

**Annex 1 - Austria**

# AUSTRIA

## **Austria – Tax issues related to the implementation of the SE**

### *INTRODUCTION*

*There are no special rules concerning the tax treatment of an SE. Thus, general rules of the KStG (Körperschaftsteuergesetz, Corporate Income Tax Law), UmgrStG (Umgründungssteuergesetz, Reorganization Tax Law), and the EStG (Einkommensteuergesetz, Income Tax Law) apply. The Guidelines on the application of the UmgrStG that might incorporate changes expected from the implementation of the SE Regulation in Austria are being prepared, but are not incorporated below as they are subject to confidential treatment.*

*As the SE has legal personality according to Art 1(4) of the Statute, it qualifies as a corporate taxpayer in terms of Sec 1(2) KStG. The list of qualified entities provided therein has not yet been amended as to the possibility to create an SE. Provided that the SE has its seat (similar to registered office) or the place of (effective) management (similar to the head office, but not necessarily conform) in Austria, it is subject to corporate income tax on its worldwide business and other income. Thus, if there is no link to Austria (ie a seat or a place of effective management) the SE is subjected to tax on its Austrian source income.*

*A resident SE may apply for group taxation under Sec 9 KStG. Further, the domestic and the international participation exemptions of Sec 10 KStG are applicable. As regards tax treaties, an SE that is taxable under the residence principle shall be considered resident in terms of a treaty modeled after the OECD MC. As for the possibility to offset losses incurred in a foreign permanent establishment the SE must qualify as Austrian resident. Under the tax authorities practice that was modified as to the decision of the VwGH (Verwaltungsgerichtshof, Supreme Administrative Court) issued in autumn 2001 (VwGH E 25.9.2001, 99/14/0217), foreign losses may be set off against domestic gains irrespective of the provisions of a tax treaty, but subject to the condition that no double-dipping of losses occurs.*

*As for the rest, the contribution or increase of capital of an SE having its seat or the place of management in Austria is subject to capital duty as such an SE is considered a domestic company in terms of Sec 4 KVG (Kapitalverkehrsteuergesetz, Capital Duty Law).*

*For general information, see IBFD guides II and III or the following summary:*

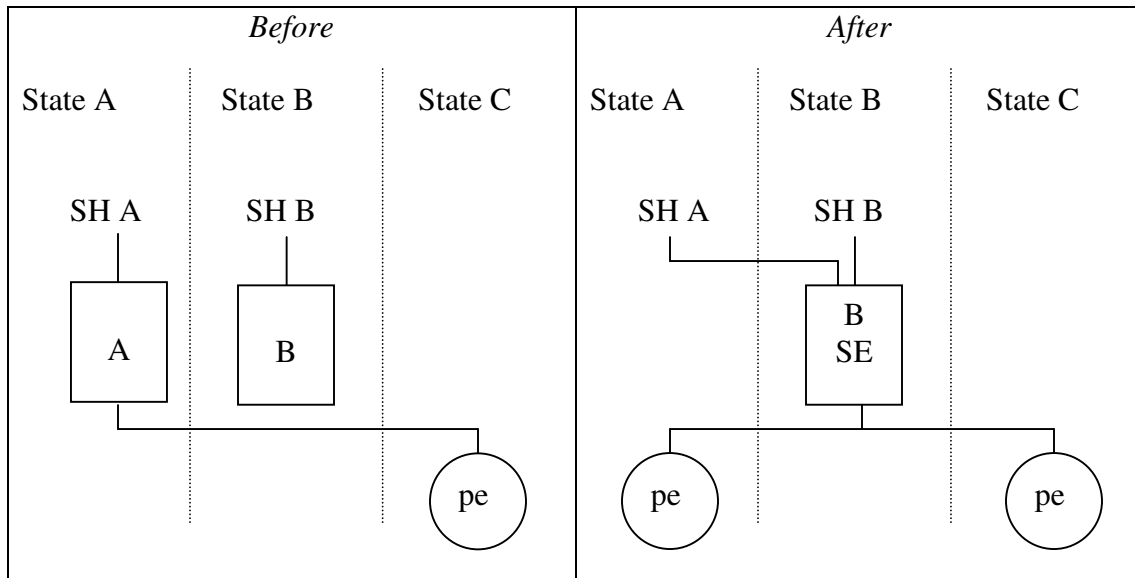
- the general corporate income tax rate is 34%; domestic dividends are exempt irrespective of the holding amount or period, foreign dividends are exempt under certain conditions (eg 25% participation and 2 years holding period); capital gains are taxable when paid in the domestic context, cross-border capital gains are exempt under the same conditions as dividends;*
- individuals are taxed at progressive rates up to 50%; capital gains realized by an individual shareholder are subject to progressive rates up to 25% under*

- certain conditions; and dividends received by an individual are taxed at 25% withholding when paid by domestic entities and at progressive rates up to 50% when foreign sourced (but see pending Lenz case, C-315/02); and*
- *Austria generally applies the exemption with progression method in its treaties.*

## CASE 1

### *Merger by acquisition*

(Art. 2 par. 1 jo. Art 17 par. 2(a) Reg. 2157/2001)



#### Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A and B are existing companies
- A and B are public limited-liability companies (see Annex I to Reg. 2157/2001)
- State A, State B, and State C are EU Member States
- A:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
  - has a permanent establishment in Member State C
- B:
  - formed under law of Member State B
  - registered office in Member State B
  - head office in Member State B
- B SE:
  - registered office in Member State B
  - head office in Member State B
  - will be covered by the EC Merger Directive

## Transactions

- A:
  - transfers all assets and liabilities to B
  - in exchange for shares in B (and cash payment if any, not exceeding 10% of nominal value of shares to be issued) issued to shareholder(s) of A
  - will be wound up without going into liquidation
  
- B / B SE:
  - as the acquiring company, B will take the form of an SE when the merger takes place (Art. 17 Reg. 2157/2001: “In the case of a merger by acquisition, the acquiring company shall take the form of an SE when the merger takes place”. Consequently, there are in fact two transactions: 1) the merger and 2) a transformation of a public limited-liability company into an SE. With regard to the transformation, see also Case 9.)
  - will be regarded as public limited-liability company governed by law of Member State B

## Questions

- 1) Assume Member State A is your country

### Tax effects for A in Member State A

- a) Will the merger give rise to any taxation of capital gains (= real value of assets & liabilities transferred minus their value for tax purposes), or is there roll-over relief?

*The merger is, generally, covered by Art I UmgrStG and therefore, the transfer does not trigger taxation of capital gains in Austria. A merger of an Austrian public limited-liability company with a foreign public limited-liability company into a SE is insofar subject to Sec 1(1) UmgrStG and therefore, tax neutral provided that the "hidden" reserves of the assets and liabilities transferred (including any goodwill) remain taxable in Austria. The taxable event is assumed for assets and liabilities in respect of which Austria loses its taxing rights. In such a case, the roll-over relief and other rules of Art I UmgrStG are not applicable.*

*Under the regime of Art I UmgrStG, the assets and liabilities are transferred at their book value provided that Austria retains its taxing rights. This will mainly not be the case if Austria is restricted to tax Austrian profits under a tax treaty with exemption method (eg if the property located in A does not qualify as a permanent establishment or immovable property under a particular tax treaty) and such a restriction has not been in place prior to the merger.*

*The provisions of Art I UmgrStG are further inapplicable if eg A has a permanent establishment in another state and there is either no tax treaty or a tax treaty providing for the credit method. In both cases, Austria will lose its taxing right through the merger. If a treaty provides for the exemption method (ie Austria has no taxing right pre-merger) there will be, however, no loss of Austrian taxing rights in the merger event. Due to the fact that cross-border mergers as described in Case 1 have not been feasible under Austrian companies law to date, the Austrian reorganization tax law will have to be harmonized with the EU Merger Directive (90/434/EEC) in such cases as described above with Art 10 of the EC Merger Directive.*

*To the extent that the transfer of assets and liabilities is accompanied by the loss of Austrian taxing rights, the merger is treated as a liquidation. The respective capital gain is subject to Austrian tax under Secs 20(1) and 19(1) KStG.*

- b) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State A, be taken over with the same roll-over relief by the permanent establishment of B SE in Member State A?

*Yes; see I(a).*

- c) Will B's permanent establishment in Member State A be allowed to take over the losses of A that have not been exhausted for tax purposes? If B would be a company resident in Member State A, would it then be allowed to take over these losses?

*In both cases, the permanent establishment of B SE and the company situated in A would be allowed to take over the losses of A subject to the following restrictions (Sec 4 UmgrStG):*

- losses incurred by the transferring company must be attributable to the business (or a part thereof or assets) transferred and the respective business (or a part thereof or assets) still exists at the merger date (Sec 4(1)(a) UmgrStG);*
- losses incurred by the acquiring company may be deducted insofar as the respective business (or a part thereof or assets) still exists at the merger date (Sec 4(1)(b) UmgrStG);*
- the business of the transferring (acquiring) company after the merger must be basically and in economic terms comparable to the business of the transferring (acquiring) company prior to the merger (Sec 4(1)(c) UmgrStG); and*
- in case of a merger between related companies, the amount of losses incurred by the subsidiary must be reduced by the amount of the write off claimed by the parent company at any time prior to the merger (Sec 4(1)(d) UmgrStG).*

*Under Sec 4(2) UmgrStG that is comparable to Sec 8(4) KStG, a loss carry forward is not available in the event of a significant change in the ownership of a company, in its organisational or economic structure. Thus, if the economic identity of the acquiring or the transferring company is lost, losses incurred by the respective company may not be set off. The restriction is not applicable if the changes are aimed at the improvement of the business structure (eg rationalization measures) at the level of the acquiring company.*

- d) Will Member State A renounce any right to tax the permanent establishment in Member State C?

*De facto yes, as B SE will be subject to (limited) corporate income tax liability in Austria. For details, see I(a).*

- e) Or will Member State A tax profits or capital gains with respect to the permanent establishment as a result of the merger? If so, will Member State A give relief for any (notional) tax charged on these profits or capital gains by Member State C?

*Austria will tax "hidden" reserves of the permanent establishment in Member State C if due to the merger, Austria loses its taxing right in respect of the "hidden" reserves (including the goodwill) of the permanent establishment located in Member State C. This is the case if the tax treaty between Austria and the Member State C provides for the credit method to avoid double taxation or in a non-treaty case. Austria may give relief for taxes levied in C on the basis of Sec 48 BAO aimed at avoidance of double taxation.*

*Due to the fact that cross-border mergers have not been possible under Austrian companies law, the Austrian reorganization tax law has to be harmonized with the EC Merger Directive (90/434/EEC), in such cases as described above with Art 10 of the EC Merger Directive.*

- f) Will Member State A reinstate in the taxable profits of A such losses of the permanent establishment as have been set off against the taxable profits of A in Member State A and which have not been recovered at the time of the merger?

*There is no explicit provision in Austrian tax law covering this issue. The reason for the lack of such a provision may be that for a long time Austria allowed to set off losses of foreign permanent establishments only if a tax treaty has been concluded between Austria and the foreign country providing for the credit method or in a non-treaty situation.*

*In a recent decision, however, the Austrian Supreme Administrative Court (VwGH E 25.9.2001, 99/14/0217) held that losses of a foreign permanent establishment are deductible in Austria even if the tax treaty provides for the exemption method. To avoid a double dip, the court stated that if in the following years the*

*permanent establishment losses are covered by the permanent establishment profits, such profits are only exempt by the treaty to the extent they have not been set off against the permanent establishment losses of the previous years.*

*By applying this decision to the question at issue one could argue that Austria could reinstate such losses in the taxable profits. As has been said, however, there is no explicit provision covering this issue.*

#### Tax effects for SH A in Member State A

- g) Will the issue of shares by B SE to SH A, resident in Member State A, in exchange for shares in A give rise to any taxation of the income, profits or capital gains of that shareholder?

*The issuance of shares by B SE to SH A is not seen as a taxable exchange of shares to the extent the merger is treated tax neutral (Sec 5(1) UmgrStG). Thus, the transaction will not give rise to any taxation of the income, profits or capital gains of that shareholder as long as SH A does not receive additional payments. If SH A receives such payments, they may give rise to income taxation depending on the specific situation of SH A. See further 1(h) to (i).*

- h) Will the issue of shares by B SE to a shareholder of A, not resident in Member State A, in exchange for shares in A give rise to any taxation of the income, profits or capital gains of that shareholder?

*Under Sec 5 (1) UmgrStG, the merger is not seen as a taxable exchange of shares though additional payments received by SH A, not resident in Austria, may give rise to taxation under domestic Austrian tax law if the interest in A (which is an Austrian corporation) amounts to at least 1% or the shares are held by a permanent establishment located in Austria. Such capital gain might be tax exempt on the tax treaty level.*

- i) Will the answers to the questions 1g) and 1h) differ if SH A is:

*In all the following circumstances, only additional payments but not the exchange of shares (to the extent the merger is treated tax neutral) may give rise to taxation. For details see 1(g).*

- i) A corporate shareholder?

*Additional payments are taxable irrespective of a holding period or the amount of the interest if the corporate shareholder is situated in Austria. If the interest in B SE amounts to at least 25% and will be held for more than two years such shares will qualify for the international participation exemption of Sec 10(2) KStG, ie dividends received and capital gains realized will be tax exempt. Thus, if, as a result of the merger, the corporate SH A holds such a*



*participation in B SE the difference between the book value and the fair market value of the participation is treated as a fictitious write off of the participation (Sec 5(7) UmrgStG). It remains subject to Austrian corporate income tax in case eg of a sale.*

*If the corporate shareholder is not situated in A, the payments will only give rise to taxation if the interest amounts to at least 1% or the shares are attributable to an Austrian permanent establishment. Such capital gain might be exempt under a tax treaty.*

ii) An individual shareholder not owning a substantial interest?

*Under Sec 31 EStG, a shareholder has a substantial interest if its direct or indirect participation amounts to at least 1% at any time during a five years period prior to the realization of capital gain (eg sale, liquidation of the company).*

*Additional payments will give rise to taxation in such situation only if the shareholder qualifies as Austrian resident and receives the payments within one year following the acquisition of shares (Sec 30 EStG). Shareholders not resident in Austria will not be taxed on such payments (Sec 98 EStG).*

*In case of a resident individual shareholder not owning a substantial interest a tax neutral step-up of the shares to the fair market value will be available under Sec 5(4) UmgrStG if the (in)direct interest in A (which is an Austrian corporation) amounted to less than 1% at any time during a five years period prior to the merger and the (in)direct shareholding in B SE after the merger is classified as a substantial interest in terms of Sec 31 EStG (ie at least 1%).*

iii) An individual shareholder owning a substantial interest?

*Under Sec 31 EStG, a shareholder has a substantial interest if its direct or indirect participation amounts to at least 1% at any time during a five years period prior to the realization of capital gain (eg sale, liquidation of the company).*

*Additional payments will give rise to taxation irrespective of where the shareholder is resident (Secs 31 and 98(8) EStG). Such capital gain might be tax exempt under a tax treaty.*

*In case of a resident individual shareholder owning a substantial interest in A prior to the merger but losing this substantial interest in the merger event the five-year period of Sec 31 EStG is extended to ten years (Sec 5(2) UmgrStG).*

iv) An individual entrepreneur?

*If the shares are attributed to the business of a resident or an Austrian permanent establishment of a non-resident entrepreneur additional payments will give rise to taxation as business profits.*

*If the entrepreneur is not resident in Austria and the shares do not qualify as business assets of its Austrian permanent establishment the payments will only give rise to taxation if the interest falls within the scope of Sec 31 EStG (ie substantial interest or at least 1% at any time during a period of five years prior to the merger). Such capital gain might be exempt under a tax treaty.*

2) Assume Member State B is your country

Tax effects for B and B SE in Member State B

- a) According to Art. 17 par. 2 Reg. 2157/2001, the acquiring company shall take the form of an SE when the merger takes place. According to Art. 37 par. 2 Reg. 2157/2001 the conversion of a public limited-liability company into an SE shall not result in the winding up of the company or in the creation of a new legal person. However, the Regulation itself does not give guidance with regard to taxation. Will the fact that B takes the form of an SE have corporate income tax consequences in Member State B?

*A reorganization of the type described (ie conversion or transformation of a public limited-liability company into an SE) will not have tax consequences in Austria.*

- b) What is the value for tax purposes that B SE has to attribute to the assets and liabilities, which are transferred to B SE as part of the merger and that form a permanent establishment in Member States A and C?

*Due to the fact that cross-border mergers as described in Case 1 have not been feasible under Austrian companies law up to date the reorganization tax law does not explicitly deal with this issue. Sec 2(1) UmgrStG indicates that the value used for tax purposes will be the relevant book value. Such value would generally not be relevant in case of a tax treaty that provides for the exemption method. In case of a tax treaty providing for the credit method or in a non-treaty situation, general tax rules provide that an appreciation up to the fair market value would have to be made. If the merger leads to taxation in the Member State A or C and a particular tax treaty or a relevant domestic measure provides for the credit method the appreciation in value is explicitly allowed by Sec 2(2) UmgrStG.*

Tax effects for SH B in Member State B

- c) Will the fact that B will take the form of an SE result in tax consequences for SH B?

*The merger should not result in any tax consequences as for SH B there is no exchange of shares by the transformation. If, however, as a cause of the merger the amount of the interest changes, such a change may result in tax consequences (see below). If SH B receives payment due to the merger, the payments may give rise to taxation depending on the specific situation of SH B.*

- d) Will the answer to question 2c) above differ if SH B is:  
i) A corporate shareholder?

*The corporate shareholder holds pre-merger and post-merger an interest in a domestic public limited-liability company and therefore, the situation does not change from a tax point of view. If the SH B receives payments due to the merger, the payments will be subject to tax. If the corporate shareholder is not situated in Austria, the payments will only give rise to taxation if the interest amounts to at least 1% or the shares are attributable to a permanent establishment in country A. Such capital gain might be tax exempt on tax treaty level.*

- ii) An individual shareholder not owning a substantial interest?

*Under Sec 31 EStG, a shareholder has a substantial interest if its direct or indirect participation amounts to at least 1% at any time during a five years period prior to the realization of capital gain (eg sale, liquidation of the company).*

*The individual shareholder holds pre-merger and post-merger an interest in a domestic public limited-liability company and therefore the situation does not change from a tax point of view.*

*Additional payments will give rise to taxation in such situation only if the shareholder is resident in Austria and receives the payments within one year after having acquired the shares irrespective of the amount of the participation (Sec 30 EStG). Non-resident shareholders will not be taxed on such payments.*

*In case of a resident individual shareholder not owning a substantial interest, a tax neutral step-up of the shares to the fair market value is available under Sec 5(4) UmgrStG if the (in)direct interest in B (which is an Austrian corporation) amounted to less than 1% at any time during a five years period prior to the merger and the (in)direct shareholding in B SE post-merger is a substantial interest in terms of Sec 31 EStG (ie at least 1%).*

iii) An individual shareholder owning a substantial interest?

*Under Sec 31 EStG, a shareholder has a substantial interest if its direct or indirect participation amounts to at least 1% at any time during a five years period prior to the realization of capital gain (eg sale, liquidation of the company).*

*Additional payments will give rise to taxation irrespective of where the shareholder is resident. Such capital gain might be tax exempt under a tax treaty.*

*In case of a resident individual shareholder owning pre-merger a substantial interest in B but losing such an interest post-merger, the holding period of Sec 31 EStG is extended from five to ten years (Sec 5(2) UmgrStG).*

iv) An individual entrepreneur?

*If the shares are attributed to the business of a resident or an Austrian permanent establishment of a non-resident entrepreneur additional payments will give rise to taxation as business profits.*

*If the entrepreneur is not resident in Austria and the shares do not qualify as business assets of its Austrian permanent establishment the payments will only give rise to taxation if the interest falls within the scope of Sec 31 EStG (ie substantial interest or at least 1% at any time during a period of five years prior to the merger). Such capital gain may be exempt under a tax treaty.*

3) Assume Member State C is your country

Tax effects for A and B SE in Member State C with respect to its permanent establishment in Member State C

- a) Will the merger give rise to any taxation in A of capital gains (= real value of assets & liabilities transferred minus their value for tax purposes) or is there roll-over relief?

*As the merger falls within the scope of Art I UmgrStG there will be a roll-over relief for assets of the permanent establishment in Austria (as Member State C), ie B SE has to carry on the tax book values. If the merger leads to taxation in Member states A or B and a single tax treaty provides for the credit method (or a similar domestic measure for the elimination of double taxation is available) a taxable step-up would presumably be possible under Sec 2(2) UmgrStG.*

- b) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State C, be taken over with the same roll-over relief by the permanent establishment of B SE in Member State C?

*Yes; see further 3(a).*

- c) Will B SE's permanent establishment in Member State C be allowed to take over the losses of A's permanent establishment that have not been exhausted for tax purposes?

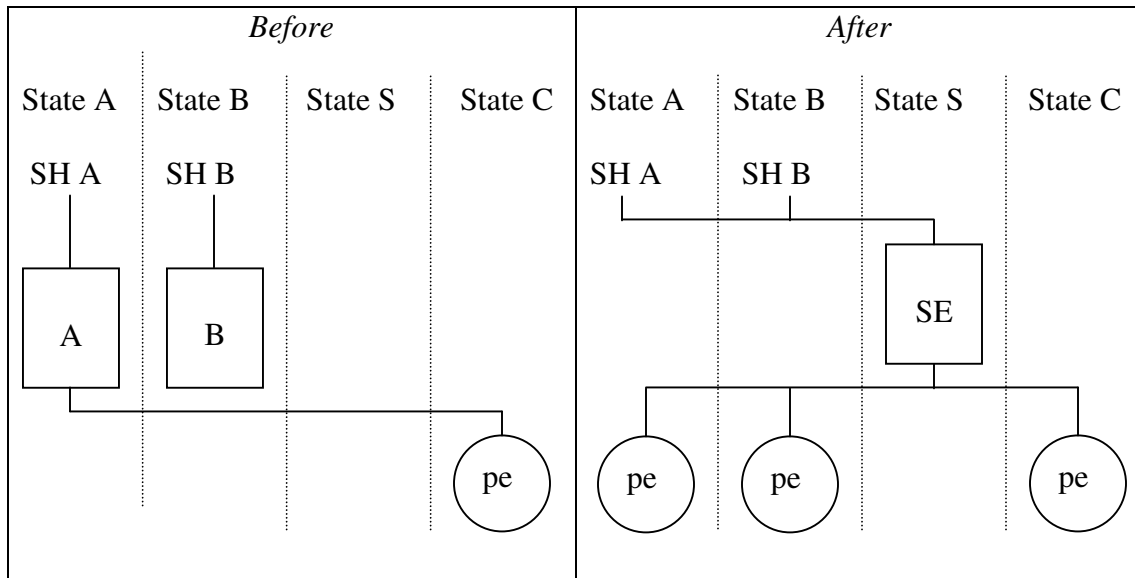
*In principle, the permanent establishment of B SE will be allowed to take over the losses of the permanent establishment of A (Sec 4 UmgrStG; see further 1(c)). Under the general rule of Sec 102(2)(2) EStG, however, the loss incurred by a permanent establishment loss can be carried forward up to the extent it is not covered by other than Austrian source income of the non-resident taxpayer in the current year.*

- d) If B SE would be a company resident in Member State C, would it then be allowed to take over these losses? See Merger Directive Art. 6.

*The permanent establishment of B SE will be allowed to take over the losses of the permanent establishment of A (Sec 4 UmgrStG; see further 1(c)). The requirements of Sec 102(2)(2) EStG need not to be met.*

## CASE 2

### *Merger by formation of a new company* (Art. 2 par. 1 jo Art 17. par 2(b) Reg. 2157/2001)



#### Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A and B are existing companies
- A has a permanent establishment in Member State C
- SE is a new company
- A and B are public limited-liability companies (see Annex I to Reg. 2157/2001)
- State A, State B, State C, and State S are EU Member States
- A:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
- B:
  - formed under law of Member State B
  - registered office in Member State B
  - head office in Member State B
- SE:
  - formed under law of Member State S
  - registered office in Member State S
  - head office in Member State S
  - will be covered by the EC Merger Directive

### Transactions

- A:
  - transfers all assets and liabilities to SE
  - in exchange for shares of SE (and cash payment if any, not exceeding 10% of nominal value of shares to be issued) issued to shareholder(s) of A
  - will be wound up without going into liquidation
- B:
  - transfers all assets and liabilities to SE
  - in exchange for shares of SE (and cash payment if any, not exceeding 10% of nominal value of shares to be issued) issued to shareholder(s) of B
  - will be wound up without going into liquidation
- SE:
  - will be a newly formed SE
  - will be regarded as public limited-liability company governed by the law of Member State S

### Questions

1) Assume Member State A is your country

#### Tax effects for A in Member State A

- a) Will the merger give rise to any taxation of capital gains (= real value of assets & liabilities transferred minus their value for tax purposes), or is there roll-over relief?

*See Case 1, I(a).*

- b) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State A, be taken over with the same roll-over relief by the permanent establishment of SE in Member State A?

*See Case 1, I(b).*

- c) Will SE's permanent establishment in Member State A be allowed to take over the losses of A that have not been exhausted for tax purposes? If SE would be a company resident in Member State A, would it then be allowed to take over these losses?

*See Case 1, I(c).*

- d) Will Member State A renounce any right to tax the permanent establishment in Member State C?

*See Case 1, I(d).*

- e) Will Member State A reinstate in the taxable profits of A such losses of the permanent establishment as have been set off against the taxable profits of A in Member State A and which have not been recovered at the time of the merger?

*See Case 1, I(f).*

- f) Or will Member State A tax profits or capital gains of the permanent establishment resulting from the merger? If so, will it give relief for any (notional) tax charged on these profits or capital gains by Member State C?

*See Case 1, I(e).*

#### Tax effects for SH A in Member State A

- g) Will the issue of shares by SE to SH A, resident in Member State A, in exchange for the shares in A give rise to any taxation of the income, profits or capital gains of that shareholder or is there roll-over relief?

*See Case 1, I(g).*

- h) Will the issue of shares by SE to a shareholder of A, not resident in Member State A, in exchange for the shares in A give rise to any taxation of the income, profits or capital gains of that shareholder or is there roll-over relief?

*See Case 1, I(h).*

- i) Will the answers to the questions 1g) and 1h) differ if SH A is:

*See Case 1, I(i).*

- i) A corporate shareholder?
- ii) An individual shareholder not owning a substantial interest?
- iii) An individual shareholder owning a substantial interest?
- iv) An individual entrepreneur?



2) Assume Member State S is your country

Tax effects for SE in Member State S

- a) What is the value for tax purposes that SE has to attribute to the assets and liabilities, which are transferred to SE as part of the merger and that form a permanent establishment in Member States A, B and C?

*See Case 1, 2(b).*

Tax effects for shareholder(s) of SE in Member State S

- b) Is there any provision in the legislation of Member State S that affects the shareholder of SE whether resident in Member State S or not? For example, are there provisions with regard to the valuation of the shares received in SE?

*The issuance of shares by SE to its shareholders is not seen as a taxable exchange of shares (Sec 5(1) UmgrStG). Thus, the transaction will not give rise to any taxation of the income, profits or capital gains of a respective shareholder as long as the shareholder does not receive additional payments. If the shareholder receives such payments they may give rise to taxation depending on the specific situation of shareholder. The tax consequences are the following:*

- *for a corporate shareholder situated in Austria, additional payments are taxable irrespective of the holding period or the amount of the interest. If the interest in A and B amounted to at least 25% each and has been held for more than two years such shares qualify for the international participation exemption of Sec 10(2) KStG but will lose this status as SE is a domestic PLLC. Therefore, there is a possibility for a tax neutral step-up (Sec 7(2)(2) UmgrStG). In other cases the corporate shareholder accounts for the book value for tax purposes;*
- *for a non-resident corporate shareholder, shares will be subject to tax in Austria if the interest amounts to at least 1% at any time during a five years period prior to the merger or the shares are attributable to its Austrian permanent establishment. Such capital gains might be tax exempt under a tax treaty. If the shares will potentially become subject to Austrian tax a step-up to the fair market value should be possible under the rationale of Sec 5(4) UmgrStG;*
- *an individual shareholder owning a substantial interest in neither A nor B, additional payments will give rise to taxation only if the shareholder is resident in Austria and receives such payments within one year after having acquired the shares irrespective of the amount of shareholding (Sec 30 EStG). Non-resident shareholders will not be taxed on such payments;*
- *for a resident individual shareholder not owning a substantial interest, a tax neutral step-up to the fair market value will be available if the*

- (in)direct interest in A or B amounted to less than 1% at any time during a five years period pre-merger and the (in)direct shareholding in S after the merger is a substantial interest, ie at least 1%;*
- *a non-resident individual shareholder is subject to Austrian tax if the interest in SE amounts to at least 1% at any time during a five year period prior to the merger or the shares are attributable to its Austrian permanent establishment. Such capital gains might be exempt under a tax treaty. If the shares will potentially become subject to tax in Austria a step-up to the fair market value should be possible under the rationale of Sec 5(4) UmgrStG;*
- *for an individual shareholder owning a substantial interest in either A or B, additional payments will give rise to taxation only if the shareholder is resident in Austria. Non-resident shareholders are not taxed on such payments;*
- *for a resident individual shareholder owning a substantial interest in either A or B, no tax neutral step-up of the shares to the fair market value will be available. Such a step-up is possible only for shares in the PLLC provided that the interest is less than 1%;*
- *a non-resident individual shareholder is subject to tax in Austria if the interest in SE amounts to at least 1% at any time during a period of five years prior to the merger or the shares are attributable to its Austrian permanent establishment. The capital gain might be exempt under a tax treaty. If the shares will potentially become subject to tax in Austria a step-up to the fair market value should be possible under the rationale of Sec 5(4) UmgrStG;*
- *a resident individual shareholder owning a substantial interest in A or B pre-merger but losing this substantial interest by the merger, the period of Sec 31 EStG is extended from five to ten years (Sec 5(2) UmgrStG); and*
- *for an individual entrepreneur additional payments will give rise to taxation if the shares are part of the business assets or attributed to the Austrian permanent establishment. The shareholder has to remain with book values in these shares for tax purposes.*

3) Assume Member State C is your country

Tax effects for A and SE in Member State C in respect of its permanent establishment in Member State C

- a) Will the merger give rise to any taxation of capital gains (= real value of assets & liabilities transferred minus their value for tax purposes) or is there roll-over relief?

*See Case 1, 3(a).*

- b) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State C, be taken over with the same roll-over relief by the permanent establishment of SE in Member State C?

*See Case 1, 3(b).*

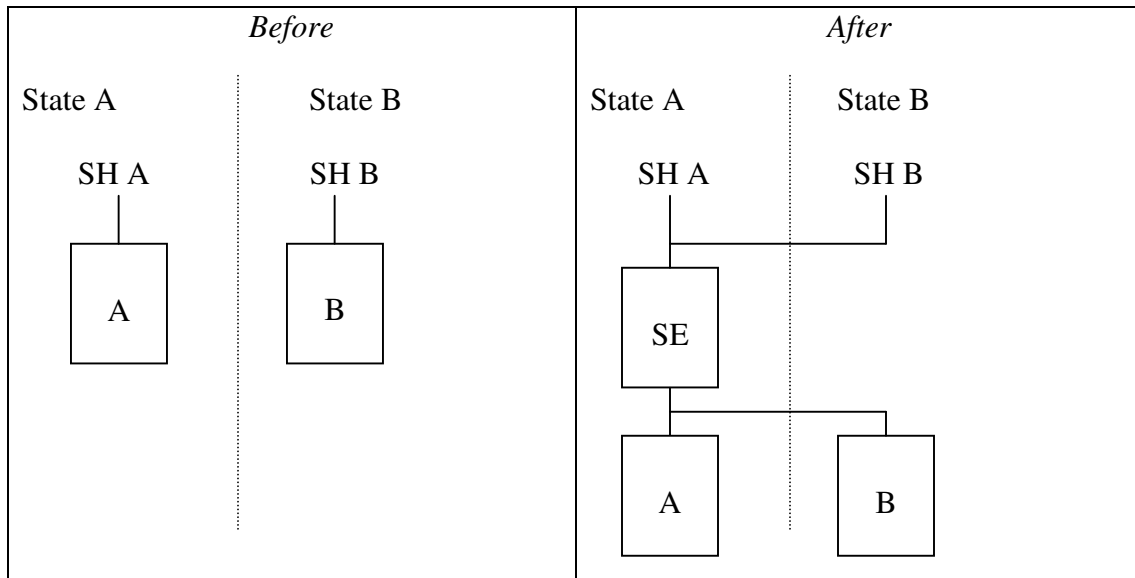
- c) Will SE's permanent establishment in Member State C be allowed to take over the losses of A's permanent establishment that have not been exhausted for tax purposes? If SE would be a company resident in Member State C, would it then be allowed to take over these losses?

*See Case 1, 3(c) and 3(d).*

### CASE 3

#### *Formation of a Holding – SE – 1*

(Art. 2 par. 2(a) jo. Art. 32, Art. 33 and Art. 34 Reg. 2157/2001)



#### Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A and B are existing companies
- SE is a new company
- A and B are public or private limited-liability companies (see Annex II Reg. 2157/2001)
- State A and State B are EU Member States
- A:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
- B:
  - formed under law of Member State B
  - registered office in Member State B
  - head office in Member State B
- SE:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
  - will be covered by the EC Merger Directive

## Transactions

- SE:
  - will be regarded as public limited-liability company governed by the law of Member State A
  - acquires holding in A and B
  - such that it obtains more than 50% of the permanent voting rights in A and B
  - in exchange for shares in SE
  - issued to the shareholders of A and B

## Questions

- 1) Assume Member State A is your country

### Tax effects for SE in Member State A

- a) Are there any provisions for the valuation for tax purposes of the shares in A and B acquired by SE? Do the shares have to be valued at the book value of the exchanging shareholder or at a higher value?

*Under Sec 18(1) UmgrStG, the shares acquired by SE have to be valued at their pre-acquisition value. In general this will be the book value (Sec 16(1)UmgrStG) though in certain cases, the fair market value is of relevance (Secs 16 and 17 UmgrStG).*

- b) Are there any provisions for the valuation for tax purposes of the shares issued to SH A and SH B? Do the shares have to be valued at the book value of the shares exchanged by the shareholder or at a higher value?

*Under Sec 20 UmgrStG, the shares issued to SH A and SH B have to be valued at the same value as the shares exchanged.*

### Tax effects for SH A in Member State A

- c) Will the issue of shares by SE to SH A in exchange for shares in A give rise to any taxation of the income, profits or capital gains of SH A or is there roll-over relief?

*As SH is resident in Austria and A is situated in Austria as well, a roll over relief is available under Sec 16(1) UmgrStG. It is assumed that besides the exchange of shares, no other payments are made.*

- d) Will the answers to the question 1c) differ if SH A is:  
i) A corporate shareholder?

*No.*

- ii) An individual shareholder not owning a substantial interest?

*No. For a resident individual shareholder owning minority interest (less than 1%), a tax neutral step-up of the shares to the fair market value is available if the (in)direct interest in A (which is an Austrian corporation) amounted to less than 1% at any time during a period of five years prior to the acquisition and the (in)direct shareholding in SE is a substantial interest, ie at least 1% (which might presumably be never the case) (Sec 20(6)(2) UmgrStG).*

- iii) An individual shareholder owning a substantial interest?

*No. A resident individual shareholder owning pre-acquisition a substantial interest in A but losing this substantial interest through the acquisition, the holding period of Sec 31 EStG is extended from five to ten years (Sec 20(5) UmgrStG).*

- iv) An individual entrepreneur?

*No.*

- 2) Assume Member State B is your country

Tax effects for SH B in Member State B

- a) Will the issue of shares by SE to SH B in exchange for shares in B give rise to any taxation of the income, profits or capital gains of SH B or is there roll-over relief?

*As SH B is resident in Austria and SE is situated in another Member State a roll-over relief is available under Secs 16(1) and 20 UmgrStG.*

- b) Will the answers to the question 1a) differ if SH B is:  
i) A corporate shareholder?

*Basically no. If SH B is a corporate shareholder it will be crucial whether the shares will receive or lose their status as international participation exemption in terms of Sec 10(2) KStG (i.e. 25% direct participation). If, as a cause of the exchange of shares, the participation receives such a status, the difference between the fair market value of such a participation and its book*

*value (“hidden” reserves) is considered a fictitious write off that is subject to tax if the participation is alienated (Sec 20(7) UmgrStG).*

ii) An individual shareholder not owning a substantial interest?

*No. As a general rule, Sec 17 UmgrStG applies. For a resident individual shareholder owning a minority interest (ie less than 1%), a tax neutral step-up to the fair market value is available if the (in)direct interest in A (which is an Austrian corporation) amounted to less than 1% at any time during a period of five years prior to the exchange and the (in)direct shareholding in SE is a substantial interest, ie at least 1% (which might presumably be never the case) (Sec 20(6)(2) UmgrStG).*

iii) An individual shareholder owning a substantial interest?

*No. A resident individual shareholder owning pre-acquisition a substantial interest but losing this substantial interest through the acquisition, the holding period of Sec 31 EStG is extended from five to ten years (Sec 20(5) UmgrStG).*

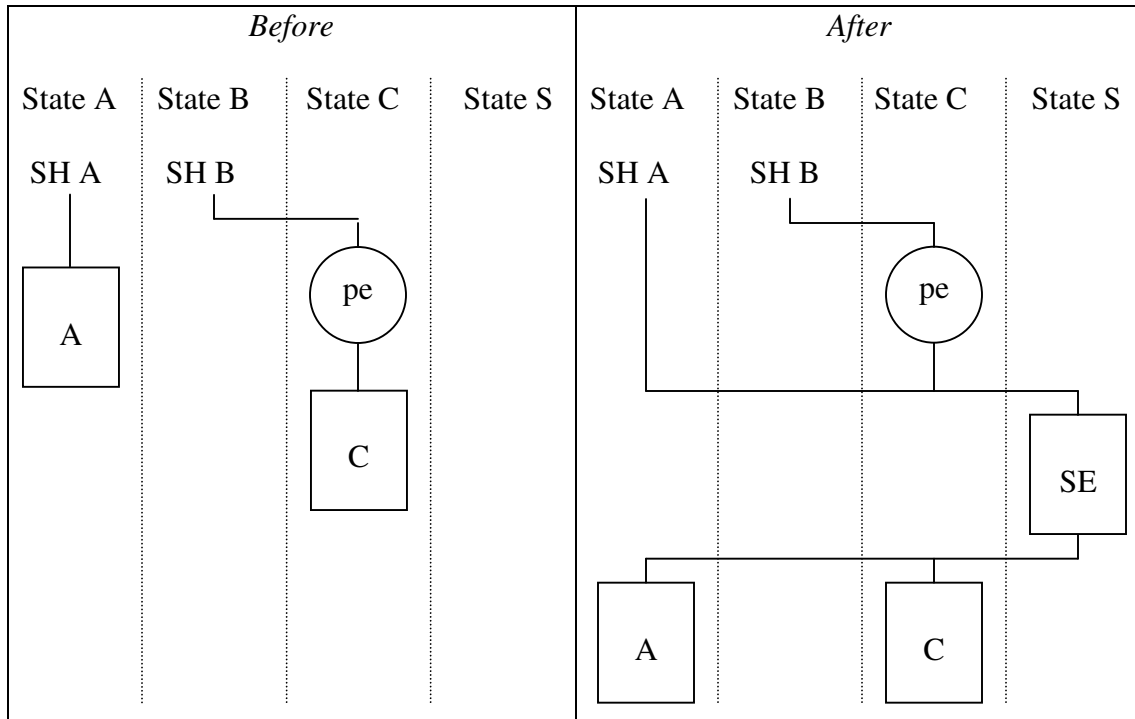
iv) An individual entrepreneur?

*No.*

## CASE 4

### *Formation of a Holding – SE*

(Art. 2 par. 2(a) and (b) jo. Art. 32, Art. 33, and Art. 34 Reg. 2157/2001)



#### Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A and C are existing companies
- The shares in C are attributable to pe in State C
- SE is a new company
- A and C are public or private limited-liability companies (see Annex II)
- State A, State B, State C and State S are EU Member States
- A:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
- C:
  - formed under law of Member State C
  - registered office in Member State C
  - head office in Member State C
- SE:
  - formed under law of Member State S



- registered office in Member State S
- head office in Member State S
- will be covered by the EC Merger Directive

### Transactions

- SE:
  - will be regarded as public limited-liability company governed by the law of Member State S
  - acquires holding in A and C
  - such that it obtains more than 50% of the permanent voting rights in A and C
  - in exchange for shares in SE
  - issued to the shareholders of A and C

### Questions

1) Assume Member State A is your country

#### Tax effects for SH A in Member State A

a) *Will the issue of shares by SE to SH A in exchange for shares in A give rise to any taxation of the income, profits or capital gains of SH A or is there roll-over relief?*

*See Case 3, 2(a).*

b) Will the answer to the above question be different in the case of:

i) SH A being an individual shareholder not owning a substantial interest?

*See Case 3, 2(b).*

ii) SH A being an individual shareholder owning a substantial interest?

*See Case 3, 2(b).*

iii) SH A being an individual entrepreneur?

*See Case 3, 2(b).*

iv) SH A being a corporate shareholder?

*See Case 3, 2(b).*

2) Assume Member State B is your country

Tax effects for SH B in Member State B

- a) Will the issue of shares by SE to SH B in exchange for shares in C give rise to any taxation of the income, profits or capital gains of SH B or is there roll-over relief?

*As mentioned above, the shares in C are attributable to permanent establishment in State C and remain, after the exchange of shares, attributable to this permanent establishment.*

*In general, there is roll-over relief under Sec 16(1) UmgrStG although there is a possibility for a taxable step-up under Sec 16(2) UmgrStG if the exchange of shares is subject to tax in Member State S and if there is a tax treaty between Austria and Member State C (or a similar domestic measure for the elimination of double taxation) providing for the credit method. Thus, under these conditions, a taxable step-up would be possible in accordance with Sec 2(2) UmgrStG.*

- b) Will the answer to the above question be different in the case of:  
i) SH B being an individual entrepreneur?

*No.*

- ii) SH B being a corporate shareholder?

*Basically no. But if SH B is a corporate shareholder it will be important whether the participation will keep or lose its status as an international participation in terms of Sec 10(2) KStG (ie 25%). If it loses such a status there is a possibility for a tax-neutral step-up under Sec 20(7) UmgrStG.*

3) Assume Member State C is your country

Tax effects for SH B in Member State C

- a) Will the issue of shares by SE to SH B in exchange for shares in C give rise to any taxation of the income, profits or capital gains of SH B or is there roll-over relief?

*As mentioned above, the shares in C are attributable to permanent establishment in State C and remain, after the exchange of shares, attributable to this permanent establishment.*

*In general, there is roll-over relief under Sec 16(1) UmgrStG although there is a possibility for a taxable step-up under Sec 16(2) UmgrStG if the exchange of shares is subject to tax in Member State S and if there is a tax treaty between*

*Austria and Member State C (or a similar domestic measure for the elimination of double taxation) providing for the credit method. Thus, under these conditions, a taxable step-up would be possible in accordance with Sec 2(2) UmgrStG.*

- b) Will the answer to the above question be different in the case of:  
i) SH B being an individual entrepreneur?

*No.*

- ii) SH B being a corporate shareholder?

*Basically no. But if SH B is a corporate shareholder it will be important whether the participation will keep or lose its status as an international participation in terms of Sec 10(2) KStG (ie 25%). If it loses such a status there is a possibility for a tax-neutral step-up under Sec 20(7) UmgrStG.*

*Remark: We assume that Member State C is our country (ie Austria). Under Austrian domestic corporate income tax law, permanent establishments of EU-corporations do qualify for the international participation exemption under Sec 10(2) KStG (see Sec 21(1)(2)(a) KStG).*

- 4) Assume Member State S is your country

Tax effects for SE in Member State S

- a) Are there any provisions for the valuation for tax purposes in Member State S of the shares of A and C acquired by SE? Do the shares have to be valued at the book value of the exchanging shareholder or at a higher value?

*See Case 3, I(a).*

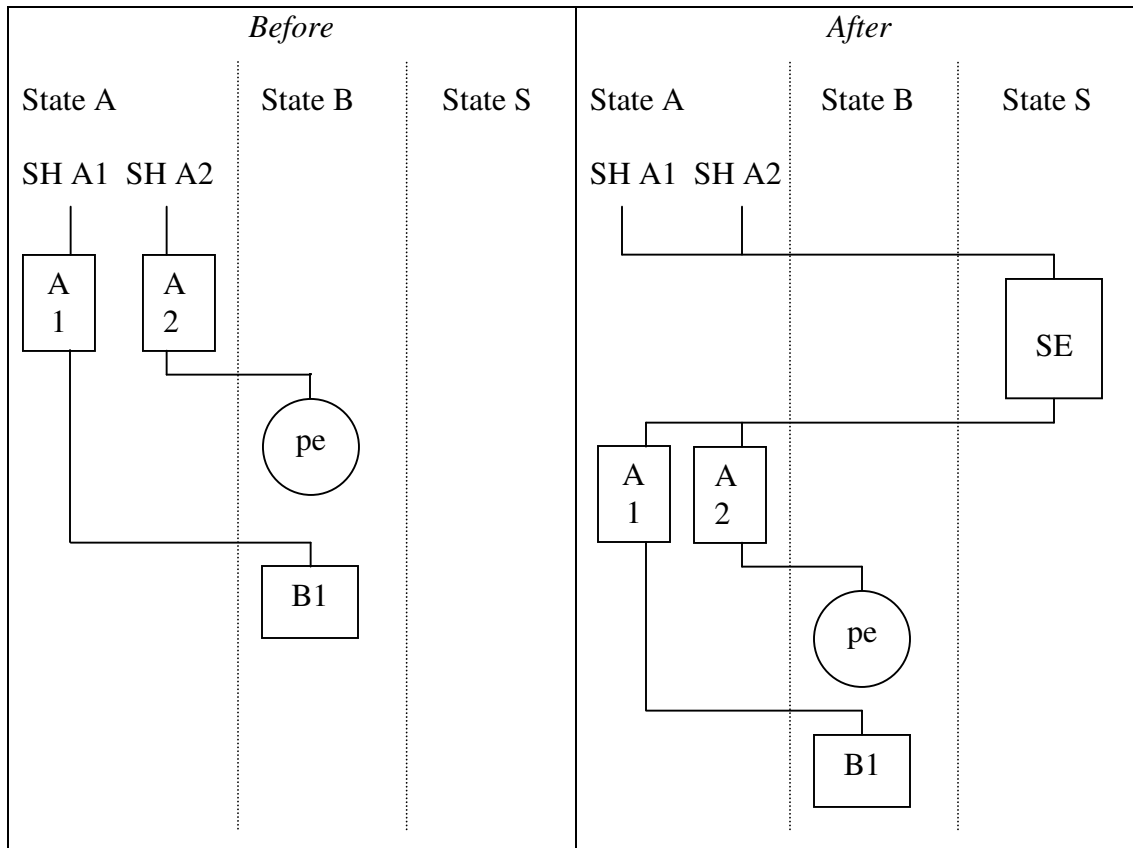
- b) Are there any provisions for the valuation for tax purposes in Member State S of the shares issued to SH A and SH B? Do the shares have to be valued at the book value of the shares exchanged by the shareholder or at a higher value?

*See Case 3, I(b).*

## CASE 5

### Formation of a Holding – SE

(Art. 2 par. 2(b) jo. Art. 32, Art. 33, and Art. 34 Reg. 2157/2001)



#### Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A1, A2, and B1 are existing companies
- pe is an existing permanent establishment of A2 in Member State B
- SE is a new company
- A1, A2, and B1 are public or private limited-liability companies (see Annex II to Reg. 2157/2001)
- State A, State B, and State S are EU Member States
- A1 and A2:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
- B1:
  - formed under law of Member State B

- registered office in Member State B
  - head office in Member State B
- SE:
  - formed under law of Member State S
  - registered office in Member State S
  - head office in Member State S
  - will be covered by the EC Merger Directive

### Transactions

- SE:
  - will be regarded as public limited-liability company governed by the law of Member State S
  - acquires holding in A1 and A2
  - such that it obtains more than 50% of the permanent voting rights in A1 and A2
  - in exchange for shares in SE
  - issued to the shareholders of A1 and A2

### Questions

1) Assume Member State A is your country

#### Tax effects for SH A2 in Member State A

a) Will the issue of shares by SE to SH A2 in exchange for shares in A2 give rise to any taxation of the income, profits or capital gains of SH A2 or is there roll-over relief?

*See Case 3, 2(a).*

b) Will the answer to the above question be different in the case of:

i) SH A2 being an individual shareholder not owning a substantial interest?

*See Case 3, 2(b).*

ii) SH A2 being an individual shareholder owning a substantial interest?

*See Case 3, 2(b).*

iii) SH A2 being an individual entrepreneur?

*See Case 3, 2(b).*

iv) SH A2 being a corporate shareholder?

*See Case 3, 2(b).*

2) Assume Member State S is your country

Tax effects for SE in Member State S

a) Are there any provisions for the valuation for tax purposes in Member State S of the shares of A1 and A2 acquired by SE? Do the shares have to be valued at the book value of the exchanging shareholder or at a higher value?

*See Case 4, 4(a).*

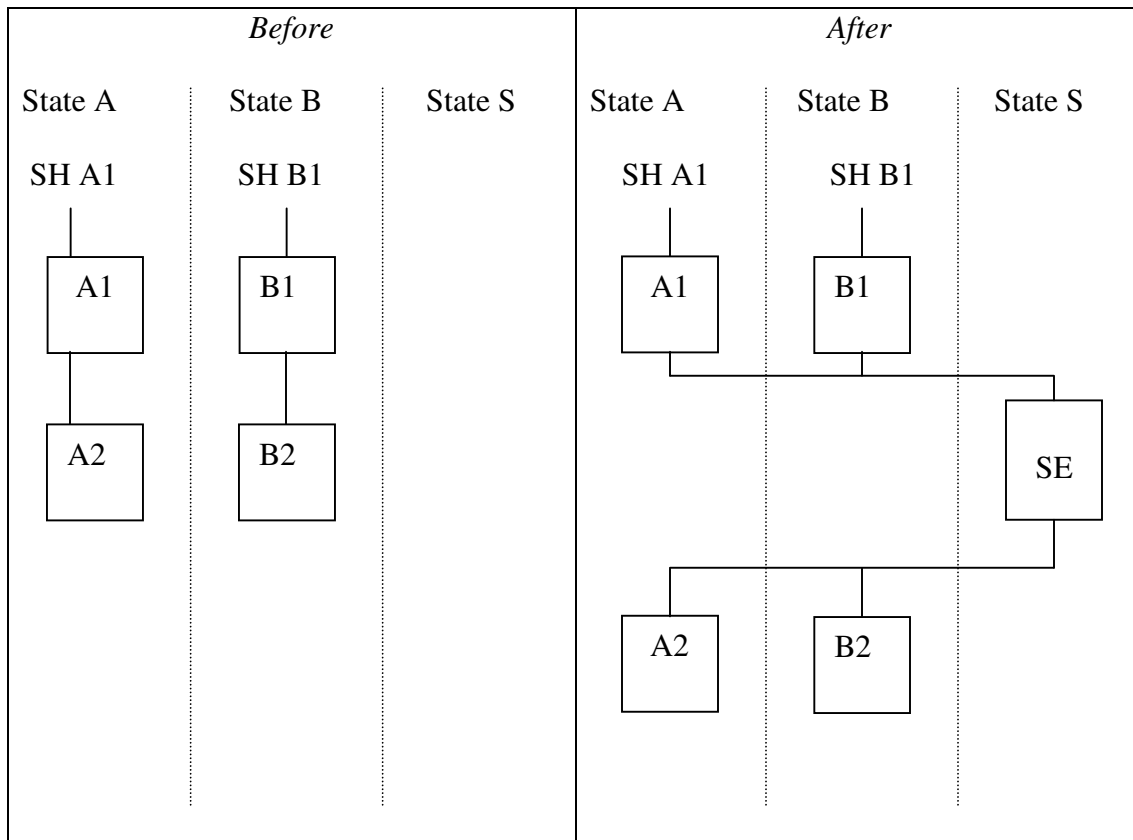
b) Are there any provisions for the valuation for tax purposes in Member State S of the shares issued to SH A1 and SH A2? Do the shares have to be valued at the book value of the shares exchanged by the shareholder or at a higher value?

*See Case 4, 4(b).*

## CASE 6

### *Formation of a Subsidiary–SE by exchange of shares*

(Art. 2 par. 3(a) jo. Arts. 35 and 36 Reg. 2157/2001)



#### Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A1, A2, B1, and B2 are existing companies
- SE is a new company
- A1 and B1 are companies or firms within the meaning of Art. 48 par. 2 of the Treaty establishing the European Community or other legal bodies governed by public or private law (Art. 2 par. 3 Reg. 2157/2001)
- State A, State B, and State S are EU Member States
- A1 and A2:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
- B1 and B2:
  - formed under law of Member State B

- registered office in Member State B
- head office in Member State B
  
- SE:
  - formed under law of Member State S
  - registered office in Member State S
  - head office in Member State S
  - will be covered by the EC Merger Directive

### Transactions

- A1 and B1:
  - form a subsidiary SE by way of contributing their subsidiaries A2 and B2 respectively to SE
- SE:
  - will be regarded a public limited-liability company governed by the law of Member State S
  - will acquire the shares in A2 and B2 in exchange for shares issued to A1 and B1

### Questions

- 1) Assume Member State A is your country

#### Tax effects for A1 in Member State A

- a) Will the issue of shares by SE to A1 in exchange for shares in A2 give rise to any taxation of the income, profits or capital gains of A1 or is there rollover relief?

*In general, there is rollover relief under Sec 16(1) and Sec 20 UmgrStG. If A1 receives shares in SE qualifying for the international participation exemption in terms of Sec 10(2) KStG (ie at least 25%), there is a fictitious write off (Sec 20(7) UmgrStG. In case the participation is sold "hidden reserves" are taxable.*

- 2) Assume Member State S is your country

#### Tax effects for SE in Member State S

- a) Are there any provisions for the valuation for tax purposes in Member State S of the shares of A2 and B2 acquired by SE? Do the shares have to be valued at the book value of the exchanging shareholder or at a higher value?

*Sec 18 UmgrStG refers to Sec 17 UmgrStG in this respect. Under Sec 17(1) UmgrStG, the shares in A 2 and B 2 have to be valued at the acquisition cost*



*attributable to shares exchanged at the level of the exchanging shareholder.  
There are two exceptions to this rule:*

- under Sec 16(2) UmgrStG, a step-up is possible if the exchange of shares is subject to tax in the Member State A or B and if a tax treaty between Austria and the Member State A or B providing for the credit method has been concluded (or a similar domestic measure for the elimination of double taxation exists); and*
- under Sec 17 (2) UmgrStG, a voluntary step-up is possible by filing an application with the tax authorities.*

*If the shares hold by SE in A2 and B2 qualify for the international participation exemption in terms of Sec 10(2) KStG (ie at least 25%) the “hidden reserves”, ie difference between their fair market value and their book value (ie acquisition cost), is deemed a fictitious write-off (Sec 18(4) UmgrStG). In case of alienation of the shares, the difference is taxable. This will be the case if there is neither a step-up under Sec 16(2) UmgrStg nor such under Sec 17(2) UmgrStG. In practise, the tax authorities did not follow such an interpretation of Sec 18(4) UmgrStG.*

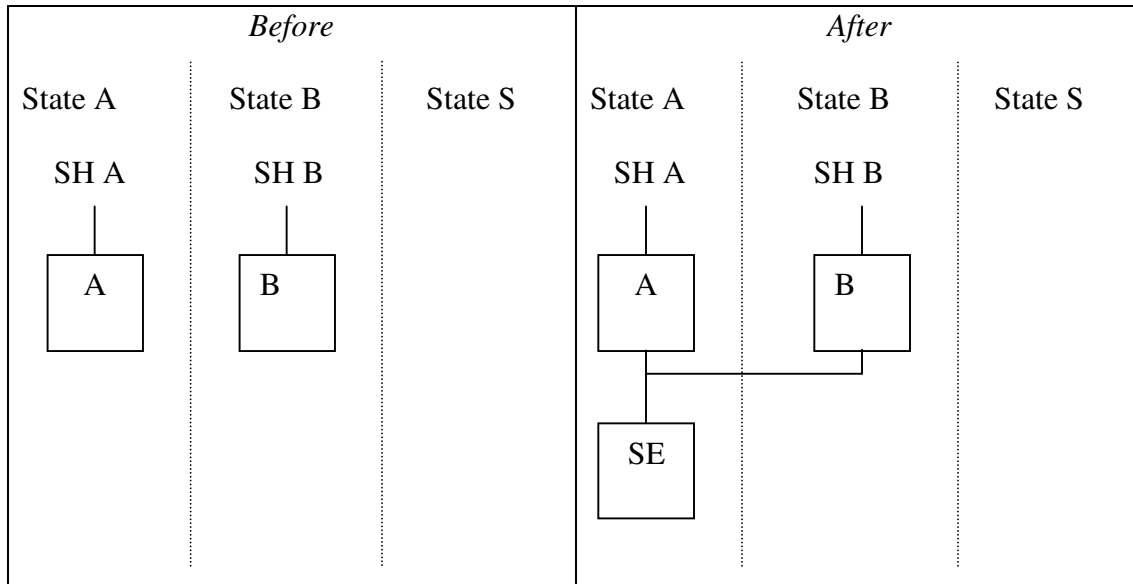
- b) Are there any provisions for the valuation for tax purposes in Member State S of the shares issued to A1 and B1? Do the shares have to be valued at the book value of the shares exchanged by the shareholder or at a higher value?

*According to Sec 20 UmgrStG, the shares issued to A1 and B1 are valued at their tax book value, acquisition cost or fair market value (Secs 16 and 17 UmgrStG) (see above).*

## CASE 7

### *Formation of a Subsidiary–SE by contribution of cash*

(Art. 2 par. 3(a) jo. Arts. 35 and 36 Reg. 2157/2001)



#### Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A, and B are existing companies
- SE is a new company
- A and B are companies or firms within the meaning of Art. 48 par. 2 of the Treaty establishing the European Community or other legal bodies governed by public or private law (Art. 2 par. 3 Reg. 2157/2001)
- State A, State B, and State S are EU Member States
- A:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
- B:
  - formed under law of Member State B
  - registered office in Member State B
  - head office in Member State B
- SE:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
  - will be covered by the EC Merger Directive

## Transactions

- SE:
  - will take the form of an SE
  - will be regarded a public limited-liability company governed by the law of Member State A
- A and B:
  - form a subsidiary SE

## Questions

It is generally assumed that an SE will for domestic corporate income tax purposes be treated as a corporate entity. However, there may be differences between the treatment of an SE and other legal entities, if certain possibilities, e.g. participation exemption or fiscal unity etc. are only allowed between certain types of legal entities and the SE is not yet included. If relevant, please mention some of these situations in your answers to the following questions.

- 1) Assume Member State A is your country

### Tax effects for A in Member State A

Will there be any tax effect for A in Member State A as a consequence of the formation of the subsidiary SE in Member State A?

*The provisions of UmgrStG do not cover the formation by contribution of cash. Although the contribution of cash does not trigger income or corporate income tax consequences, capital transfer tax of 1% of the contributed cash will be levied.*

*As for the other questions raised above see our general remarks in the Introduction.*

- 2) Assume Member State B is your country

### Tax effects for B in Member State B

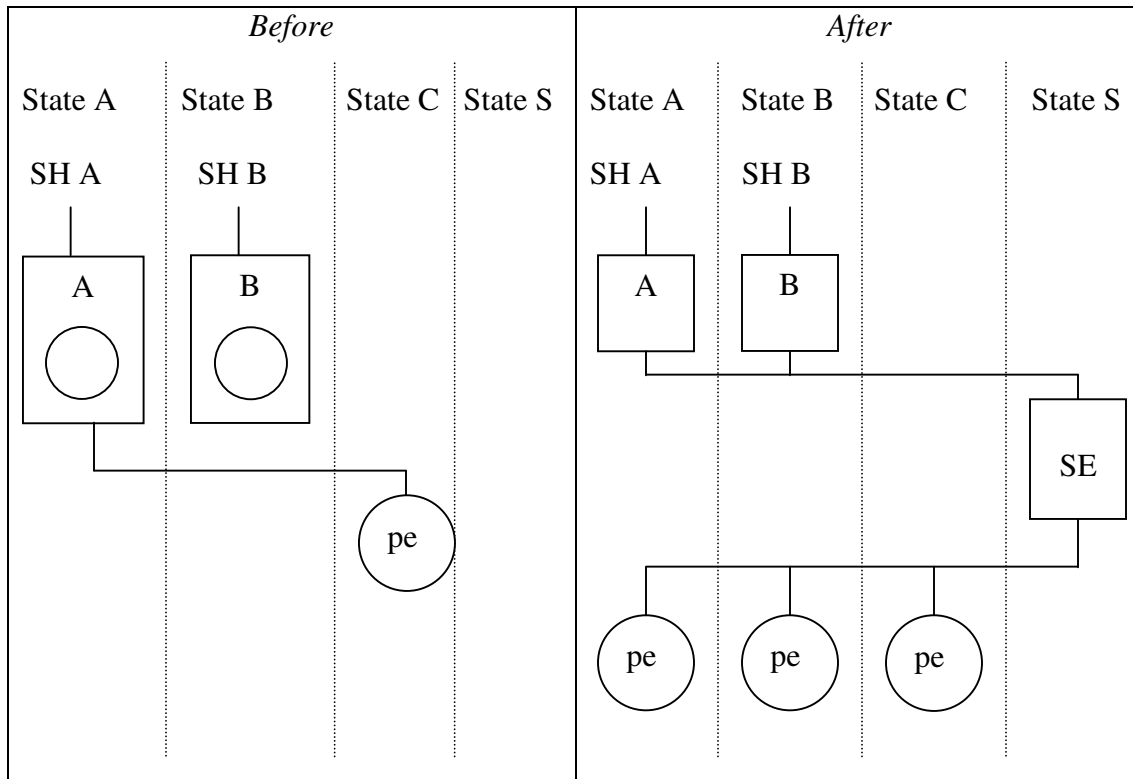
Will there be any tax effect for B in Member State B as a consequence of the formation of the subsidiary SE in Member State A?

*There will not be any immediate tax effect.*

## CASE 8

### *Formation of a Subsidiary–SE by transfer of assets*

(Art. 2 par. 3(a) jo. Arts. 35 and 36 Reg. 2157/2001)



### Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A, and B are existing companies
- SE is a new company
- A and B are public or private limited-liability companies (see Annex II)
- A and B are companies or firms within the meaning of Art. 48 par. 2 of the Treaty establishing the European Community or other legal bodies governed by public or private law
- A has a permanent establishment in State C
- State A, State B, State C and State S are EU Member States
- A:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A

- B:
  - formed under law of Member State B
  - registered office in Member State B
  - head office in Member State B
- SE:
  - formed under law of Member State S
  - registered office in Member State S
  - head office in Member State S
  - will be covered by the EC Merger Directive

### Transactions

- SE:
  - will take the form of an SE
  - will be regarded a public limited-liability company governed by the law of Member State S
- A (and B):
  - form a subsidiary by way of contributing their branches in Member State A (and B respectively) to SE in exchange for the issue of shares by SE to A (and B respectively)
- A:
  - will transfer its permanent establishment in Member State C to SE in exchange for the issue of shares by SE to A

*Remark: It is assumed that the branches in Member State A and B and the permanent establishment in Member State C qualify as business or parts of a business in terms of Sec 12(2)(1) UmgrStG.*

### Questions

1) Assume Member State A is your country

#### Tax effects for A and SE in Member State A

- a) Will the transfer of assets give rise to any taxation of capital gains (= real value of the assets and liabilities minus their value for tax purposes) or is there roll-over relief?

*Branch in Member State A: In general, there is roll-over relief under Sec 16(1) UmgrStG.*

*Permanent establishment in Member State C: In general, there is roll-over relief (Sec 16(1) UmgrStG). The rule of Sec 16 (2) UmgrStG provides for the possibility of a taxable step-up if the exchange of shares is subject to tax in Member State C*

*and if there is a tax treaty between Austria and Member State C that provides for credit method (or a similar domestic measure for the elimination of double taxation exists).*

*As the shares of A in SE qualify for the international participation exemption in terms of Sec 10(2) KStG (ie at least 25%) there is a fictitious write-off that amounts to “hidden reserves” attributable to the branch at the time of transfer (Sec 20(7) UmgrStG). In case of alienation of the shares the write-off amount will be taxable and therefore, the participation is not tax exempt to this extent. I assume that this would be the case only if there is a tax treaty between Austria and Member State C that provides for the credit method or a similar domestic measure for the elimination of double taxation exists.*

- b) May provisions or reserves which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State A be taken over with the same roll-over relief by the permanent establishment of SE in Member State A?

*Yes.*

- c) Are there any provisions in the legislation of Member State A for the valuation for tax purposes of the shares in SE acquired by A?

*Under Sec 20 UmgrStG, the shares issued to A are valued on the same basis and at the same value as the assets transferred (see above).*

*Transfer of branch in Member State A: As the shares of A in SE qualify for the international participation exemption in terms of Sec 10(2) KStG (ie at least 25%) there is a fictitious write-off that amounts to “hidden reserves” attributable to the branch at the time of transfer (Sec 20(7) UmgrStG). In case of alienation of the shares the write-off amount will be taxable and therefore, the participation is not tax exempt to this extent.*

*Transfer of permanent establishment in Member State C: As the shares of A in SE qualify for the international participation exemption in terms of Sec 10(2) KStG (ie at least 25%) there is a fictitious write-off that amounts to “hidden reserves” attributable to the permanent establishment at the time of transfer (Sec 20(7) UmgrStG). In case of alienation of the shares the write-off amount will be taxable and therefore, the participation is not tax exempt to this extent. I assume that this would be the case only if there is a tax treaty between Austria and Member State C that provides for the credit method or a similar domestic measure for the elimination of double taxation exists.*

- d) Will SE's permanent establishment in Member State A be allowed to take over the losses of A which have not been exhausted for tax purposes? (If SE would be a company resident in Member State A, would it then be allowed to take over these losses?)

*In both cases, the permanent establishment of SE and the company situated in Member State A, would be allowed to take over the losses of A attributable to the branch transferred under Sec 21 UmgrStG. There are, however, certain restrictions (Sec 21(1) UmgrStG):*

- the transfer of the branch has to be made at the tax book value (ie no-step-up under Sec 16(2) UmgrStG); and*
- loss carry forwards transferred must be attributable to the business transferred and the business must exist at the transfer date.*

*Further restrictions are provided for by making reference to Sec 4(1)(c) and (d) UmgrStG:*

- the business of the transferring (acquiring) company after the transfer must be basically and in economic terms comparable to the business of the transferring (acquiring) company prior to the merger (Sec 4(1)(c) UmgrStG); and*
- in case of a transfer between related companies, the amount of losses incurred by the subsidiary must be reduced by the amount of the write off claimed by the parent company at any time prior to the merger (Sec 4(1)(d) UmgrStG).*

*With regard to the losses of the acquiring company, the following must be considered (Sec 21(2) UmgrStG):*

- losses incurred by the acquiring company may be deducted insofar as the respective business (or a part thereof or assets) still exists at the transfer date (Sec 4(1)(b) UmgrStG); and*
- the business of the transferring (acquiring) company after the transfer must be basically and in economic terms comparable to the business of the transferring (acquiring) company prior to the transfer (Sec 4(1)(c) UmgrStG);*

*In addition, reference is made to Sec 4(2) UmgrStG (Sec 21(3) UmgrStG) in that a loss carry forward is not available in the event of a significant change in the ownership of a company, in its organisational or economic structure. Thus, if the economic identity of the acquiring or the transferring company is lost losses incurred by the respective company may not be set off. The restriction is not applicable if the changes are aimed at the improvement of the business structure (eg rationalization measures) at the level of the acquiring company.*

- e) Will Member State A renounce any right to tax the permanent establishment in Member State C?

*De facto, yes, as SE will be subject to corporate income tax on a source basis only (ie limited tax liability). For details, see Case 1, 1(a).*

- f) Will Member State A reinstate in the taxable profits of A such losses of the permanent establishment in Member State C as have been set off against the taxable profits of A in Member State A and which have not been recovered (see art. 10 par. 2 of the EC Merger Directive)?

*There is no explicit provision in Austrian tax law covering this issue. The reason for the lack of such a provision may be that for a long time Austria allowed to set off losses of foreign permanent establishments only if a tax treaty has been concluded between Austria and the foreign country providing for the credit method or in a non-treaty situation.*

*In a recent decision, however, the Austrian Supreme Administrative Court (VwGH E 25.9.2001, 99/14/0217) held that losses of a foreign permanent establishment are deductible in Austria even if the tax treaty provides for the exemption method. To avoid a double dip, the court stated that if in the following years the permanent establishment losses are covered by the permanent establishment profits, such profits are only exempt by the treaty to the extent they have not been set off against the permanent establishment losses of the previous years.*

*By applying this decision to the question at issue one could argue that Austria could reinstate such losses in the taxable profits. As has been said, however, there is no explicit provision covering this issue.*

- g) Or will Member State A tax profits or capital gains of the permanent establishment resulting from the transfer of assets?

*See Case 8, 1(a).*

- h) If question g) is answered affirmatively, will Member State A give relief for the notional tax charged on these profits or capital gains by Member State C, assuming that Member State C would have levied tax (see art 10 par. 2 of the EC Merger Directive)?

*See Case 8, 1(a).*



2) Assume Member State S is your country

Tax effects for SE in Member State S

- a) What is the value for tax purposes that SE has to attribute to the assets and liabilities of the permanent establishments in Member States A, B and C that is transferred to SE as part of the merger?

*In general, this will be the tax book value under Sec 16(2) UmgrStG although there is a possibility for a taxable step-up under Sec 16(2) UmgrStG if the exchange of shares is subject to tax in Member States A, B and C and if there is a tax treaty between Austria and Member States A, B and C providing for the credit method or a similar measure for the elimination of double taxation exists on the domestic level.*

Tax effects for A as shareholder of SE in Member State S

- b) Is there any provision in the tax legislation of Member State S that affects A as shareholder of SE?

*According to Sec 20 UmgrStG, the shares issued to A as a shareholder of SE are valued on the same basis and at the same value as the assets transferred (see above). It has to be noted also, that A will become subject to limited tax liability in Austria (assuming they own a substantial interest in SE, ie at least 1%). Whether or not they will be taxed upon a sale of the shares in SE depends on the applicable tax treaty.*

3) Assume Member State C is your country

Tax effects for A and SE in Member State C in respect of its permanent establishment in Member State C

- a) Will the transfer of assets give rise to any taxation of capital gains (= real value of assets & liabilities transferred minus their value for tax purposes) or is there roll-over relief?

*In general, there is roll-over relief under Sec 16(1) UmgrStG although there is a possibility for a taxable step-up under Sec 16(2) UmgrStG if the exchange of shares is subject to tax in Member State A and if there is a tax treaty between Austria and Member State A providing for the credit method or a similar measure for the elimination of double taxation exists on the domestic level.*

- b) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State C, be taken over with the same roll-over relief by the permanent establishment of SE in Member State C?

*Yes.*

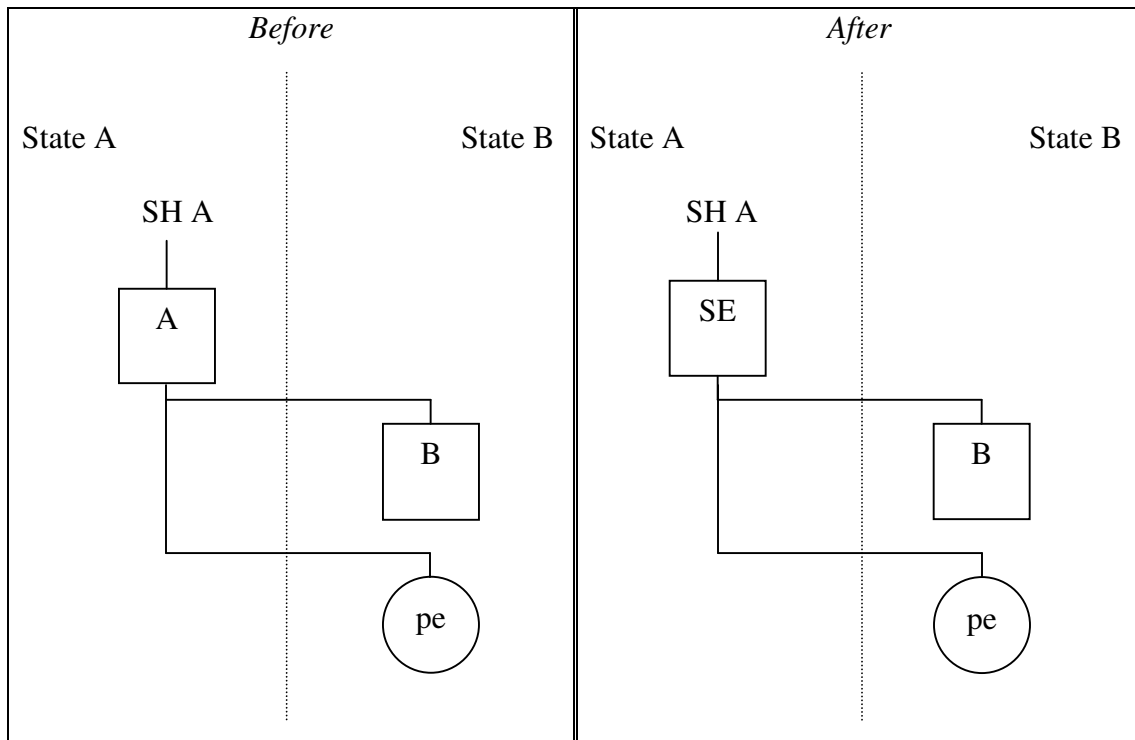
- c) Will SE's permanent establishment in Member State C be allowed to take over the losses of A's permanent establishment that have not been exhausted for tax purposes? If SE would be a company resident in Member State C, would it then be allowed to take over these losses?

*In general, the permanent establishment of SE will be allowed to take over the losses of the permanent establishment of A under Sec 21 UmgrStG (see further Case 8, 1(d)). As a general rule, however, the permanent establishment loss can only be deducted if it exceeds the worldwide income of SE and the requirements of Sec 102(2)(2) EStG are met.*

## CASE 9

### *Transformation of public limited-liability company into an SE*

(Art. 2 par. 4 jo. Art. 37 Reg. 2157/2001)



#### Facts and assumptions

- SH = shareholder(s), resident in the respective country in which SH is situated
- A and B are existing companies
- pe is an existing permanent establishment
- A and B public limited-liability companies (see Annex I of Reg. 2157/2001)
- State A and State B are EU Member States
- A:
  - formed under law of Member State A
  - registered office in Member State A
  - head office in Member State A
- B:
  - formed under law of Member State B
  - registered office in Member State B
  - head office in Member State B

## Transactions

- A will be transformed into an SE, governed by the law of Member State A (Pursuant to Art. 37 par. 2 Reg., the transformation shall not result in the winding up of A or in the creation of a new legal person. However, the Regulation itself does not give guidance with regard to taxation.)

## Questions

*Remark: The mere transfer of the legal personality of A into SE does no change the tax characterization of A in any respect. Therefore, the transformation is without any tax consequences.*

- 1) Assume Member State A is your country

### Tax effects for A in Member State A

- a) Will the transformation of A into an SE give rise to any taxation of capital gains (= real value of assets and liabilities transferred minus their value for tax purposes) or is there roll-over relief for the business carried on in Member State A, or in Member State B through a permanent establishment?

*See remark above.*

- b) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State A, be carried over to SE in Member State A?

*See remark above.*

- c) Will SE be allowed to take over the losses of A that have not been exhausted for tax purposes?

*See remark above.*

### Tax effects for SH A in Member State A

- d) Will there be any effect for SH A because of the transformation of its subsidiary company A into an SE?

*See remark above.*

- e) Will the answer to question d) be different in the following situations:

*No to all.*

- i) SH is a corporate shareholder?
  - ii) SH is an individual shareholder not owning a substantial interest?
  - iii) SH is an individual shareholder owning a substantial interest?
  - iv) SH is an individual entrepreneur?
- 2) Assume Member State B is your country

Tax effects for the shareholder of B in Member State B

- a) Will there be any effect for the shareholder of B because of the transformation of its parent company A into an SE?

*See remark above.*

Tax effects for A and SE in Member State B

- b) Will A be subject to any taxation of capital gains (=real value of assets and liabilities minus their value for tax purposes) or is there roll-over relief?

*See remark above.*

- c) If not, what is the value for tax purposes that SE has to attribute to the assets and liabilities of the permanent establishment in Member State B?

*See remark above.*

- d) May provisions and reserves, which are partly or wholly exempt from tax and which are not derived from permanent establishments outside Member State B, be taken over with the same roll-over relief by the permanent establishment of SE in Member State B?

*See remark above.*

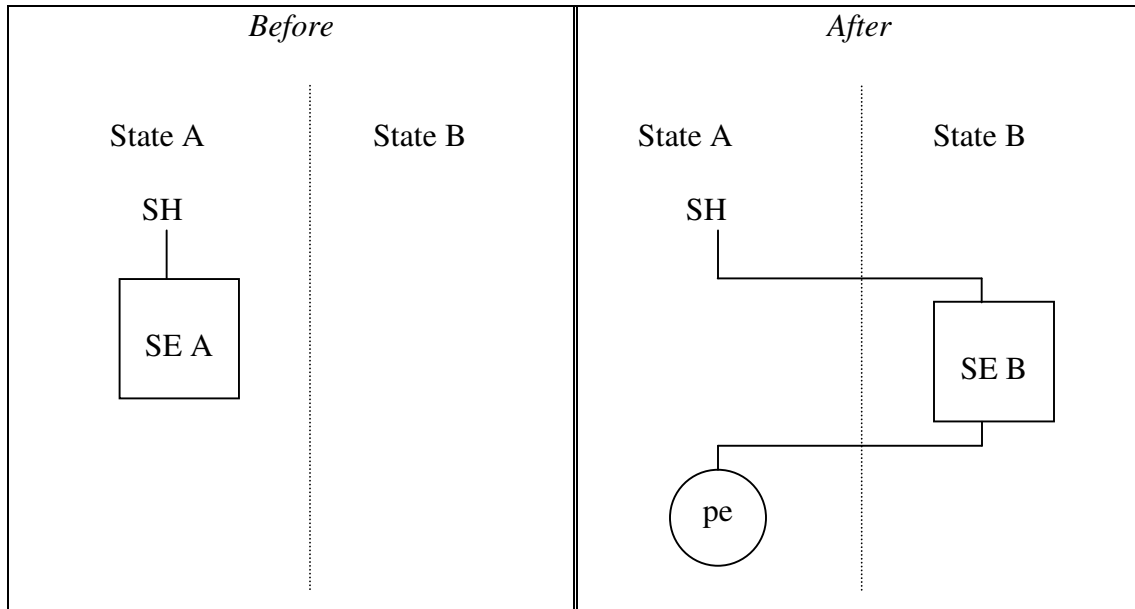
- e) Will SE's permanent establishment in Member State B be allowed to take over the losses of A's permanent establishment that have not been exhausted for tax purposes?

*See remark above.*

## CASE 10

### *Transfer of registered office of an SE*

(Art. 8 par. 1 jo. Art. 37 Reg. 2157/2001)



#### Facts and assumptions

- SE is an existing SE
- State A and State B are EU Member States
- SE A:
  - formed under the law of Member State A
  - registered office in Member State A
  - head office in Member State A
- SE B:
  - statutes are amended to conform to the law of Member State B
  - registered office in Member State B
  - head office in Member State B

#### Transactions

- registered office and head office of SE are transferred to Member State B (pursuant to Art. 8 Reg. 2157/2001 such a transfer shall not result in the winding up of SE or in the creation of a new legal person)

## Questions

*Remark: There is up to date neither tax legislation nor administrative guidance with respect to this case. Thus, the following is based on the actual law and practice.*

### 1) Assume Member State A is your country

#### Tax effects of the transfer for SE

##### a) Does the transfer entail a winding up of SE for tax purposes?

*No. Basically, SE changes its tax status from unlimited to limited Austrian corporate tax liability. Thus, it becomes taxable on its Austrian source income only.*

##### b) What are the tax consequences in case of a winding up of SE?

*In principle, none. But see below.*

##### c) Does it make a difference whether or not a permanent establishments of SE B remains in Member State A?

*Yes; as in such a case it has to be assumed that the assets of SE are transferred from Member State A to Member State B. If the permanent establishment does not remain in Member State A Sec 6(6) EStG provides for a taxation of the “hidden reserves” of the permanent establishment assets. For the assets not attributable to the permanent establishment, it will have to be assumed that such a transfer subject to Sec 6(6) EStG will take place when the registered office and head office of SE are transferred to Member State B*

##### d) If after the transfer of the registered office, SE B will have a permanent establishment in Member State A, can SE B take over the provisions and reserves which are partly or wholly exempt from tax with the same roll-over relief?

*Yes.*

##### e) If after the transfer of the registered office, SE B will have a permanent establishment in Member State A, can SE B's permanent establishment in Member State A take over the losses of SE A that have not been exhausted for tax purposes?

*In principle, yes. It has to be noted that the tax status changes from unlimited corporate tax liability to limited corporate tax liability.*

Tax effects of the transfer for SH

- f) What are the tax effects for SH in case the transfer results in a winding up of SE for tax purposes?

*The transfer does not result in a winding up of SE for tax purposes.*

- g) Is the answer to 1f) different if:

*No, to all.*

- i) SH is a corporate shareholder?
  - ii) SH is an individual shareholder?
  - iii) SH is an individual not owning a substantial interest?
  - iv) SH is an individual owning a substantial interest?
  - v) SH is an individual entrepreneur?
- h) Are there any effects for tax purposes if the transfer of the registered office is not considered as a winding up for tax purposes?

*Yes (see below).*

- i) Is the answer to 1h) different if:
- i) SH is a corporate shareholder?

*Dividends from SE A were subject to the domestic participation exemption under Sec 10(1) KStG. This exemption does not require a minimum participation or minimum holding period. However, a capital gain would have been subject to tax. Dividends received from SE B are subject to the international participation exemption, which requires a participation of at least 25% and a minimum holding period of two years (for the calculation also the holding period of the participation in SE A will be taken into account). If these requirements can be met, also capital gains deriving from the sale of the participation should be exempt.*

- ii) SH is an individual shareholder?

*Dividends received from a domestic corporation are only taxed at a rate of 25%. Foreign dividends (i.e. dividends from SE B) are subject to the progressive tax rate up to 50%. Whether or not such a differentiation is in line with EU law is heavily discussed in Austria and will soon be decided by the ECJ.*



- iii) SH is an individual not owning a substantial interest?

*Assuming that the amount of the participation does not change, there are no consequences.*

- iv) SH is an individual owning a substantial interest?

*Assuming that the amount of the participation does not change, there are no consequences.*

- v) SH is an individual entrepreneur?

*Capital gains deriving from the sale of a domestic corporation are subject to only 50% of the applicable income tax rate. This tax rate reduction is applicable in the case of a sale of a foreign corporation as well.*

- 2) Assume Member State B is your country

Tax effects of the transfer for SE

- a) If SE is considered to be a new company, how should the assets and liabilities of SE be valued?

*There are no specific provisions as for the valuation of the assets. Therefore general rules must be applied. Domestic assets will be valued according to their book value. Foreign assets that will be transferred to B will be valued according to their fair market value at the time of the transfer (Sec 6(6) EStG. Foreign assets, which are not transferred to B, will be valued according to their book value.*

Tax effects of the transfer for SH

- b) Are there any tax effects for SH in case the transfer results in a formation of a new SE in your country? For example, with regard to the valuation of the shares in SEB?

*SH will be subject to limited tax liability in Austria. Therefore dividends paid by SE B will be subject to withholding tax of 25% id not exempt according to the parent/subsidiary directive or reduced by a tax treaty. Capital gains deriving from a sale of the participation will also be subject to limited tax liability if the shareholding amounts to at least 1%. In this case SH gets a step up in basis for the participation in SE B when the registered office is transferred form A to B. However, the taxation right for capital gains shall in general be eliminated by an applicable tax treaty.*