly artificial' used in the *Cadbury* judgment has not been replicated in legislation and as a result the situations as whether or not the UK language is in compliance will be, ultimately, determined by the courts.	

Has your tax authority sought to rely on Article 11(1)(a) in order to impose holding period requirements, continuity of ownership or business requirements, nationally or residence requirements, or the requirement to obtain the prior approval of the tax administration before carrying out an operation falling within the scope of the Directive?	Reference
11.4 Other restrictions imposed on relief under the Directive No such restrictions have been imposed.	

How have the concepts of 'valid commercial reasons', 'restructuring' and 'rationalisation' been interpreted in your national legislation?	Reference
11.5 Interpretation of 'valid commercial reasons', 'restructuring' and 'rationalization' In this context, the concepts of 'restructuring' and 'rationalization' have not been addressed. The overarching requirement in UK Law in order to benefit from the relief stipulated in the Directive is that the transaction must be carried out for bona fide commercial purposes and not have as its main purpose, or one of the main purposes, tax avoidance, which is how the concept of 'valid commercial reasons has been transcribed into local law.	

Which party has the initial burden of proof to establish the existence or absence of 'valid commercial reasons'?	Reference
<u>11.6 Establishment of proof</u> Under UK law, corporation tax is a self assessed tax and returns are submitted on the basis that any adjustments in respect of, for example, whether or not a particular transaction has been carried out for bona fide commercial purposes. Under challenge from HMRC, the taxpayer will need to demonstrate to the Inspector that the transaction has been carried out for bona fide commercial purposes. However, it is possible to apply for pre transaction rulings from HMRC as to whether the merger, division, partial division or exchange of shares has been carried out for bona fide commercial purposes. In this instance, the burden of proof is on the taxpayer to establish that the transaction has been carried out for bona fide commercial purposes.	

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