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Summary

Company reorganisations are becoming more and more frequent in order to stay competitive in an international market place and to adapt to the changing economic environment. In this matter, taxation is one of the most important issues and is often a barrier to restructuring operations which is the consequence of the large variation in the effective tax rates in the Community. Therefore, the creation of a level playing field is seen as important. In the European Single Market, it should not make a difference if companies from one Member State, or more than one Member State are involved in a reorganisation.

The main problem with reorganisations is the potential loss of taxing jurisdiction by the “home” State of the company’s capital. Without having special rules reserves hidden in the assets would crystallise thus preventing the reorganisation taking place. Moreover, the Community had to balance the competing financial interests of the Member States and of the companies conducting cross-border operations keeping in mind the aim of reaching tax neutrality.

The solution adopted by the Community was the Merger Directive of 23 July 1990. It postpones the tax charge to a later disposal. This was a historical breakthrough in the history of the Community because it was the first time that the Member States agreed a significant piece of direct tax legislation in the Community.

The scheme of the Merger Directive is to provide a deferral of taxation in certain situations involving (i) mergers, (ii) divisions, (iii) transfers of assets and (iv) exchange of shares. The Merger Directive was incorporated into Swedish law and came into force on 1 January 1995 as Sweden joined the European Community.

Preface

This essay was written as a contribution to the Wintercourse Seminar 2003, which was held on April 4 –11 at Stockholm School of Economics in Sweden. The Wintercourse Seminar is organised by EUCOTAX (European Universities Cooperating on Taxes). EUCOTAX is based on the desire of the participating universities (Barcelona, Leuven, London, Paris, Rome, Stockholm, Tilburg, Osnabrück, Vienna and Washington) to set up a permanent structure in order to stimulate the instruction in and research on European aspects of tax law.

This essay was based upon a questionnaire which provided a checklist for the participants working with cross-border reorganisations. The scope of the paper is thus set in regard to the questionnaire.

In general every chapter deals with one specific area and some of the specific subjects are described more briefly than others in order to better emphasize the characteristic items in regard to Swedish rules. Hence, some of the introductory issues will only give a brief understanding in order for non-Swedish readers to better understand the peculiarities in later chapters.

Abbreviations

CFC	Controlled Foreign Company
EC	the European Community
EEA	the Agreement on European Economic Area
EEC	European Economic Community
EU	European Union
GET	Guide to European Taxation
IBFD	International Bureau of Fiscal Documentation
IGOL	the EC-Reorganisation Tax Law, <i>Lag (1994:1854) om inkomstbeskattning vid gränsöverskridande omstruktureringar inom EG</i>
ITA	the Income Tax Act, <i>Inkomstskattelagen (1999:1229)</i>
NJA	the Supreme Civil Court Rulings
OECD	Organisation for Economic Cooperation and Development
OJ	Official Journal
Prop	Proposition (government bill)
RSV	Riksskatteverket (the National Tax Board)
RÅ	the Supreme Administrative Court rulings
SFS	Svensk Författningssamling
SIL	<i>Lag (1947:576) om statlig inkomstskatt</i>
SOU	Statens offentliga utredningar (governmental official reports)
VAT	Value Added Tax

1 Background

1.1 Introduction

As many companies today consider the whole EU as their "home market" and accordingly seek to establish effective pan-European business structures, this results in EU-wide reorganisation and centralisation of business functions within a group of companies.

Cross-border reorganisation is one of the few areas of direct taxation where there has been harmonisation at Community level. The relevant Community instrument is Council Directive 90/434/EEC on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States, more commonly known under the name "the Merger Directive".¹

In most cases, reorganisations are initiated in order to help a group of companies, or other types of related companies, to function more effectively. Consequently, these activities affect the taxation of the involved companies. Depending on the geographical coverage and corporate structure, its overall tax rate can be significantly affected by the range of rules across the EU.

It is a well-known fact that tax compliance costs for international and cross-border activities are substantial. Moreover, such costs are regressive to size, which means that they hit small and medium-sized enterprises harder than larger.²

The purpose of the EU Merger Directive, which came into force in 1990, is hence to harmonise tax treatments and prevent tax obstacles in relation to cross-border reorganisations. However, today companies within the EU still argue that their

¹ Council Directive 90/434/EEC of 23 July 1990 on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States, Official Journal L 225, 20.08.1990.

² *Company taxation in the internal market*, COM (2001) 582, p.49.

perception of the EU as their "home market" generally does not correspond to a uniform tax reality.³

The Merger Directive was incorporated into Swedish law by enacting specific national legislation, the *EC-Reorganisation Tax Law*⁴. The law came into force on 1 January 1995 as Sweden joined the European Community. This law is now abolished and the provisions are integrated in the *Income Tax Act (ITA)*⁵ through Ch. 37 (mergers and divisions), Ch. 38 (transfer of assets) and Ch. 49 (exchange of shares).

1.1.1 Purpose

This paper will give a general report of the concept of cross-border reorganisations in Swedish law. The purpose is to give an overview of the Swedish legislation and, in relevant areas, its coherence with the EU Cross-border Merger Directive.

1.1.2 Terminology

To avoid any confusion, the same terminology as in the Merger Directive (Article 2) will be used when it is possible. Swedish legislation will first and foremost be recited in English.

1.1.3 Method

The method that will be used in this thesis is legal dogmatic. The material that will be studied includes written law, cases, preparatory works and legal literature and articles.⁶

³ COM (2001) 582, p.6.

⁴ *Lag om inkomstbeskattning vid gränsöverskridande omstruktureringar inom EG*, (IGOL).

⁵ *Inkomstskattelagen (1999:1229)*, (ITA).

⁶ The hierarchy of Swedish legal sources is as follows: written law, preparatory work and case law. It is also possible to refer to doctrine in order to interpret and clarify a vague legislation.

1.1.4 Limitations

The focus of this paper will be reorganisations from a Swedish taxation perspective, both domestic and international. The main subject is direct- and indirect income tax in regard to limited liability companies (*aktiebolag*); other forms of enterprises will however be discussed when necessary. The Swedish rules regarding taxation of owners of closely held companies will not be considered, except when it is distinctly stated.

It is not the purpose to investigate the implications of the Cross-border Merger Directive on other countries within the EU, or to discuss Swedish tax treaties with other Member States.

1.1.5 Disposition of the Paper

The first chapter of this paper contains a brief introduction to the subject as well as some basic information about Swedish company law and Swedish tax law. Chapter 1 also includes a brief introduction to the major forms of reorganisations and the coherence between the Merger Directive and Swedish national legislation as well as the differences between company law and tax law.

Chapter 2, 3 and 4 cover the Swedish legislation on different forms of domestic and international reorganisations (mergers and divisions, transfer of assets and exchange of shares) and how these reorganisations are treated for tax purposes.

Chapter 5 deals with some specific questions on reorganisations and how they are treated for tax purposes. This includes how a situation is handled if the transferring company owns shares in the receiving company or if the receiving company own shares in the transferring companies. Aforementioned reorganisations include implications on a company law level and at a tax law level. The transfer of a branch to another Member State and the transfer of the seat of a company, to another Member State are furthermore discussed. The last part of chapter 5 compares the Swedish anti-abuse provisions with Article 10 in the Merger Directive.

In chapter 6 three questions regarding non-income tax are discussed. The questions include the treatment of reorganisations in regard to value-added tax, capital contributions and stamp taxes.

Chapter 7 concludes the document with some remarks regarding the importance of a harmonisation between tax law and company law, on a national level as well as a Community level. The benefit of a full implementation in the Member States of the Merger Directive, which would cover both domestic and international reorganisations, is also emphasised.

1.2 The Swedish Internal International Company Taxation

1.2.1 Company Law and Limited Liability Companies

Swedish company law regarding enterprises consists of four main forms of legal co-operation: limited liability companies (limited by shares), partnerships, associations and foundations. This essay will predominantly discuss limited liability companies from a tax law position.

A characteristic of the limited liability company is the fact that the owners are not personally liable for the company's obligations. The Swedish Companies Act⁷ contains provisions governing both a private and a public company form. The basic rule is that the provisions in the Companies Act's are valid for both types of companies limited by shares. The difference between the company forms relates, on the one hand, to the required amount of the share capital (minimum 100,000 and 500,000 SKr respectively), and on the other hand to some specific rules contained in the Companies Act concerning the fact that shares in a public company are designated for public trading. Accordingly, a private company may offer, or seek to disseminate, its shares and other financial instruments to new

⁷ *Aktiebolagslagen (1975:1385).*

shareholders only to a very limited extent. It must be evident from the company's name whether the company is a private or a public company.⁸

1.2.2 The Principle of Neutrality in Swedish Tax Law

One of the most basic viewpoints in Swedish tax law is the principle of neutrality. This principle is supposed to achieve rules which are neutral with aspect of taxation. Regarding company taxation one principle is that the tax rules should not influence whether an economic activity is pursued through one single entity or by multiple entities, i.e. a group of companies. Since all Swedish companies are defined as a single tax entity, Swedish groups of companies are not taxed on a consolidated basis.⁹

1.2.3 Tax Law and Foreign Legal Persons

A *foreign legal person* refers to an association that, according to the legislation in the country where it is domiciled, has rights and obligations and can speak for the court and other governmental organs.¹⁰ In other words, that it possesses its own legal capacity. This includes the element of not having the right to use freely the capital assets of the association. Both these requirements have to be fulfilled in order to be a company defined as a foreign legal person.¹¹

A foreign company is defined for Swedish tax purposes as a foreign legal entity that is subject to taxation in its country of residence, with a similar taxation as Swedish resident companies.¹² In respect of foreign legal persons, some tax provisions make a distinction between foreign companies and foreign legal entities other than foreign companies.

⁸ See generally http://www.legal500.com/devs/sweden/cl/sdcl_001.htm, article on Swedish limited companies, downloaded at 3 February 2003.

⁹ However, a group of companies can, under certain circumstances, exploit the rules on untaxed group contributions to avoid chain taxation and apply profit equalisation.

¹⁰ ITA Ch. 6 Sec. 8

¹¹ See generally *Handledning för internationell beskattning*, Rikskatteverket, 6th ed, 2002.

¹² ITA Ch. 5 Sec. 8.

A Swedish company always is considered to have full tax liability in Sweden if it is registered there.¹³ Full tax liability means that it is destined to pay tax on the total income, independent of where in the world it is generated.¹⁴ A foreign legal person has a limited tax liability, which means that it is only liable to pay tax on income gained in Sweden.¹⁵

A foreign company is subject to Swedish national income tax in the following cases:

1. business income effectively connected with immovable property or a permanent establishment in Sweden;
2. business income realised through the sale of shares in a Swedish housing association;
3. profit shares from Swedish economic associations;
4. any amount of refunded tax in respect to which a corresponding deduction has been granted in an earlier year.¹⁶

A Swedish subsidiary of a foreign parent company is treated in the same manner as any other Swedish company for tax purposes. Subsequently a subsidiary of a Swedish company, which has a permanent establishment abroad, is exclusively taxed in the other country as long as the income is not transferred from the country of establishment. This rule is effective as long as the CFC-taxation is not applied.¹⁷ The Swedish CFC-rules apply when a foreign subsidiary is a subject to low taxation and give rise to direct taxation for profits for owners, which holds shares in a foreign legal person. The tax is subsequently continual as from when

See the Guide to European Taxation, Vol. II (GET-II), *The Taxation of Companies in Europe*, International Bureau of Fiscal Documentation (IBFD), Sweden, Suppl. No.162, April 2002, p.38.

¹³ A legal person is considered Swedish if it is registered in Sweden or if not registered, where the physical presence of its board is situated.

ITA Ch. 6 Sec.3.

¹⁴ ITA Ch. 6 Sec. 4.

¹⁵ ITA Ch. 6 Sec. 7.

¹⁶ See generally *Handledning för internationell beskattning*, Riksskatteverket, 6th ed, 2002.

¹⁷ CFC is short for "Controlled Foreign Company".

the earnings of the foreign legal person arise and not when the dividends are transferred to the shareholders.¹⁸

1.3 Major Forms of Reorganisation in Sweden in accordance with the Merger Directive

In order to make the Swedish rules concerning reorganisation easier to overview, they have been organised in four main categories in accordance with the Merger Directive: mergers, divisions, transfers of assets and exchange of shares.

The transfers of assets category will deal with transfers of assets below market value together with the transfer of a branch, a transfer of all assets in a company and transfer of shares issued for a consideration other than cash (a so-called “apportemission”). Other important instruments worth mentioning are various internal transfers of assets within a group of companies’, which will be analysed under the category Mergers, and *the Lex Asea Rule*, which will be discussed under Divisions.

Below there will be a short presentation of the four main methods used in a Swedish domestic or cross-border reorganisation; the presentation involves both tax law and company law provisions.

*1.3.1 Mergers*¹⁹

In the earlier rules, governing tax-exemption on mergers²⁰ there were not any regulations that governed mergers between self-contained companies.²¹ This was the reason why it was not very common with mergers in Sweden or mergers between Swedish and foreign companies. The rules in Ch. 37 today include a wide-ranging regulation on both domestic as well as international mergers.²²

¹⁸ See generally *Handledning för internationell beskattning*, Riksskatteverket, 6th ed, 2002.

¹⁹ The rules regarding mergers and divisions are regulated in Ch. 37 ITA.

²⁰ See the old *State Income Tax Law, Lag (1947:576) om statlig inkomstskatt*, Sec. 2 paragraph 4.

²¹ The legislation regarding mergers is found in Ch. 37 in ITA.

²² International Bureau of Fiscal Documentation, *Commentary on the EC Direct tax measures and member states implementation*, EC corporate tax law, Sweden - i, Suppl. No. 23, June 2002.

A merger is defined in Ch. 37 Sec. 3 in ITA. It is an operation whereby all the assets and other liabilities of one or more companies are transferred into another company. The transferring company or the transferred companies are to be dissolved without liquidation. This is the same definition as in Art. 2 of the Merger Directive.

From a company law perspective, one of the most common forms of mergers between Swedish companies is when a parent company absorbs its wholly owned subsidiary; consequently, this is called *absorption*.²³ An absorption can also be carried out when an existing company, which is self-contained, is taken over by another not related company. The same rules apply to both procedures. However, in the latter case the shareholders in the absorbed company are regarded as having disposed their shares.²⁴

The other kind of merger used according to company law, is when two or more companies establish a new company that takes over their assets and liabilities. In return, the new company issues its own shares. This kind of merger is called a *combination*.²⁵

1.3.2 Divisions

There are no company law provisions regarding divisions in Swedish law and until recently there were not any tax provisions either. However, as a limited number of rules regarding tax on reorganisations were introduced in 2000, it is now possible, under certain circumstances, to divide a company into smaller units without immediate tax consequences.²⁶

²³ Ch.14 Sec. 22 in the Companies Act.

See Riksskatteverkets handledningar, *Skattehandledning 2002*; part 3, Ch.16, *Fusioner och fissioner*.

²⁴ This is usually compensated by a merger-remuneration (*fusionslikvid*) to the shareholders.

²⁵ See *the Companies Act*: Absorption, Ch. 14 Sec. 1; Combination, Ch. 14 Sec.2; and Merger, Ch. 14 Sec.8.

²⁶ *Inkomstskattelagen – En kommentar. Del II*, Andersson, Mari et al, Nordstedts juridik, Göteborg 2001.

The definition of divisions is located in Ch. 37 Sec. 5. A division is an operation in which a company transfers all assets, debts and other liabilities to two or more companies. The transferring company is to be dissolved without liquidation. A qualified division of a Swedish parent company (i.e. a division which correspond to the requirements of Art. 10(1) in the Merger Directive) may distribute all the shares in a Swedish, or a foreign subsidiary, to its shareholders tax-free.²⁷ In other cases where the business may be divided, general tax principles apply.

1.3.3 Transfer of Assets

A transfer of assets means, contrary to mergers, that the transferring company continues to exist and this will influence the closing balance of the transferring company. Swedish tax law contains a number of specific rules regarding transactions between related companies, but no provisions as how to carry out a transfer of assets from a parent company to its subsidiary, or between related companies. The principles regarding those kinds of actions are therefore based on case law. The established practice is that it is possible to transfer the entire business, or a whole branch, of one company to another, with the same owner, without the seller incurring taxation of any price difference.²⁸

If a transfer of assets is *below the market price* Swedish enterprise taxation applies the fundamental principle that the assigning enterprise must pay tax in accordance with its market value. This taxation theory means that the tax effect will be the same as if the assets had been sold at market price.²⁹ However, a pricing below market value is generally permitted if certain criteria are met.

²⁷ ITA Ch. 37 Sec.11-15.

Inkomstskattelagen – En kommentar. Del II, Andersson, Mari et al, Nordstedts juridik, Göteborg 2001.

²⁸ See RÅ 1989 ref.19 (The Supreme Administrative court ruling, ref.19 in 1989).

²⁹ ITA Ch. 14 Sec.19.

The most important instrument to level the burden of income tax within a group of companies is *group contribution*; in general, such transfers are tax-free if both the paying and the receiving companies are liable to pay tax in Sweden.³⁰

1.3.4 Exchange of Shares

One of the most common ways of reorganisation is when a company takes over another company's shares in exchange for its own.³¹ In order to qualify for a tax deferral in this case the shareholders do not obtain any cash payments, or just a small amount (10%). When the shares later leave the company, or the receiving company leaves the initial group of companies, the acquired shares are taxed as well as the deferred gain of the shares transferred in the first transaction.³²

1.4 Correspondence of Definitions

1.4.1 Coherence between the Merger Directive and National Legislation

The Swedish definitions of domestic- and cross-border reorganisations correspond to the definitions in the Merger Directive and the incorporated provisions take priority over any other provision in the ITA concerning cross-border reorganisations. The requirements for the directive's provisions to apply are that the reorganisation concerns companies resident in a Member State.

One important feature regarding the Swedish implementation, that stretches further than the aims of the Directive, is that the provisions in the Merger Directive are applicable on domestic reorganisations as well. The definitions in national law are therefore not supposed to be different compared to the legislation on cross-border reorganisations and the Directive.

³⁰ International Bureau of Fiscal Documentation, *ECTL*, Sweden - vi, Suppl. No. 23, June 2002.

³¹ ITA Ch. 49 Sec. 2.

³² *Ibid.*

The Merger Directive is not by itself applicable on solely national reorganisations. However, in accordance with the EC Court's ruling in the Leur Bloem-case³³ the EC law is applicable on national situations when the applicable regulation covers both national and harmonised situations. In other words, since the Swedish regulations on reorganisations are applicable on both cross-border and domestic reorganisations the regulation must be interpreted according to EC rules even on solely national relocations. This is an interesting progress. Before 1998, i.e. when Sweden first regulated international and national reorganisations in the same set of laws, Swedish interpreters only read tax regulations in accordance with the purposes behind the EC law when they dealt with cross-border reorganisations. Now, it is necessary that also Swedish tax lawyers, who are specialised on national transfers, are well familiar with the Merger Directive and the result aimed for in the Directive.

1.4.2 Coherence between Company Law and Tax Law

The main principle underlying Swedish tax law is that tax law follows company law insofar as tax law considerations do not require a different approach.³⁴ However, as regards reorganisations, the definitions for tax purposes in Swedish law do not coincide with the definitions for company law purposes. Swedish company law contains rules on mergers but not on divisions. The tax definitions on the other hand match with the definitions in the Merger Directive despite the fact that many of the regulated transactions cannot be performed according to company law.³⁵

The Swedish law regarding taxation of businesses and reorganisations is also very closely related to the rules governing financial accounting. One of the legislative aims in this context is that it should be possible to take financial statements

³³ C-28/95 A. Leur-Bleum v. Inspecteur der Belastingdienst/Ondernemingen Amsterdam 2 REG 1997.

³⁴ *Ibid.*

³⁵ Wiman, Bertil, *Beskattning av företagsgrupper*, Norstedts Juridik, Stockholm, 2002, p. 218.

prepared by a company, for commercial purposes, and use them as a basis for the taxation of the business.³⁶

³⁶ International Bureau of Fiscal Documentation, *Mergers & Acquisitions (M&A)*, Sweden, p. 19, Suppl. No. 17, December 1999.

2 Mergers and divisions

2.1 Taxable Reorganisation

A merger or a division contains tax issues from two different views, the company aspect and the shareholder aspect.³⁷ Questions regarding capital gains or losses are possible within both kinds of aspects. From a company point of view the questions regarding capital gains is dealt with in Ch. 37 ITA, together with the tax treatment of other assets and liabilities in connection with a merger or a division. Capital gains to a shareholder are dealt with in Ch. 49 ITA (as regard to exchange of shares and not cash transfers).

2.1.1 Conditions for a Qualified Merger or Division

The term “qualified” in regard to mergers or divisions is new; it is used in order to define mergers and divisions that have tax-continuity.

A foreign company resident in another Member State always qualifies for a merger or a division according to Ch. 37 Sec. 9 ITA, if it fulfils the requirements in Art. 3 (a) and (c) of the Merger Directive.³⁸ In order to qualify for tax exemption in Sweden there are however, some additional criteria, which have to be fulfilled.

The transferring company should have been liable for income tax before the merger or division took place. The income of the transferring company should not have been *fully* exempted from income tax due to a tax treaty (ITA Ch. 37 Sec.11). The receiving company must immediately after the merger or division, qualify for the same tax liability as the transferred company, in correspondence to the business carried out in the transferred company. The received company inherits

³⁷ Wiman, *Beskattning av företagsgrupper*, p. 189ff.

³⁸ Unless the company is resident in another Member State according to a double tax treaty, ITA Ch. 37 Sec.10.

the transferred company's tax position at the time of the merger or division (Ch. 37 Sec.12 and Sec.17).³⁹

A qualified merger is not only a merger between a parent company and its subsidiary but also includes mergers such as absorption's and combinations and equivalent arrangements.

The above provisions cover the requirements of Art. 10(1) in the Merger Directive. One might even conclude that the Swedish legislation is more generous than the Directive regarding the distinction between mergers and divisions taken place in more than one Member State. In Swedish legislation there is no difference between mergers and divisions taking place within one Member State, between two member states, or within or between non-member states, as long as they qualify.

2.1.2 Taxes on Mergers

All Member States permit, under certain conditions, some sort of deferral of gains on mergers. The deferral can be achieved by two means: a full deferral until subsequent realisation (similar in effect to rollover relief), or a deferral by means of an instalment plan for tax payments due on any gains arising as a result of the merger. However, in general, a qualified domestic or international merger (or division) does not give rise to any taxation for the involved companies in Sweden.⁴⁰ As the receiving company "replaces" the transferring company the transfer of assets, liabilities and untaxed reserves in connection with the merger is tax free as there is no taxable gain or deductible capital loss for any of the involved companies.⁴¹ A full rollover of tax attributes takes place. Consequently, no deductions following the merger or division are allowed to the transferring company.

³⁹ Regarding the inherited tax position for the receiving company, see e.g. RÅ 2000 ref. 18.

⁴⁰ ITA Ch. 37 Sec. 17.

⁴¹ International Bureau of Fiscal Documentation, *The Taxation of Companies in Europe*, The Guide to European Taxation: Vol. II, GET-II, Suppl. No. 162, April 2002, p 141.

It has been argued that the Swedish rules regarding the inherited tax position for the receiving company in a merger go beyond what is required by the Merger Directive. The most important criteria are that both the transferring and the receiving company must be subject to Swedish tax with respect to the transferred assets. This permits transfers of permanent establishments in Sweden to be subject to foreign mergers and divisions. The receiving company according to the Swedish legislation is obliged to deal *with all tax attributes* of the transferring company.⁴²

Two relevant cases concerning mergers on commercial terms were brought before the court in 1990.⁴³ In these cases, several enterprises assigned their businesses into a newly formed company. The number of shares was obtained in accordance with the value of their respective businesses. No beneficial transfers occurred between the owners. The Supreme Administrative Court held that since the transfers were based on commercial terms and no gifts had been made, there should be no taxation on any value difference.⁴⁴ However, there are some exceptions regarding the taxation of the receiving company.⁴⁵

*2.1.3 Appreciated Value of Transferred Assets*⁴⁶

Under the provisions on depreciation for tax purposes, the taxpayer may use a declining balance method if a corresponding depreciation is made in the commercial accounts. Thus, depreciation for tax and accounting purposes is identical.⁴⁷ If the receiving company books a higher value on the assets from the transferred company in its commercial accounts, the receiving company will be

⁴² Wiman, *Beskattnings av företagsgrupper*, p. 193ff, 218.

International Bureau of Fiscal Documentation, *The Taxation of Companies in Europe*, The Guide to European Taxation: Vol. II, GET-II, Suppl. 21.

⁴³ RÅ 1990 not. 393 and RÅ 1990 not. 394.

⁴⁴ RÅ 1990 not. 393 and RÅ 1990 not. 394

See also RÅ 1990 ref. 115.

⁴⁵ ITA Ch. 37 Sec. 20-28.

⁴⁶ ITA Ch. 37 Sec.20.

⁴⁷ Wiman, *Beskattnings av företagsgrupper*, p. 193ff.

taxed on the difference between the value in the hands of the transferor and the appreciated value. This income must be taxed immediately or over a period of three years (1/3 each year). The same rules apply if the transferred assets appreciate for other reasons in the receiving company's hands.

It could be discussed whether this is coherent with respect of Art. 4(2) and (3) in the Merger Directive, since the receiving company may opt to have e.g. a new depreciation, computed on a different basis than the transferring company.⁴⁸

*2.1.4 Transfer of Losses in a Merger or Division*⁴⁹

The rules regarding transfer of losses are complicated. However, they do not distinguish between purely domestic and cross-border reorganisations. Art. 6 of the Merger Directive require that any provisions on transfers of losses applicable to domestic reorganisations are applicable to reorganisations covered by the Merger Directive.⁵⁰

In general, a taxpayer engaged in a business activity may carry a loss forward to the next tax year, at which point it will be used as a deduction. The procedure may then be repeated, and a loss can therefore be carried forward indefinitely, until income is produced to offset the loss.⁵¹

The rules concerning transfers of losses are troublesome since the intention of the legislators is twofold.⁵² On one hand, the intention is that it should be possible to make a transfer of losses in a merger or a division. On the other hand, the

⁴⁸ ITA Ch. 37 Sec.20.

International Bureau of Fiscal Documentation, *Guide to European Taxation*, ECTL, Suppl. No. 21, June 2002, iii.

International Bureau of Fiscal Documentation, *Guide to European Taxation*, Note. 102 Suppl. 13, May 1996 by Bertil Wiman.

Inkomstskattelagen – En kommentar. Del II, Andresson et al, p. 876.

⁴⁹ Ch. 37 Secs. 21-26.

⁵⁰ International Bureau of Fiscal Documentation, *Guide to European Taxation*, ECTL, Suppl. No. 21, June 2002, iii.

⁵¹ ITA Ch. 40 Sec.2.

International Bureau of Fiscal Documentation, *Guide to European Taxation*, ECTL, Suppl. No. 21, June 2001, iii.

legislator has been bound to limit these possibilities in regard to the tilts on losses, in relation to changes of ownership.⁵³ For the legislator, tilts on losses in relation to changes of ownership are an important instrument to stop tax diversion within groups of companies. The tilts on losses are supposed to impede the possibilities for the taxpayer to neutralise a taxable income by incorporating a company with deductible losses. The rules concerning transfer of losses in Ch. 37 in the ITA constitute an exemption from the principle that only the company, which generated the loss, may use it.⁵⁴

In a merger or a division the receiving company is supposed to acquire the same tax position as the transferor, this also applies to losses.⁵⁵ However, a qualified domestic or international merger, which is not fully owned⁵⁶ by the parent company, does not allow deduction for losses until five years after the reorganisation. The absorbing company obtains the same right to carry forward and to carry back as the absorbed company before the merger. It may not set off losses against group contributions received from the other company during the first six years after the change of ownership.⁵⁷ One might say that the old loss is quarantined for 6 years.⁵⁸ A company that has acquired control over a not related, loss-making company permanently loses its right to deduct losses in excess of 200% of the acquisition price.⁵⁹

⁵² Wiman, *Beskattnings av företagsgrupper*, p.98f., 195f.

⁵³ Tilts in connection to changes of ownership are found in Ch. 40 of the ITA.

⁵⁴ Wiman, *Beskattnings av företagsgrupper*, p.98f., 195f.

⁵⁵ Wiman, *Beskattnings av företagsgrupper*, p.98f.

⁵⁶ ITA Ch.37 Sec.22 compared to Ch.40 Sec.5, (which further directs to Ch.1 Sec.5 in *the Companies Act*). To be defined as a wholly owned company it is constituted that the owner must control more than 50% of the shares, and have the ability to vote for more than 50% of the total amount of votes. It is also possible to be defined as a wholly owned company if the owner e.g. have a dominating control due to a treaty with the shareholders.

⁵⁷ ITA Ch. 37 Sec. 24.

⁵⁸ ITA Ch. 37 Sec. 24.

One exception from the quarantine is, if it before the merger has been possible to offset taxable income between the companies through tax consolidation, by way of so called group contributions (koncernbidrag). Group contributions are deductible to the donor and taxable for the recipient.

⁵⁹ Wiman, *Beskattnings av företagsgrupper*, p.98f., p. 195f.

Deduction for business losses and losses regarding portfolio investment shares are only available to mergers between a parent company and its fully owned subsidiary (or when the transferring company is an insurance company or a banking company)⁶⁰. If the shares in the subsidiary are held for business reasons, tax relief will be available against business income for that part of the loss corresponding to an actual loss.⁶¹

2.1.5 Merger (and Division) Considerations

There are no tax consequences incurred on the shareholders of the parent company in connection with a parent-subsidary merger. Regarding other mergers, it is deemed that the shares have been sold to the receiving company. If the receiving company do not obtain all the shares in the transferring company, merger considerations may be paid, though only to those shareholders that does not own any shares in the receiving company.⁶² Any merger considerations for the sold shares are taxable. However, a tax deferral may apply in accordance with the rules on exchange of shares within a group of companies.⁶³

2.1.6 Tax Law Divisions and Company Law Divisions

The term “division” has no definitive signification, it includes any operation in which a company dissolves without liquidation and transfers all assets, debts and other liabilities to two or more companies.⁶⁴

There are a number of different reasons for a division. For example if a company wants to specialise on one certain branch of activity it might be helpful to separate

⁶⁰ See ITA Ch. 37 Sec. 2 with references to Ch. 42 Sec. 21 compared to Ch. 48 Sec.10.

⁶¹ ITA Ch. 25 Secs. 6-27.

⁶² See ITA Ch. 37 Sec. 13 and Prop. 1999/2000:2 part 2 p. 435.

⁶³ See e.g. International Bureau of Fiscal Documentation, *Guide to European Taxation*, ECTL, Suppl. No. 17, December 1999.

⁶⁴ ITA Ch. 37 Sec.5.

Lodin et al, 2000, p. 435.

International Bureau of Fiscal Documentation, *Guide to European Taxation*, ECTL, Suppl. No. 23, June 2002, ii.

it from other branches in the company, or if a group of companies is preparing a merger, a division might be effective in order to separate one specific branch.⁶⁵

There are many different kinds of techniques to divide a company; the most common ones are spin-offs, split-offs and split-ups. A spin-off is a distribution of a subsidiary to the shareholders of the parent company whereas a split-off is the equivalent situation but usually preceded by a transfer of the inner assets from the original company to its subsidiary. A split-up means that the assets and debts of the company are transferred to two or more new companies and that the original company ceases to exist, with or without liquidation. There are, despite the use of these models, no company law provisions in Sweden regarding divisions.⁶⁶

The company law regulation on divisions has not been harmonised with the tax laws in Sweden, which results in incoherence between company law and tax law. This is a suppressed domestic problem, which until now has been dealt with on a case by case basis in the Swedish courts. However, it has international implications as well, particularly when it is technically possible for a company in another Member State to make a division, which has consequences from a Swedish company law perspective.⁶⁷

2.1.7 Conditions for Deferral in regard to Shareholders

The Swedish legislator regards mergers as an exchange of shares for the shareholders; consequently the rules on deferral of taxes for the shareholders are not regulated in Ch. 37 ITA.⁶⁸

2.1.8 Divisions According to Lex Asea (Spin-offs)

A substitute to the rules on divisions is a rule called *Lex Asea*. This rule, which is implemented from case law, allows for a tax-free division of a company

⁶⁵ *Ibid*, Lodin.

⁶⁶ Rutberg, Anne, *Fission - nationella och internationella skattefrågor*, Skattenytt 1995, nr 7-8.

⁶⁷ *Ibid*.

⁶⁸ Wiman, *Beskattnings av företagsgrupper*, p. 189-190.

positioned on a Swedish or a foreign market, if the part of the company that will be divided is transferred to a newly formed or existing subsidiary (Ch. 42 Sec.16). The subsidiary must mainly carry on activities other than just the holding of cash deposits or securities. All shares of the subsidiary must then be distributed to the shareholders of the parent company in proportion to their shares in the parent company.⁶⁹ Since the market value usually is higher than the tax value there would normally be a risk of taxation. However, the shareholders are not taxed on the dividend if the company is listed on the stock exchange (which excludes most of the smaller companies) and if the shares do not constitute a current asset in their hands (i.e. that the shares are considered to be in the hands of the parent company instead).⁷⁰

The tax basis is computed by comparing the market value of the shares in the parent company before and after the distribution. Any difference is attributed to the received shares, the tax basis of the shares in the parent company is deemed to be reduced by that amount.⁷¹ In a division the profit periodisation reserve and replacements reserves are divided among the receiving companies in proportion to the net value of the transferred assets.⁷²

⁶⁹ ITA Ch. 42:16 and the International Bureau of Fiscal Documentation, *Taxation of Companies in Europe*, Guide to European Taxation: Vol. II, GET-II, Suppl. No. 160, December 2001, p 142.

⁷⁰ *Ibid.*

⁷¹ International Bureau of Fiscal Documentation, *The Taxation of Companies in Europe*, Guide to European Taxation: Bertil Wiman, Suppl. No. 17, May 1998, p 15.

⁷² *Ibid.*

3 Transfer of Assets

3.1 Taxable Reorganisation

The established practice in Sweden is that it is possible to transfer the entire assets, or the full assets of one of the company's branches, from one company to another, with the same owner, without the seller incurring tax on the price difference.⁷³ The remuneration must be at arm's length, and must consist of shares in the receiving company.⁷⁴ The Swedish definition seems to be consistent to the definition in Art.2(c) of the Merger Directive.⁷⁵

A Swedish company that transfers assets and debts to a company in another Member State will be taxed if these assets and debts are effectively connected to permanent establishment in a third Member State. Losses will not be deductible except when a tax credit would have been granted according to a tax treaty and if the Merger Directive has not been applicable.⁷⁶

In the case of an international transfer of assets, which does not involve all assets of the transferring company, only the profit periodisation reserve, replacements reserves and the right to deduction for losses may be transferred in correspondence with its net value. Amounts included in the balance sheet as a provision/reserve for future liabilities are transferred if connected with the transferred branch. The remuneration (i.e. the purchased value of the securities, which the transferring company has received as consideration) shall exceed the fiscal value of the

⁷³ Branch of activity (verksamhetsgren) constitutes, in this context, a part of business suitable to be separated into an independent business activity.

See RÅ 1989 ref.19 (The Supreme Administrative court ruling, ref.19 in 1989).

⁷⁴ ITA Ch. 14 Sec.19.

⁷⁵ International Bureau of Fiscal Documentation, *The Taxation of Companies in Europe*, Guide to European Taxation: Bertil Wiman, Suppl. No. 17, May 1998, p. 15.

⁷⁶ Wiman *Beskattning av företagsgrupper* p. 83 f.

transferred assets; transfer of assets that constitutes a capital gain for the receiver is otherwise regarded as a gift from the transferor.⁷⁷

An international transfer of the internal assets within a company is usually taxed. For example, the transfer of machines and fixtures from a Swedish parent company to its subsidiary abroad, is not possible without incurring tax of some sort for the Swedish parent company.⁷⁸

3.1.1 Transfer of Assets below Market Value

Reorganisation within an existing group of companies may motivate a tax exemption on transfer of assets. An income, which is generated from such a transfer, will not be taxed until the assets leave the initial group of companies to an external buyer. The legislator motivates this exemption with the fact that if a reorganisation is impeded this may also have harmful effects on the socio-economic development.⁷⁹

A pricing below market value is generally permitted if certain criteria are met. For example, when two parties are subject to Swedish tax (thereby generally including permanent establishments of foreign companies), tax exemption is possible if the acquiring company does not have a loss carried forward from the previous year.⁸⁰

3.1.2 Untaxed Group Contributions

Within a group of companies, the most common form of transferring assets is made as an *untaxed group contribution*. A group contribution is deductible for the transferring company and taxed by the receiving company. These kinds of contributions are called *open contributions* in order to separate them from ordinary business transactions, which are deductible anyway.⁸¹ To cope with the

⁷⁷ *Ibid*, Wiman, p. 89 ff.

⁷⁸ Alhager, 2002 p.170.

⁷⁹ Wiman, *Beskattning av företagsgrupper*, p. 121.

⁸⁰ That is, if the Swedish rules for taxing owners of closely held companies are not being bypassed, See Wiman, *Beskattning av företagsgrupper*, p. 218.

⁸¹ ITA Ch. 35 Sec.1 paragraph 2. See Wiman, *Beskattning av företagsgrupper*, p. 68f.

EC rules regarding freedom of establishment, the Swedish regulations on group contributions is also valid for foreign companies.⁸²

In order to qualify for a group contribution, the foreign company must be a member of the EEA⁸³ and be equivalent to the Swedish companies listed in Ch. 35 Sec. 2.⁸⁴ One important feature is that the receiving company must have tax liability in Sweden for the businesses, which the group contribution derived from.⁸⁵

3.2 Conditions for Tax Exemption

3.2.1 Transfer of Assets

Companies resident in a Member State qualify for tax-free group contributions if both the paying and the receiving companies are liable to tax in Sweden and the contributions are taxable as business income carried out in Sweden and are not tax exempted because of a treaty. Due to treaty rules, these rules also apply to Swedish companies' resident in a foreign state but with a permanent establishment in Sweden. If both the receiving and the transferring company are residents of other Member States than Sweden; and the transferring company has a permanent establishment in Sweden, this company will be regarded as a Swedish company.⁸⁶

3.2.2 Tax Exemption on Capital Gains

Until recently, there have not been any tax exemption rules for capital gains on the sale of shares in a subsidiary. Capital gains in a Swedish limited liability company have been taxed in the same manner as ordinary income of business. If the profit is kept in the subsidiary and realised through the sale of the company, a taxable

⁸² Wiman, *Beskattning av företagsgrupper*, p. 81ff.

⁸³ The agreement on the European economic area.

⁸⁴ ITA Ch. 35 Sec. 2.

See e.g. C-200/98 and RÅ 2000 ref. 17.

Wiman *Beskattning av företagsgrupper* p. 83.

⁸⁵ ITA Ch. 35 Sec. 2.

capital gain will occur, even though the same profit could have been received as a tax-exempt dividend. Accordingly, the tax-regulations in this aspect were not "symmetrical". However, the rules which came into force 1 January 2003, means that capital gains on certain business shares are tax-free and that capital loss is not deductible.⁸⁷

⁸⁶ International Bureau of Fiscal Documentation, *M&A*, Sweden, Suppl. No.17, December 1999, p. 24 ff.

⁸⁷ See generally SOU 2001:11 *Utdelningar och kapitalvinster på företagsägda andelar*.

4 Exchange of Shares

4.1 A General Overview

According to a main rule of Swedish taxation an exchange of shares is a taxable event.⁸⁸ The taxable gain is calculated as the difference between the fair market value of the shares received and the average acquisition cost of the shares that have been disposed of.⁸⁹ However, subject to certain conditions, it is possible to claim a deferral of the tax payment. Thus, the taxable gain shall be calculated at the time of the sale but payment of the tax may be deferred. However, special rules apply for individuals covered by Ch. 48 a, ITA, according to this regulation the roll over method should be used. The roll over method stated in Ch. 48 a, is equal to the method stated in the Merger Directive.⁹⁰

Ch. 49 Sec. 5 states that the regulations on exchange of shares should not be applied if the regulations in Ch. 48 a, on exchanges of shares made by individuals or Ch. 25 on intra-group transfers of shares are applicable. Consequently Ch. 48 a, and Ch. 25 will initially be described followed by Ch. 49.

4.1.1 Rules Applicable on Individuals (Ch. 48 a)

Special rules apply to individuals who have their permanent place of residence in Sweden or permanently stay in Sweden. When such individuals sell listed shares for consideration of shares in the acquiring company, they will under certain conditions have a right to defer the taxation of such sale until the received shares are disposed of, terminated or the individual ceases to have the permanent residence in Sweden or permanently stay in Sweden. According Ch. 48 a Sec. 10 the roll over relief method should be applied. In accordance with the roll over

⁸⁸ ITA Ch. 44 Sec. 3.

⁸⁹ ITA Ch. 44 Secs. 13-14.

⁹⁰ The rules described are applicable irrespective of whether the acquiring company is Swedish or foreign Ch. 24 Secs. 20-21.

relief method the shares received shall not attribute to a tax value higher than the shares exchanged was immediately before the exchange. When the received shares are sold on later date taxation will automatically occur on the increased value on the shares before the exchange.

To qualify for a deferral of the tax payment the following conditions must be fulfilled:

- The seller is an individual who have his/her permanent place of residence in Sweden or permanently stay in Sweden;
- The acquirer must be a Swedish limited company or a foreign company;
- Consideration for the shares sold must be at fair market value;
- The consideration shall be shares in the acquiring company and any cash payment may amount to maximum 10 percent of the nominal value of the shares received;⁹¹
- The acquiring company must hold more than 50 percent of the votes in the acquired company at the end of the calendar year during which the share exchange occurred;
- The shares sold must be listed at the time of the offer of exchange and the shares sold must not be so called qualified shares in a closely held or previously closely held company (from 1 January 2003 there is no requirement that the shares should be listed and the rules will be applicable on qualified shares)⁹².

4.1.2 Intra-group transfers of shares (Ch. 25)

Ch. 25 embraces transfers of shares within Swedish and certain foreign corporate groups. The regulations apply equally to exchanges of shares and ordinary sales of shares, i.e. Ch. 25 do not stipulate that not more than 10 percent cash may be used in case of intra-group transfers of shares. This means that any amount of cash

⁹¹Based on advance tax rulings and court practice, it is uncertain how the condition that any cash part of the consideration may amount to maximum 10% of the nominal value of the shares received should be interpreted. If sale and exchange agreements etc. are properly drafted, it might be possible to argue that the sale is divided into two separate transactions of which one concerns sale of shares for consideration of only shares in the acquiring company and the other one concerns sale of shares for consideration of cash.

⁹² I.e. taxation year 2004.

could be used and the parties could still claim a deferral of the capital gain (fair market value less acquisition cost for tax purposes). Intra-group transfers of shares resulting in losses must not be deducted until the shares are disposed of to an independent third party or no longer exist, according to Ch. 25 Sec. 30 §.⁹³

Corporate shareholders are granted a deferral of the tax payment if claimed and the exchange of shares fulfils the requirement of Ch. 25. Thus, the taxable gain shall be calculated at the time of the sale but the payment of tax may be deferred.

To qualify for a deferral of the tax payment the following conditions must be fulfilled:

- The acquirer must be part of the same corporate group as the transferring party;
- The parent company of the corporate group must be a qualifying legal person, including but not limited to Swedish and foreign limited liability companies;
- The share must be a share in a Swedish or foreign company;
- The transferring company must together with other group companies hold shares representing at least 25 percent of the votes in the transferred company, or be able to prove that the shares are held for business reasons;
- The consideration for the exchanged shares could be less than fair market value; and
- There are no requirements as to the consideration, i.e. it could be cash, shares or other remuneration in kind.

The deferred tax payment must be made when the transferring company ceases to be resident in Sweden, ceases to exist (otherwise than through a merger with a company of the same corporate group) or if the transferred shares no longer exist or are transferred to a person not belonging to the same corporate group as the transferring company.

⁹³The Merger Directive does not deal with intra-group losses on shares, and therefore exchanges of shares resulting in capital losses will not be further developed.

4.1.3 Other exchanges of shares (Ch. 49)

An exchange of shares could under other circumstances than those mentioned above qualify for a deferral of the tax payment if claimed. Thus, the taxable gain shall be calculated at the time of the sale but the payment of tax may be deferred.

The following conditions must be fulfilled:

- The acquirer must be a Swedish limited company or a foreign company;
- Consideration for the shares sold must be at fair market value;
- The consideration shall be shares in the acquiring company and any cash payment may amount to maximum 10 percent of the nominal value of the shares received;
- Any consideration in cash must be less than the capital gain (in case the shares sold have been stock item, the difference between the total consideration and the tax value of -the shares must exceed the cash consideration);
- The seller is not an individual selling listed shares who qualifies for a deferral of the taxation according to Ch. 48 a;
- If the seller is an individual he must have his permanent place of residence in Sweden or permanently stay in Sweden.
- the acquiring company must hold more than 50 percent of the votes in the acquired company at the end of the calendar year during which the share exchange occurred; and
- if the shares sold are so called qualified shares in a currently or previously closely held company and the seller alone or together with relatives holds at least 25% of the votes in the acquiring company, the acquiring company's operations must in principal consist of business activity or holding of subsidiaries with business activities.

It is not possible to defer the payment of tax related to part of the sale that has been for consideration of cash.

The deferred tax payment must be made when the shares received are disposed of (unless also such disposal is an exchange of shares), terminated or when the holder (if an individual) ceases to be resident or permanently stay in Sweden.

4.2 The Roll over Relief method

The method for deferral presented in the Merger Directive is a roll over relief method.⁹⁴ The roll over relief method implies that shareholder's do not attribute the shares received to a tax value higher than the shares exchanged had immediately before the exchange. The consequence of the method is that when the shares are sold on later date taxation will automatically occur on the increased value on the shares before the exchange.

4.2.1 *The Swedish method*

In the Swedish regulations another method than the roll over relief method is used (Ch. 49 and Ch. 25). According to the Swedish method the capital gain is calculated on the time for the exchange of shares and is divided on the shares received. The reason for using this method instead of the roll over relief method is that the latter method was difficult to combine with the allocation rules for the dispose of shares in close held companies.⁹⁵

A roll over relief method equal to the method presented in the Merger Directive is now used in the Ch. 48 a. This method is applicable on exchanges made after 1 January 2002.⁹⁶ The 48 a Chapter has been amended once again. After 1 January 2003 the chapter is extended to cover exchanges of shares in closely held companies.

4.2.2 *Are the Swedish deferrals consistent with the Merger Directive?*

In general, a directive only states what goals will be accomplished and it is therefore the Member States free choice to choose the method of implementation.

The purpose behind the Merger Directive is to make it possible to postpone the taxation on exchanges of shares. The method used in the Merger Directive is the

⁹⁴ Article 8.2 in the Merger Directive.

⁹⁵ Prop. 1998/99:15 s 179.

roll over relief method. The question is if there is a demand for the Member States to use the roll over relief method or if it only is a proposed method.

The roll over relief is a method for the Member State to use in order to protect their economically interests. The method is not designed in order to grant the tax subjects certain rights. The Merger Directive only grants the tax subjects the right to exchange shares without being immediately taxed. As long as the tax subjects do not get immediately taxed on the exchange it therefore should not matter, one might think, which method is used to defer the taxation.⁹⁷

However, the suitability of the Swedish method could be argued. The roll over relief method is to be applied on exchanges of shares made by individuals covered by Ch. 48 a. According to the amendments to the regulation the roll over relief method also should be applicable on exchanges of shares in closely held companies. The reason why Sweden did not applied the roll over relief method was the difficulty to combine the roll over relief with the allocating rules for dispose of shares in closely held companies. Since the legislators now seems to value the benefits with the roll over method higher than the benefit of an easier allocation method there should be no reasons not to use the roll over relief method on all exchanges of shares. The roll over relief is also the method applied internationally.⁹⁸

4.3 Taxation of Deferred Capital Gain

In accordance with the roll over relief method the capital gain will be taxed when the transferring person sells the shares received as compensation. There are no other rules in the Directive under which the deferred tax should be carried back to

⁹⁶ If the individual claims it the roll over relief method is also applicable on exchanges made after 1 January 2001. 48a:10 ITA.

⁹⁷ Kristina Ståhl, Omstruktureringar och EG-rätten – några synpunkter på den nya regleringen, Skattenytt 1998 p. 816 and Leif Gäverth, Andelsbyte och fördelning av uppskovsbelopp, Skattenytt 2000 page 557.

⁹⁸ *Ibid*, Ståhl.

taxation. Neither is there any limitation of who should be covered by the Directive.

4.3.1 The Swedish method

The deferred tax payment must be made when the transferring company ceases to be resident in Sweden (a so-called exit tax) and when it ceases to exist (except in the case of a merger with a company in the same group of companies) or if the transferred shares cease to exist or are transferred to a company not belonging to the same corporate group as the transferring company.

4.3.2 Are the Swedish regulations consistent with the Merger Directive?

According to Ch. 25 Sec. 17 the deferred capital gain should be reversed when the acquiring party disposes of the shares received. It has been questioned whether this would be in conformity with the Directive.⁹⁹ If the transfer is an intra-group transfer of shares between Swedish companies the transferring company should be taxed on the increase of value prior to the intra-group transfer, while the acquiring company would be taxed on the change in value after the intra-group transfer. Normally, the taxable result would be the same as if the transferring company had disposed of the shares to a person not belonging to the same corporate group as the transferring company immediately.¹⁰⁰

In case the intra-group transfer takes place between a Swedish and a foreign company, the outcome may differ substantially. The Swedish taxation of the capital gain is unconditional if the shares are disposed of. In case the value of the shares transferred has decreased, or if the transferred company has been forced into liquidation or bankruptcy, the foreign company may make a loss that is larger

⁹⁹ Kristina Ståhl, Omstruktureringar och EG-rätten – några synpunkter på den nya regleringen, Skattenytt 1998.

than the Swedish company's gain, i.e. there may be an overall loss at the disposal of the shares. A foreign loss is not possible to set off against Swedish domestic profits.

The Directive, on the other hand, does not stipulate that gains at the exchange of shares should be taxed at the disposal of the transferred shares. Article 8.2 of the Directive only states that "*The application of paragraph 1 shall not prevent the Member States from taxing the gain arising out of the subsequent transfer of securities received in the same way as the gain arising out of the transfer of securities existing before the merger, division or exchange.*"

The Swedish law could be interpreted in conformity with the Directive, in such way that the Swedish regulations would not trigger any taxation at the disposal of the transferred company. One could also disregard of the Swedish regulations if the Directive is directly effective.

The discussion of whether the Swedish tax regulations are in conformity with the Directive are likely more of theoretical than practical interest, as granted deferrals are proposed to be forgiven from 1 July this year (2003).¹⁰¹ At the same time the regulations on intra-group transfers will be abolished. This means that no Swedish taxation will be levied in case shares are transferred within a group at a capital gain. The forgiving of already granted deferrals removes the risk for situations where a corporate group pays tax in an overall loss situation. By using the proposed, generous regulations on deferral of capital gains many Swedish groups could effectuate tax planning measures that were likely not intended. For example, a Swedish company holding shares with an inherent unrealised gain in foreign partnerships may transfer these shares to a foreign company within the same corporate group. Normally, the foreign company will obtain the market value/acquisition price of the shares as acquisition value for tax purposes, i.e. the

¹⁰⁰ In case the shares have decreased in value it is often possible to equalize the taxable profit through group contributions, but this possibility may be hampered for different reasons e.g. mergers or acquisitions of companies with tax loss carry-forwards.

¹⁰¹ See generally SOU 2001:11.

corporate group will obtain a tax free step-up of the tax basis of the shares. The higher taxable basis could be used for an immediate external sale of the shares, which should be exempt from income tax if the market value remains unchanged until the sale is executed. Certain corporate groups may transfer the shares to affiliated companies resident in tax havens, who pay low or no taxes on the disposal of shares, if a future gain is expected and there is no immediate plan to dispose of the shares.

5 Special Questions

5.1 The Transferor Company own Shares in the Transferee Company

If the transferor company owns shares in the transferee company there are several different scenarios and outcomes depending on how the relationship between the two companies is formed. Since the transferring company owns shares in the receiving company one must nonetheless conclude that there is a merger between two, in some way, related companies, and that a so-called absorption is at hand.

The transferred company owns shares in the receiving company, hence, as it is an absorption, the transferred company will be dissolved and its assets incorporated by the receiving company, after the merger has taken place. As the receiving company obtains all of the assets in the transferring company, it would also get hold of its own shares.¹⁰²

According to the Companies Act Ch.7 Secs. 1 & 2, a limited company may not subscribe for, buy or as security obtain its own shares.¹⁰³ However, there are three exceptions of which one correspond to a company that acquires a business in which the shares constitute a part of the transferring company's assets.¹⁰⁴ The shareholder (i.e. the transferred company) is taxed on the capital gain as usual.

In order for the receiving company to obtain a market price for its shares, it must get rid of the shares within three years or they will be dissolved.¹⁰⁵

Merger considerations are paid, though only to those shareholders of the transferring company that does not own any shares in the receiving company.¹⁰⁶ In

¹⁰² Ch. 4 in the Companies Act.

¹⁰³ The provision in the Companies Act that prohibits a company to buy its own shares is said to prevent loss-making companies from risking its own capital in mischief of its creditors.

¹⁰⁴ Ch. 4 Sec. 4 in the Companies Act.

¹⁰⁵ *Ibid.*

this context, the shares indirectly owned by the shareholders in the transferring company would probably not be regarded as being owned by the shareholders, this would consequently block any merger considerations. As all the assets in the receiving company are dissolved in connection with merger, the shares would be sold at the same time. Any payments for the sold shares are taxable. However, in the case of an exchange of shares in connection with the merger, a tax deferral according to the rules on exchange of shares within a group of companies may apply.¹⁰⁷

5.2 The Receiving Company own Shares in the Transferred Company

If the receiving company own shares in the transferred company there are no immediate tax consequences for the shareholders. A parent-subsiary merger is consequently tax-free for the shareholders of the parent company in connection with a merger.¹⁰⁸

Regarding other mergers, it is deemed that the shares have been sold to the receiving company. If the receiving company does not obtain all the shares in the transferring company, merger considerations may be paid, though only to those shareholders that does not own any shares in the receiving company.¹⁰⁹ Any considerations for the sold shares are taxable.¹¹⁰

5.3 Transfer of a Branch of Activity

If a branch of activity is transferred from Sweden to another Member State the established practice in Sweden is that it is tax-free. It must, however, include the

¹⁰⁶ See Ch. 37 Sec. 13 ITA.

Prop. 1999/2000:2 part 2, p. 435.

¹⁰⁷ *Ibid*, prop. 1999/2000:2 part 2.

¹⁰⁸ Riksskatteverket, *Skattehandledning 2002*; part 3, Ch.16, *Fusioner och fissioner*.

¹⁰⁹ See Ch. 37 Sec. 13 ITA.

Prop. 1999/2000:2 part 2 p. 435.

¹¹⁰ According to the rules on exchange of shares within a group of companies, a tax deferral may apply.

entire assets, or the full assets of one of the company's branches of activity and the assets must be transferred from one company to another within the same group of companies, in order for the seller to avoid taxation of any price difference.¹¹¹ The remuneration must however be at arm's length, and must consist of shares in the receiving company (i.e. a consideration other than cash, which is called "apportemission").¹¹²

A transfer of a branch of activity is only possible between a parent company to its subsidiary (whereas e.g. a transfer of assets below market value is possible to transfer both ways, both up and down within the same group of companies).¹¹³

Companies in other Member States qualify under the provisions on transfers of assets in Ch.38 Sec.3, which states that a company is considered to belong to a Member State if it is taxed there.¹¹⁴ A Swedish company that transfers a branch of activity to a company in another Member State will consequently be taxed if these assets and debts are effectively connected to a permanent establishment in a third Member State.¹¹⁵

The most essential criteria, in order to determine if a company from another Member State will qualify for a tax-free transfer of a branch, is whether it is taxed in Sweden.¹¹⁶ In order to make a tax-free transfer the selling company must be liable for tax in Sweden immediately before the transfer, for at least some part of its business.¹¹⁷ The buying company must moreover, immediately after the

¹¹¹ See RÅ 1989 ref.19.

A Branch of activity (verksamhetsgren) constitutes, in this context, a part of business suitable to be separated into an independent business activity. The Swedish definition seems to be consistent to the definition in Art.2(c) of the Merger Directive.

¹¹² Wiman, *Beskattning av företagsgrupper*, p. 121ff.

¹¹³ *Ibid*, Wiman, p.122.

¹¹⁴ It should not have been classified as having its domicile in another Member State according to a tax treaty. In that case it is defined as if it belonged to the other Member State.

¹¹⁵ Losses will not be deductible except when a tax credit would have been granted according to a tax treaty and if the Merger Directive has not been applicable.

¹¹⁶ Ch.38 Secs.6-7.

¹¹⁷ The earnings are not allowed to be exempt from tax because of a tax-treaty. See Wiman, *Beskattning av företagsgrupper* p.147.

transfer become liable for tax in Sweden for the same part of the business, as that of the selling company, before the transfer. The earnings of the buying company are not allowed to be exempt from tax in Sweden due to a tax-treaty.¹¹⁸

5.4 Transfer of Seat to another Member State¹¹⁹

According to the so-called incorporation principle, the seat of the company in Sweden is based on where the company is registered.¹²⁰ The company is consequently destined to follow the rules in the country where the company was funded. Where the company is geographically located is not important, neither where the businesses actually is practised. If the company is founded in compliance with the Companies Act and if it is registered in the Swedish register for limited liability companies, it is consequently bound to follow the Swedish regulations.¹²¹

Emigration of a Swedish company to another Member State is not regulated under company law.¹²² An enterprise that wants to emigrate and cease to be a Swedish company must deregister, i.e. liquidate.¹²³ If a company wishes to change its seat to another Member State the shareholders must consequently change the articles of association and deregister the company, followed by an actual change of seat or registration abroad. The ways to transfer a company's seat may differ depending on which kind of principle that is used for establishment of a seat in the other country.¹²⁴

¹¹⁸ Wiman, *Beskattnings av företagsgrupper*, p.147.

¹¹⁹ Please note that this chapter is based on a private law perspective only!

¹²⁰ *The Companies Act*, Ch. 2 Secs. 1-13.

¹²¹ *The Companies Act*, Ch. 2 Secs. 1-13.

¹²² International Bureau of Fiscal Documentation, *Taxation of Companies in Europe*, GET-II, Suppl. No.151, June 2000, p.24-36.

¹²³ International Bureau of Fiscal Documentation, *Taxation of Companies in Europe*, GET-II, Suppl. No.151, June 2000, p.24-36.

¹²⁴ *Ibid.*

5.5 Anti-abuse Doctrines

The two most important anti-abuse doctrines regarding tax law in Sweden is the Tax Avoidance Act and a principle called “Look through”. These remedies against tax evasion are similar to the anti-abuse clause (Article 11) in the Merger Directive.

5.5.1 *The Tax Avoidance Act*

One of the most questioned laws in Sweden, in the recent decades, is the Tax Avoidance Act.¹²⁵ The legislation is supposed to help Courts to prevent transactions, which is legal in a civil-law perspective although its intention is tax avoidance. The true intention of the taxpayer is supposed to be distinguished from an independent point of view and the taxpayer must have acquired a tax incentive, which is not inconsiderable.¹²⁶ The law is supposed to be practised on a case by case basis and the tax incentive is bound to be the major reason for the transaction.¹²⁷

One of the most important criteria in the Tax Avoidance Act is that the transaction is destined to be contrary to the purpose of the law. This means that the provisions, which create the foundation for the transaction in a civil law perspective (and consequently is applied to avoid tax), would be analogously applicable.¹²⁸ If the Tax Avoidance Act were applicable to the transaction the tax would be based on the real grounds of the operation or as if the transaction never took place.¹²⁹

¹²⁵ *Lag (1995:575) mot skatteflykt.*

Prop. 1994/95:209, bet. 1994/95:SkU30.

¹²⁶ Prop. 1996/97:170 p. 15.

¹²⁷ Prop. 1982/83:84 s 17.

¹²⁸ Prop. 1996/97:170 s 17 f.

¹²⁹ *Ibid.*

5.5.2 The “Look through” Principle

Another important principle in Sweden, which might correspond to the anti-abuse clause (Article 11) in the Merger Directive, is so-called “Genomsyn”. This principle is first and foremost used if the Tax Avoidance Act is not applicable.¹³⁰

Genomsyn means “look through” and it is based on case law. It has been developed by the Supreme Administrative Court in order to impede fake contracts and transfers.

The Court normally checks every part of a transfer independently, hence if it is an obvious simulated action in order to gain tax relief’s, the Court have used the “look through” principle.¹³¹ In the course of using this principle the court looks at every part of a transaction as if it were one collective body, instead of examining each part of a transaction independently, which is the common practice.¹³²

A “look through” is only motivated if the tax consequences are in disparity with the transfer according to civil law and that the action is arranged entirely for tax reasons.¹³³

The result of a fake transaction or contract that has fallen short with the “look trough” principle is that the arranged benefits are denied. The formal (simulated) contract is left without and the actual transaction or action is treated, and taxed, according to what was actually meant to happen, not what was formally arranged.¹³⁴

¹³⁰ *Ibid.*

¹³¹ Prop. 1994/95:209 p. 34.

¹³² *Ibid.*

¹³³ Grosskopf, *Skatteplanering och skatteflykt*, Skattentytt 1989, p 11 ff.

¹³⁴ SOU 1996:44 p. 118.

The Swedish anti-abuse doctrines described above ought to be comparable to those described in the Merger Directive Article 11. One thing that might be controversial is however the application of Article 11 and that of the Swedish anti-abuse doctrines. Since both the Tax Avoidance Act and the “look through” principle are used very restrictively it might be more difficult to stop reorganisations which are performed for tax relief purposes only.¹³⁵

¹³⁵ The impact of the “look through” principle and the Tax Avoidance Act has been criticised over the years as they are seen as a threat to a predictable and uniform law making. For further reading in regard to the Tax Avoidance Law see e.g. Hultqvist, *Legalitetsprincipen*, 1995 p. 392 ff. Grosskopf, *Skatteplanering och skatteflykt*, Skattenytt 1989, p. 11, Bergström, Skattenytt no. 6, 2001. Mutén SST 1992 p. 279 ff.

6 Non-income Tax Questions

6.1 Reorganisation for VAT purposes

VAT is an indirect tax on products and services, which is considered in every element of a transaction until it reaches the consumer.¹³⁶ VAT is, with some few exceptions, present within all transactions connected to business activity.¹³⁷ It does not constitute a real cost for an enterprise, as it is taxable when the company buy a product or a service and deductible when the company sell it. For example, when a foreign company transfers assets (sell a product) within a business transaction, the receiving (buying) company is liable for the tax; a so-called reversed tax liability, that is, if the receiving company is VAT registered in Sweden.¹³⁸

According to Ch.3 Sec.25 in the Value added tax Act (the provision is equivalent with Art. 5.8 in the 6th VAT-Directive) the transfers of assets within a company are however, exempted from VAT if the receiver is entitled deduction or remuneration for VAT. This exception includes transfers of assets in the cause of a merger or other similar procedures. There are moreover, no rules, which states that it has to be a whole branch of activity that is transferred. One fundamental regulation is however, that the transferring company does not have a higher tax pressure than the receiving company.¹³⁹

In the case of divisions there are no specific provisions regarding VAT consequences, the most likely solution is that they are treated in the same way as mergers according to Ch.3 Sec.25 in the Value added tax Act.¹⁴⁰

An exchange of shares is not taxed either, transfers of shares and participation's are, according to Ch. 3 Sec.9 in the VAT-Act, always tax-free.

¹³⁶ Melz Peter, *Mervärdesskatt*, Stockholm, 2001, p. 11 ff.

¹³⁷ Ch. 1 Sec. 1 in *the Value Added Tax Act*.

¹³⁸ Melz Peter, *Mervärdesskatt*, Stockholm, 2001, s. 11 ff.

¹³⁹ Alhager, *Omstruktureringar och moms*, 2002 p. 131ff.

There are four main categories for VAT purposes in regard to international reorganisations.¹⁴¹

1. The selling of the internal assets of a subject in one country to a subject in another country, when the internal assets **remain** in one country and e.g. Ch.3 Sec.25 in the VAT-Act **is** applicable.
2. The selling of the internal assets of a subject in one country to a subject in another country, when the internal assets **remain** in one country and e.g. Ch.3 Sec.25 in the VAT- Act **is not** applicable.
3. The selling of the internal assets of a subject in one country to a subject in another country, when the internal assets **does not remain** in one country and e.g. Ch.3 Sec.25 in the VAT- Act **is** applicable.
4. The selling of the internal assets of a subject in one country to a subject in another country, when the internal assets **does not remain** in one country and e.g. Ch.3 Sec.25 in the VAT- Act **is not** applicable.

In the first example above, there is a reorganisation in which the internal assets **remain** in the country even though the “business” is transferred abroad. The internal assets (i.e. the machines, goods or fixtures) remain in Sweden and the Swedish VAT-Act **is** applicable (Ch.3 Sec.25). As the receiving company switch place with that of the transferring company it also inherits its VAT-position seeing that the internal assets have not been moved out of the country and consequently no tax is paid.¹⁴²

In the second example there is a transfer of internal assets which **remain** in the country even though the “business” is transferred abroad, though Ch3 Sec.25 **is not** applicable. Ch.25 Sec.25 is not applicable if a transfer does not constitute a transfer of a branch of activity or if the transfer is not connected with a merger. That is, the transfer is defined as a normal business transaction and because of

¹⁴⁰ Alhager, *Omstruktureringar och moms*, 2002 p. 136 f.

¹⁴¹ Alhager, *Omstruktureringar och moms*, 2002 p. 168 ff.

that, the transfer is taxed in Sweden. If the transferring company is foreign and not liable to tax in Sweden, the transaction is tax-free.¹⁴³

A transfer of a branch from one country to another is not very common and practically very difficult. In the case where the internal assets (branch of activity) are actually transferred abroad and Ch.3 Sec.25 is applicable, it would probably constitute tax liability for the transferor. The receiving company must, in order to make a tax-free transfer for the transferor, be permitted to a tax deduction according to Ch.3 Sec.25.¹⁴⁴

In the fourth example, there is an actual transfer of the internal assets abroad and Ch.3 Sec.25 is **not** applicable. This is defined as an ordinary acquisition, which means that the receiver of a so-called intra-community acquisition pays the VAT.¹⁴⁵

6.2 Capital Contributions

Every transaction between a parent company and its subsidiary is a capital contribution. A capital contribution can be constituted by bonds, remissions of debts, groups of companies contributions, transfers of internal assets (as machinery etc.), regular disbursements and by taking over the responsibility of a debt.¹⁴⁶

6.2.1 Capital Contributions in General

An unconditional capital contribution from a shareholder is not deductible for the donor and therefore not taxed by the company. The contribution is nevertheless added to the initial share value paid by the shareholder.¹⁴⁷ One condition in order

¹⁴² Alhager, *Omstruktureringar och moms*, 2002 p. 168 ff.

¹⁴³ *Ibid.*

¹⁴⁴ However, it may at the same time constitute an inter-community transfer according to Ch.3 Sec. 30, which would make the transfer tax-free.

See Alhager, 2002 p. 176f.

¹⁴⁵ Alhager, *Omstruktureringar och moms*, 2002 p. 168 ff.

¹⁴⁶ Lodin et al. p. 328 ff.

¹⁴⁷ *Ibid.*

to make a tax-free transaction is that the capital contribution in reality is a contribution and nothing else; the shareholder contribution must consequently improve the financial position of the company. If only some shareholders contribute others may indirectly show a profit on their shares, which might have the effect that the contribution is defined as a gift and therefore taxed.¹⁴⁸

A conditioned shareholder contribution, which is granted with certain restrictions and usually involves a repayment to the donor, is not deductible for the contributor and may not be added to the value of the shares. Such contributions are not an obligation for the company as such, thus for the shareholders. For tax purposes however, a conditioned shareholder contribution is seen as a debt from the company to the donor and the repayment is defined as a tax-free refund for a loan.¹⁴⁹

There is a deliberate incoherence between company law and tax law regarding capital contributions. A repayment of a shareholder contribution is seen as a dividend in company law matters, and as a refund for a loan in tax law matters. This incoherence, which is based on case law, is justified by the need of a tax provision that constitutes a tax-exception for shareholder contributions.¹⁵⁰ One might think that it would have been easier to make an exemption in the ITA regarding conditioned capital contributions in order to avoid this incoherence but so far no such provision has been introduced.¹⁵¹

6.2.2 Over-capitalisation

If a group of companies does not have the possibility to use tax-free group contributions it might use over-capitalisation as an alternative way to transfer

¹⁴⁸ In the case NJA 1960 p. 642 I & II, the Court defined the shareholder contributions as gifts and the shareholders which gained on the transactions was taxed. Even the contributor themselves was taxed, since the court considered the contribution to the company as a gift to themselves! A shareholder contribution that is made in order to save a company from liquidation is never taxed as it increases the financial position of the company and not primarily the shareholders.

¹⁴⁹ Lodin et al. p. 328.

¹⁵⁰ Prytz and Tamm, p. 128.

capital.¹⁵² The parent company lends money and uses them to make a capital contribution to its subsidiary. The subsidiary then invests the capital and pay tax in the country where it is situated. Finally the gains of the invested capital are transferred as a dividend to the parent company. By using over-capitalisation the parent company avoids being taxed in its own country and may benefit from lower tax rates.

6.3 Stamp Taxes and Reorganisations

Sweden has no stamp taxes on purchases of shares. The previous purchase tax on shares amounted to 2% of the value when a new company was formed or when an existing company issued new shares.¹⁵³ The reasons for abolishing stamp tax on shares were that the government thought it hindered the development of beneficial conditions for the economic life, in particular for small- and medium sized companies. To pay tax for a business which was not even started seemed unfair and unsound according to the governmental bill.¹⁵⁴

¹⁵¹ *Ibid.*

¹⁵² The Swedish term is räntearbitrage.

¹⁵³ *Lag (1984:405) om stämpelskatt på aktier.*

Prop. 1994/95:25 p.25.

Ståhl/Österman, *EG-skatterätt*, p.260f.

¹⁵⁴ Prop. 1994/95:25 p.49.

Sweden has chosen to ignore stamp taxes entirely and consequently EU Directive 69/335/EEG is not applicable.

7 Remarks on Harmonisation

The overall economic framework has changed significantly since the early nineties. An unprecedented wave of international mergers and acquisitions, the emergence of electronic commerce and the growing development of tax havens all change the fiscal situation for companies within the European Community. These general global developments are still in progress and are particularly strong within the Internal Market.

As company tax arrangements have a tendency to create obstacles to a commercially straightforward organisation many might think that a uniform law on reorganisations would improve business development within the Internal Market. It could also be argued that the coherence between company law and tax law is one of the most important steps in order to tackle the complex legislation on reorganisations.

Though tax arrangements applying to cross-border reorganisations, covered by the Merger Directive, have existed since 1990, there are still no corresponding company law provisions. The company law directive (on cross-border mergers on public limited companies) which aims to permit and regulate cross-border company mergers has not yet been adopted.¹⁵⁵

The lack of improvements on a company law level is unfortunate and the poor legislation regarding mergers is of course a source of extra costs for companies that are unable to improve their organisation. Currently only cross-border transfers of assets or exchange of shares can be undertaken in all Member States.¹⁵⁶ A uniform adaptation of the existing Merger Directive would probably change this situation.

¹⁵⁵ *Tenth proposal for a Council directive on cross-border mergers on public limited companies* (COM (84) 727 final of 8 January 1985).

¹⁵⁶ *Company taxation in the internal market*, COM 2001 (582) Final, p. 234.

In the case of cross-border mergers and divisions there is still a problem with the fact that some national legislations do not allow companies to be absorbed or divided by foreign companies.¹⁵⁷ If cross-border mergers or divisions of companies are not legally possible, the Merger Directive has no effect.

One important feature of the Swedish implementation, that stretches further than the aims of the Directive, is that the provisions in the Merger Directive are applicable on domestic reorganisations. The definitions in national law regarding domestic reorganisations are therefore not supposed to be different compared to the legislation on cross-border reorganisations. In accordance with the EC Court's ruling in the *Leur Bloem-case*¹⁵⁸ the EC law is applicable on national situations when the applicable regulation covers both national and harmonised situations. So consequently the Swedish regulations on reorganisations are applicable on both cross-border and domestic reorganisations.

This is the most natural solution and moreover the most preferable one. By enacting the Merger Directive to cover domestic reorganisations as well, the difficulties with two separate systems are eliminated. A uniform legislation within the whole of the European Community would be easier to apply and that is necessary in order to prompt the development of a completely coherent and common system on reorganisations.

¹⁵⁷ E.g. Sweden regarding divisions.

¹⁵⁸ C-28/95 A. *Leur-Bleum v. Inspecteur der Belastingdienst/Ondernemingen Amsterdam 2* REG 1997.

If national rules in all Member States are adjusted to cover domestic reorganisations, it would ease the effort towards a fully satisfactory implementation of the Merger Directive in the whole Community, as the impact of such legislation would grasp to adjacent national legislation and by doing so, come to an end with rigid national schemes.

A uniform enactment of the Merger Directive that would cover domestic reorganisations would consequently pick up the pace on harmonisation.

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