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Cross border mergers in Sweden; Whether the Swedish merger rules comply with EU law

by

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Abstract

Background:

In Sweden, mergers between Swedish parent companies and domestic subsidiaries are in most cases carried out with a continuation of the tax burden, while mergers between Swedish parent companies and foreign subsidiaries are, in principle, not. The exception is when the Swedish intra-group deduction rules apply. However, they are very limited in their scope and application. It is uncertain whether such difference in treatment between domestic and foreign subsidiaries is compatible with Sweden's obligations towards the EU.

Results:

In regards to cross border merger rules, EU law makes a difference between rules which are built upon the Merger Directive and those who are not. When the directive applies, domestic and foreign subsidiaries are, in principal, to be treated in the same way. However, in regards to mergers which do not qualify for the benefits of said directive, EU law allow for some difference in treatment between domestic and foreign subsidiaries. Nevertheless, in a merger, a taxpayer must, as a minimum standard, be able to deduct losses in a foreign subsidiary, if the losses are considered final in accordance with the case law of the CJEU.

Conclusion:

The Swedish rules which are adopted based on the Merger Directive are incompatible with EU law. The Swedish rules applicable to other kinds of mergers are incompatible with EU law in regards to their limited loss calculation, however, compatible with EU law in regards to their limitation to factual losses.

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In August I am starting to work as a tax consultant at EY in Stockholm and I would not have been there if it was not for all persons around me. Matilda, my family, my friends, my mentors and my teachers in Växjö, Lund, Stockholm, Gothenburg, Malmö and so fourth. Many of you mean more to me than you can imagine.

Lastly, it has been a tough year and it is great that it is finally coming to an end. The Masters Programme in European and International Tax Law is, from a studies perspective, like nothing I have ever experienced before. If anyone interested in the programme would ever read this all I will say is; be prepared for a lot of studies but also a lot of fun.

Table of Contents

List of Abbreviations

ABL : Law for Companies with Limited Liability (Aktiebolagslag (2005:551))

ATAD : Anti Tax Avoidance Directive

ATR: Advanced Tax Ruling

BATR : Board for Advanced Tax Rulings

CJEU : Court of Justice of the European

EEC : European Economic Cooperation

EU : European Union

MD : Merger Directive

PE : Permanent Establishment

Prop. : Proposition (the word has the same meaning in Swedish as in English)

PSD : Parent-Subsidiary Directive

Ref. : Commentary (Referat)

RÅ : Annual Publication of the Swedish SAC (Regeringsrättens Årsbok)

SAC : Supreme Administrative Court (of Sweden) (Högsta Förvaltningsdomstolen)

SITA : Swedish Income Tax Act (Inkomstskattelag (1999:1229))

STA : Swedish Tax Agency (Skatteverket)

TEU : Treaty on the European Union

TFEU : Treaty on the Function of the European Union

1 Background

1.1 Background to the issues in Sweden

1.1.1 The pending case before The Supreme Administrative Court of Sweden

In July 2016, the Swedish Board for Advanced Tax Rulings ("BATR") delivered a decision on the utilisation of foreign losses in Sweden, when a German subsidiary was being merged into a Swedish parent company.[1] Due to continuous losses, the German company was to be wound up and the operations in Germany would stop in its entirety. Therefore, the company asked the BATR to determine whether the Swedish parent company would have the right to deduct the losses in Germany if the German subsidiary would be absorbed by the Swedish parent.

The facts of the case, which were undisputed, were that there were no other company in Germany in which the existing losses could be utilised in, and therefore no existing or potentially future profits to offset the loss against. Another fact was that the transaction would not fulfil the criteria of being a so called "qualified merger" and would not allow the parent company for a deduction in accordance with chapter 37 of the Swedish Income Tax Act ("SITA"). The reasoning behind the latter was due to the fact that the subsidiary was not taxable in Sweden prior to the merger, something which is stipulated as a prerequisite in paragraph 11 of stated chapter. However, the taxpayer held the legislation incompatible with EU law and that a deduction of those losses should, nonetheless, be allowed according to those rules, in the same way as would had been done if the subsidiary had been established and taxable in Sweden. The Swedish Tax Agency ("STA") agreed that not allowing for the deduction of losses from foreign subsidiaries was incompatible with European Union ("EU") law but that the loss must be limited through application of chapter 35 a of the SITA, which regards so called intra-group deductions.

The majority of the BATR (6/9 board members) held that the demand for "taxable in Sweden prior to the merger" was proportional and compatible

[1] See decision of 2016-07-07, the BATR, Advanced Tax Ruling, dnr 30-14/D.

with EU law. They argued that since Germany has no rules which allow the carry forward of losses through domestic mergers, the taxpayer should have no right to deduct the losses, as the losses could not be considered final. The majority relied upon previous case law from the Swedish Supreme Administrative Court ("SAC") which states that Sweden should not be demanded to heal a flaw in another Member States tax treatment[2] and that the Court of Justice of the European Union ("CJEU") case *K*[3] proved that such limitation in the utilisation of losses is compatible with EU law.

As tax rulings only need a majority vote to become final the taxpayer was disallowed a deduction of the loss. However, the minority of the board (accordingly 3/9 board members) still held that the parent company should have the right to deduct the losses based on the *Marks & Spencer*[4]-doctrine. The minority stated that the criteria stipulated in that judgement had been fulfilled and that denying a deduction of the loss based only on the treatment in Germany was incompatible with EU law and thus, disagreed with the interpretation of EU law made by the majority. The decision, which is binding for the taxpayer and the STA, has been appealed by both the taxpayer and the STA and is now pending before the Swedish SAC.

To fully understand the complexity and the underlying reasons to the decision, the fundamental issues of mergers in general and the specific issues related to Sweden must be brought into light.

1.1.2 Mergers in general and why issues exist in cross border situations

In an international perspective, the term "merger" refers to a transaction which combines two businesses by transferring ownership of the businesses to a single entity, however, a merger may also be the restructuring of two or more companies so they come under a common owner.[5] In the process of a merger, the dissolved entity or entities are being stripped of their current legal personality and loses their right to carry on rights and obligations – rights which then, taking Sweden as an example, are carried forward by the successors.[6] From a tax perspective the loss of legal personality also lead to the loss of rights for states to impose taxes on the entity being dissolved in the merger, as the assets, on which taxes are levied, are no longer attributable to the formerly existing legal entity.

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[2] See, RÅ 2009 ref. 13-15.
[3] Judgement of 7 November 2013, *K*, C-322/11, EU:C:2013:716.
[4] Judgement of 13 December 2005, *Marks & Spencer*, C-446/03, EU:C:2005:763.
[5] See explanation, "merger, n.1." *OED Online*. Oxford University Press, March 2017. Web. 3 June 2017.
[6] See for instance, ABL 23:34.

As stated, problems with mergers arise in connection to the change of ownership of either a company, or the assets of a company. From the tax perspective, some of the issues of mergers can be deduced from rulings, for instance in the CJEU. These amount to, apart from (1) the loss of legal personality by one or more of the entities involved, issues connected to (2) the valuations of the transferred assets and/or entities, (3) the potential continuity of the tax burden or (4) related to the abuse of law, that is, if the merger is carried out without commercial reasons.[7]

In addition to this, issues arise in cross border situations as the parties to the cross border activity then resides in different jurisdictions. Then, two or more states might claim rights to tax the same assets. Disparities between legal orders and inconsistent application of rules can also lead to assets being taxed twice or not at all.[8] As there is no common exhaustive international legal order for neither legal ownership nor the taxation of businesses, rules are in principle determined by each jurisdiction. Furthermore, in cross border mergers one state might not just lose their right to tax the entity further on, but they might lose their right to tax what would have been fully taxable in their jurisdiction prior to the merger.[9]

The issues of mergers from a tax perspective can be described through the following scenarios;

Scenario 1.

Two companies exist in this scenario. Company X in country A and company Y, a wholly owned subsidiary of X, who also resides in country A. Both companies are recognised by their domestic law as legal personalities with the right to carry on rights and obligations. They are also subject to tax in their tax jurisdiction, thus company X and Y will be taxed in country A. Domestic rules apply accordingly.

The management of company X has decided to merge company Y into company X (thus becoming XY). After the merger company Y will cease to exist and will be stripped of its legal personality and, from a legal perspective, there will no longer be any tax subject called ”Y”. Instead the only legal personality subject to tax further on, will be X as it has absorbed Y (XY).

As no cross border element is existing in this scenario, the merger will be a domestic issue for country A. Tax issues that arise in this context can for instance be connected to valuations and tax continuity. Tax continuity in regards to mergers relates to when the acquiring company, who absorbs the dissolved company, also takes on the tax position of its predecessor. When

[7] See for instance, Judgement of 21 February 2013, *A OY*, C-123/11, EU:C:2013:84.
[8] See for instance, C-446/03, *Marks & Spencer.*
[9] Compare a merger to the shift of tax residency in Judgement of 29 November 2011, *National Grid Indus*, C-371/10, EU:C:2011:785.

criteria for tax continuity are met, tax that would normally be due on, for instance the untaxed value of the acquired shares, is postponed until a later point in time. This is also known as a deferral of taxes.[10]

Nevertheless, the treatment of domestic mergers is in principle not a problem in an international context as international legislations such as, for instance EU law, or legal acts as double tax treaties, only regulate cross border situations. Thus, not a problem to be solved by neither bilateral agreements nor EU law. Furthermore, from a state perspective, there is a symmetry in this scenario taking into account for both profits and losses. However, in the second scenario we include a cross border element;

Scenario 2.

Three companies exist in this scenario. Apart from company X and Y in country A, being structured the same way as above, there is now a third company ”Z” as well. Z is also a wholly owned subsidiary of X. However, it resides in country B. All companies are once again recognised by their domestic laws as legal personalities with the right to carry on rights and obligations. They are also subject to tax in their tax jurisdiction.

The management in company X has decided that the subsidiaries Y and Z should be merged into the parent company X.

Through the merger the companies Y and Z will become part of company X and lose their legal personalities, and in turn they can no longer carry on any rights or obligations. They also lose their personalities as taxable subjects.

The merger between X and Y will be the same as in scenario 1.

However, the suggested merger will lead to a situation where country B becomes deprived of its right to tax the assets of company Z further on. In a scenario where company Z carries on profits or losses at the moment of the merger, the symmetric treatment of the profits and losses in country B is broken. A deferral of the taxes in company Z would mean that country B would lose out on taxing any untaxed assets in company Z, which country B would have had to the right to tax, had company Z continued to exist there. Thus, country B might want to safeguard their right to tax the untaxed values. In most cases this is done by a so called exit tax which essentially protects the domestic tax base and makes sure that country B is granted the right to the taxation of untaxed gains even though the gain is not realised.[11] Untaxed gains are, as essentially stated, most often the inherent increased value of an asset or entity. This connection exists as most states consider that this untaxed value should be attributable to their state because of the

[10] See explanation, "defer, v.1." *OED Online*. Oxford University Press, March 2017. Web. 3 June 2017 (subsection 2(a)).
[11] See case C-371/10, *National Grid Indus.*

operations carried out in their jurisdiction giving rise to that increase in value.[12]

At the same time, if country B applies an exit tax, issues regarding country A's right to tax the same assets in the jurisdiction of A could arise, if country A does not recognise the treatment of country B. This could for instance lead to double or non-taxation of gains on the same asset.

Nevertheless, there are also situations relating to the opposite scenario, being when company Z carries on losses. In that situation, country A can be the one that tries to establish limits to the recognition of such losses and might want to protect their tax base as that country would be the one loosing out on tax revenue if A fully accept to take the loss of the inherited company into account in the jurisdiction of A.[13] Allowing for the deduction of the losses in Z would, thus, lead to the symmetry between profits and losses being broken once again just as for exit taxes. Those scenarios must not only entail actual losses, but can also include the overtaking of debts or assets and the right to deduct decreasing or increasing values on those assets and debts.

Evidently, cross border mergers can create problems for both taxpayers and states. In Sweden, taxation is carried out on a global basis, nevertheless, a subsidiary abroad is an establishment over which Sweden has no taxing powers as it not registered in Sweden.[14] Thus, Sweden have no rights to take on the profits of a foreign subsidiary and, evidently, Sweden will be reluctant to take on the losses of the same company, as that would lead to an asymmetric treatment of profits and losses. Looking back at the decision from the BATR, it becomes apparent why the state wants to limit the deduction and protect their tax basis, as the loss did not arise in Sweden. However, one may then ask the question of why there is a problem in Sweden related to a German subsidiary.

1.1.3 Mergers in Sweden and the effects of EU law

Through the entry into the EU in 1995, Sweden gave up some of its' sovereignty in exchange for access to the internal market. By entering into the Union, Sweden also had to accept that Swedish laws must align with the Treaty on the Functioning of the European Union ("TFEU"). Thus, the TFEU is the primer legal act in Sweden.

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[12] Compare to, for instance, Council Directive (EU) 2016/1164, of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market, (the "ATAD"), preamble, paragraph 10

[13] See for instance, Judgement of 3 February 2015, *Commission vs UK*, C-172/13, EU:C:2015:50.

[14] See chapter 6, paragraphs 3 & 4 of the SITA.

Furthermore, at the time, several directives had already been implemented in the EU, one of them being the Merger Directive ("MD")[15], and Sweden was obliged to transpose that directive into the Swedish legislation. The purpose of the MD is to make it easier for companies to restructure themselves within the EU, limiting the tax consequences,[16] this is done by postponing the moment of when untaxed gains are to be taxed.[17]

In Sweden, this implementation lead to the current Swedish legislation regarding mergers, which can be found in chapter 37 of the SITA. These rules did not exist prior to the implementation of the MD and the rules are based on the scope and definitions found in the directive.[18] Prior to the implementation of these rules the Swedish rules on mergers were also much less developed in general.[19] Especially, the rules were underdeveloped in regard to mergers through so called absorptions, and the introduction of the MD required a broadening of the scope of those rules, both in regards to civil law as well as tax law.[20] Furthermore, the introduction of the MD, and also the introduction of new civil law rules, opened up the possibility of entering into cross border mergers, something which was impossible before.[21]

Based on this, it would seem to the reader that mergers were a completely new phenomenon to Sweden, however, that is not the entire picture. In Sweden, as will be further shown below, the tax legislation allows groups of companies to apply rules which essentially means that mergers between associated companies can be carried out without tax consequences.[22] Furthermore, Sweden also has rules which enables companies an unlimited so called carry-forward of losses, which means that tax losses from previous years can be utilised for tax purposes in forthcoming fiscal years.[23] These sets of rules in combination create a possibility for transactions equivalent to mergers and a system of almost unlimited loss utilisation within company groups.

Thus, Sweden introduced rules regarding mergers in addition to already existing rules on intra-group contributions, which, in essence, can be used to

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[15] See Council Directive (EU) 2009/133/EC of 19 October 2009 on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different Member States and to the transfer of the registered office of an SE or SCE between Member States

[16] See *Merger Directive*, Council Directive (EU) 2009/133/EC, preamble paragraph (2)

[17] *Ibid*., preamble paragraph 7.

[18] Compare, SITA 37:3 & 5 to *Merger Directive*, Council Directive (EU) 2009/133/EC, article 2.

[19] See, Ståhl, K, *Fusiondirektivet, Svensk Beskattning i EG-rättslig* belysning, p.41-42.

[20] *Ibid.,* p.41-42.

[21] See ABL 23:36, introduced based on Directive 2005/56/EC of the European Parliament and of the Council of 26 October 2005 on cross-border mergers of limited liability companies.

[22] See chapter 35 of the SITA

[23] SITA chapter 40 regarding, "*Tidigare års underskott"*

serve the same purpose. As such, these rules are in practise targeting the same situations but still co-exist as two different parts of the Swedish tax legislation.

Going back to EU law, the TFEU stipulates through the freedom articles, that equal treatment shall apply between nationals of the different Member States.[24] Thus, a national of one Member State should not be treated worse than a national of another. This includes that it is incompatible with EU law to apply different rules to what is known as "comparable situations", or applying the same rules to "non-comparable" i.e. different situations.[25] Thus, EU law essentially requires Member States to enact tax rules which do not create a difference in treatment between domestic and foreign taxpayers.

This is where the issues of the Swedish rules start. The Swedish rules on group taxation are only applicable to companies with tax residency in Sweden. Thus, these rules create a difference in treatment between taxpayers established in Sweden compared to taxpayers established in another Member State, something, which, in principle, is prohibited by the TFEU and thus, perhaps make these rules incompatible with EU law. Looking back at the decision from the BATR, the taxpayer argues for an application of the same rules as would have been applied domestically, despite the fact that the subsidiary is established in Germany which accordingly should be the case if the rules are incompatible with EU law.

However, the reader might then ask why these rules should govern the cross border merger, when rules regarding cross border merger exist through the implementation of the MD. Since the Swedish intra-group contribution rules apply to the same situations as the merger rules, it seems, from the decision from the BATR, as if the the rules also practically apply as part of one set of rules. Furthermore, as will also be shown below, apart from the factual issues of the case, the way the Swedish merger rules have been implemented, make them virtually impossible for foreign subsidiaries to access. It is, however, uncertain whether such *de facto* difference in treatment, in regards to the implemented rules, is compatible with EU law.

Nevertheless, the nationality restriction in the rules on the Swedish group taxation rules has led to the implementation of the rules regarding intra-group deductions. This legislation was enacted in response to the *Marks & Spencer*-ruling[26] of the CJEU, known as the start of the *final loss*-doctrine, and the rules makes it possible to deduct a loss in a foreign subsidiary if it is considered to be "final" in accordance with that legislation. However, these

[24] See for instance, *Freedom of Establishment*, art. 49 of TFEU
[25] See for instance Judgement of 14 February 1995, *Schumacker,* C-279/93*,* EU:C:1995:31, paragraph 30.
[26] Case C-446/03, *Marks & Spencer*

rules are limited in several ways and it is not evident that these rules are themselves compatible with EU law either.

Evidently, from a Swedish perspective, dealing with cross border mergers means not just dealing with the merger legislation in itself, but also rules regarding intra-group contributions and intra-group deductions. The three sets of rules practically apply to the same situations and therefore, based on the fact that they treat foreign situations differently in comparison to domestic ones, the rules can be questioned on their compatibility with EU law, either as separate legislations or taken as a whole.

1.2 Aims and question of the thesis

The aim of the thesis is to find out whether the Swedish merger legislation as a whole is compatible with EU law. The question of the thesis can be phrased as; What are the criteria and limitations of EU law in connection to national laws on loss relief in the context of cross border mergers between Member State of the EU and is the Swedish legislation compatible with these criteria?

The aim is to do this by comparing the law as it stands in Sweden to the law as it stands in EU law. More specifically, the aim is to provide for an analysis of the framework and the limits of the principles set out in the jurisprudence of the CJEU in connection to cross border mergers. Furthermore, based on the conclusions drawn in the analysis, it is the aim of the author to provide for a qualified and valid comment on how the Swedish SAC should settle the pending case regarding a cross border merger between Sweden and Germany. The aim is also to provide for a proposal on how the Swedish legislation could be amended.

1.3 Method and material

The material in this thesis was updated till 1 June 2017.

As the thesis is trying to establish whether the Swedish legislation is compatible with EU law, the method used in the thesis is the legal dogmatic research method. The legal dogmatic research method tries to establish the law as it stands from a positivist normative perspective by applying written

and unwritten rules, principles, concepts, case law, doctrines and literature.[27] It can be said that the method essentially tries to establish how the law *should* be applied rather than describing how the law is *actually* applied. As the thesis involve both Swedish law as well as EU law, it is fundamental for the reader to get acquainted with the law as it stands both in Sweden and in the EU. The jurisdictions have different legal sources as well as different hierarchies for those sources which means that the sources will be different. Nevertheless, the sources are handled the same way as the method suggests, by identifying the sources, by analysing them, by systemizing them and lastly by confronting them with each other in an academic way.[28]

In the background, references are made to the case law of the CJEU and the ATAD, despite talking about mergers internationally. The author's reason behind this was to support the explanation regarding mergers with empirical evidence of some kind, without obliging the author to conduct an empirical study of its own.

In the presentation of the Swedish law, it becomes necessary to provide for a translation of the Swedish legal sources. The translations of the Swedish sources are the author's own, which can entail small discrepancies in the language between English and Swedish and could in some cases mean that there is a more accepted translation. The primer source of law in Sweden is the legislation which is thus the starting point. In addition to the written law the rulings from the SAC are deemed to have the second highest value in the legal hierarchy together with the preparatory works carried out when stipulating laws. However, case law from the SAC always supersede if the two sources collide. Nevertheless, the preparatory works are important in Sweden as they provide for a wide background to why the laws were enacted. Therefore, it is natural to use them as part of the explanation. Last in the Swedish hierarchy are the publications by legal researchers and other legal publications, such as official statements from the STA. In connection to this, the Swedish law also allows for so called Advanced Tax Rulings ("ATR"). An ATR is a legally binding decision between a taxpayer and the STA which is decided by a board of tax experts known as the BATR. An advanced ruling does however have no jurisprudential status, nor any higher legal status than academic publications or an official statement from the STA. Nonetheless, both ATRs and the STA statements have a lot of practical value which makes them interesting to analyse.[29]

In the parts regarding EU law it is natural to start in the TFEU as that is the primer legal source in the EU. In connection to this it is also natural to look

[27] Vranken in Douma, S, Legal Research in International and EU Tax Law, Kluwer, 2014, p. 18
[28] Douma, S, *Legal Research in International and EU Tax Law*, Kluwer, 2014, p. 20.
[29] Explanation to the Swedish legal hierarchy can be found in for instance, Sandgren, Claes, 2006, *Rättsvetenskap för uppsatsförfattare*

at the case law of the CJEU as the court is the ultimate interpreter of EU law.[30] The cases that has been chosen for the analysis are the ones that are either referred to the most in other cases of the CJEU or in doctrinal articles. The choices have also been influenced by the materials dealt with during the Masters programme. In addition to the case law of the CJEU the thesis deals with opinions of the Advocate Generals ("AG") as well as doctrinal publications. The opinions of the AGs, which are not binding for any part but merely guidance and have the same legal status as legal research, have been used to provide for a background to cases or to enhance the argumentations both in the description of the law as it stands as well as the analysis of the author. The opinions of the AGs are useful for that purpose as they often develop around concept and principles or provide for a wider context than rulings in the CJEU. The legal research articles used to complement the reasoning of both the CJEU and to enhance the authors own arguments are articles written primarily by scholars and published in the most recognised legal papers in the EU as well the most recognised legal papers in Sweden.

Furthermore, due to objectivity reasons the author has refrained from using any source which could be affected by personal agendas.

1.4 Delimitations

The thesis will only be looking at the Swedish rules and thus analyse the criteria and distinctions made in the Swedish law and compare it to EU law.

The thesis will be looking at the issues regarding merger from a perspective where Sweden is the state of residence. Issues relating to source taxation, such as exit taxes can some times be commented shortly but without any analysis. The main reason for this is because the author believes that the Swedish exit tax rules, in general, comply with the criteria stipulated in the case law of the CJEU (perhaps with minor adjustments). The Swedish exit tax rules also seem to be in line with the criteria in the ATAD, which means that even after an adoption of that directive, the rules would persevere. In connection to this, mergers between standalone companies have been left outside the thesis and the thesis will primarily deal with affiliated companies. The reason behind this is, if companies in Sweden do not meet the requirements for tax consolidation, exit taxes apply even domestically. Thus, making these rules less interesting to analyse from an EU law compatibility perspective.

[30] See for instance TFEU art. 263

Furthermore, the Swedish merger rules contain several technicalities and it is possible that other parts of the intra-group contribution legislation contain issues related to the EU compatibility. However, these issues will not be dealt with due to the extent of thesis and as the latest decision from the BATR pending before the SAC are connected to valuation of losses and the recognition of the laws in other Member States those seemed to be the most interesting topics to write about.

In the analysis of EU law, the thesis is limited to the fundamental freedoms and in part the MD. At the start of the thesis, it was the aim of the author to provide for a discussion regarding issues in connection to the Swedish application of the directive. However, the discussion regarding the MD will be very limited. This is due to, as will be shown below, that in practise, Sweden does not apply the rules of the directive. In addition to this, as the Swedish "final loss-rules" apply instead, it is to be noticed that several authors have already written academic articles in regards to the *final loss*-doctrine of the CJEU.[31] However, the Swedish application of this doctrine is not dealt with in those publications and therefore still an interesting topic to write about.

Potential State Aid issues are also left outside of the discussion found in the thesis despite that being part of EU primary law.

Furthermore, tax treaties are an integral part of the sphere of international taxation and even though Sweden as well as many other EU countries have committed to such agreements they are not directly part of EU law and for the most part left outside of the thesis.

1.5 Outline of the Thesis

The thesis will continue in part 2 by a more detailed description of the Swedish laws applicable in cross border merger, as to provide for a benchmark to compare to EU law. In part 3 the author first analyses whether the Swedish rules amount to a discrimination or a restriction of EU law. Then the author goes on to analyse the potential justifications of such discrimination or restriction. The proportionality of the potential justification is discussed in part 4. Lastly, the thesis is summarized and conclusions are drawn in part 5.

[31] See for instance, Lang. M, *Has the Case Law of the ECJ on Final Losses Reached the End of the Line?*, 2014, European Taxation or Danish, M, *What remains of the Marks and Spencer Exception for Final Losses? – Examining the Impact of Commission v. United Kingdom (Case C-172/13),* 2015, European Taxation

In some parts an analysis of the Swedish rules and/or application of the law will be drawn directly in connection to the descriptive text, while in some parts the Swedish legislation is being analysed in a subchapter of its own. This distinction if primarily drawn on the relevance of that chapter for the overall aim of the thesis.

2 The Swedish rules

2.1 The Swedish rules on cross border mergers

2.1.1 Qualified and unqualified mergers

It was previously stated that the Swedish rules regarding mergers are based on the MD, these rules are found in chapter 37 of the SITA. In Sweden, mergers are split into two classifications. First there are the so called ”qualified mergers”, which in short can be explained as the mergers which fulfils the criteria set out in the MD. When these rules apply, tax continuity applies and no capital gains tax normally due will be subject to taxation until a later point in time. The transferee also takes on the position of the transferor regarding the value of assets and obligations.[32] However, these tax rules are limited to domestic as well as cross border mergers within the EU/European Economic Area (“EEA”).[33] Secondly, mergers which do not fulfil the criteria of the MD are *a contrario* called ”unqualified mergers”.[34]

The rules apply either when a Swedish company is the transferor i.e. the company being dissolved or the transferee i.e. the company absorbing the transferred company.[35] The transferor must prior to the merger be taxable in whole or in part and, the transferee must, immediately after the merger, be fully taxable.[36]

Furthermore, the requirements for the transferor to take part in a qualified merger are stated as being, “in part taxable” and that “the income cannot in its entirety be tax free according to a tax treaty”.[37] According to Andersson M. et Al.[38] the paragraph must be read as “taxable according to the SITA”.[39] Even though the wording of the legislation stipulates no such demand, the same statement can be found in the preparatory works to the first

[32] See SITA 37:17 & 18
[33] See SITA 37:4 with reference to paragraphs 11-15 in the same chapter.
[34] See SITA 37:4, *a contrario.*
[35] See SITA 37:11 and SITA 37:12.
[36] See SITA 37:11 & 12
[37] See SITA 37:11.
[38] Mari Andersson, Judge of the Swedish SAC, Anita Saldén Enérus, Judge of the Swedish SAC & Ulf Tivéus, tax professional at Skeppsbron Skatt.
[39] See Andersson, M, et. Al., 2017, *Inkomstskattelagen – en kommentar*, commentary on chapter 37, paragraphs 11 & 12.

introduction of the merger rules[40] and in preparatory works to the amendment of the Swedish tax legislation.[41] Thus, a merger can only take place if the transferor is in part taxable according to the SITA. In turn, a company established in another Member State, for instance a subsidiary of a Swedish parent, would need to be taxable in Sweden, for example, through a Permanent Establishment ("PE") to fulfil that criterion. If that is not the case, a subsidiary cannot be part in a qualified merger according to the implemented Swedish rules. As a consequence, the Swedish implementation essentially requires the transferor to be established in Sweden.

The Swedish Board for Advanced Rulings held, in 2008, that the Swedish implemented legislation constituted a restriction of the freedom of establishment. Furthermore, the board believed that the restriction would be hard to justify.[42] However, even though the ruling was appealed to the SAC, it was decided without the SAC neither requesting a preliminary ruling from the CJEU nor without a publishing of the decision. As the question has not been appealed since, there is no Swedish jurisprudence to rely on regarding how Sweden actually applies the provision.[43] Without any further jurisprudence, the part taxable according to the SITA must be considered to be the law as it stands. Thus, a cross border merger cannot be treated as qualified if the transferor is established abroad without being at least in part taxable in Sweden. In practise making almost all cross border mergers fall short of the qualification.

In the cases of mergers which do not fulfil the criteria for tax continuity, the adopted rules of the MD are, thus, inapplicable and instead the taxation of these mergers are to be determined based on the general domestic rules for company taxation. These "unqualified mergers" include domestic, as well as cross border mergers and the rules regarding intra-group contributions and intra-group deductions apply to those merger per analogy. This is because of the fact, as we saw in the previous chapter, that a merger between two domestic companies can be carried out without actual tax consequences even if the merger falls out of the criteria in the MD, if these rules become applicable.

2.2 Intra-group contributions

Companies in Sweden are standalone entities for tax purposes. However, to simplify the tax treatment of company groups, Sweden applies a tax

[40] See Prop. 1998/99:15, p. 221.
[41] See Prop. 1999/2000:2, part 2, p.434.
[42] See decision of 2008-01-28, the BATR, Advanced Tax Ruling, dnr 26-07/D.
[43] See The SAC, judgement number 7565-08.

consolidation regime, found in chapter 35 of the SITA, with the purpose to reduce the tax liabilities for a company group to the same level as standalone entities.[44] For the rules to apply a parent company must own more than 90% of the shares in a subsidiary.[45] Thus, it only applies to companies where the parent company exercises a definite influence over the subsidiary.

The consolidation regime works in such a way that groups of companies, which fulfil the criteria for the consolidation regime, can make contributions between affiliated companies in the group. These contributions are considered deductible for tax purposes for the payer and considered taxable income for the payee.[46] As such a loss in one group company can be utilized by way of transferring profits, or rather income, from the income making affiliated company to an affiliated company carrying a loss. Furthermore, an actual loss or gain is not necessary to fulfil the criteria of sending an intra-group contribution as there is nothing in the legislation that puts limits on the contributions. Thus, a contribution can be sent from one company to another even if it creates a loss in the first company.[47] Even though the rules primarily target a parent-subsidiary situation, contributions can also be sent between subsidiaries of the same parent, as if it would have been sent through the parent.[48] Mergers are also treated as an intra-group contribution leading to a merger with no tax consequences if the same criteria are met.[49]

The rules regarding intra-group contributions are, as previously stated, only applicable to affiliated companies with tax residency in Sweden, or a company with tax residency in the EU/EEA who carries on a PE in Sweden (intra-group contributions can be sent from a Swedish company to the PE or vice versa, when the PE is resident for tax purposes in Sweden). This is due to the fact that an intra-group contribution only becomes deductible for the payer if the contribution is taxable in Sweden in the hands of the payee.[50]

However, in response to the *Marks & Spencer* and *A OY*[51] rulings in the CJEU, where the court, in essence, held that a taxpayer should be able to deduct a loss in a subsidiary established abroad which is considered final,[52]

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[44] See Prop. 1999/2000:2 p.421.
[45] SITA 35:2.
[46] SITA 35:1.
[47] See for instance, The STA, 2017, *Vad är ett koncernbidrag? – Rättslig vägledning*, http://www4.skatteverket.se/rattsligvagledning/edition/2017.3/331639.html?q=koncernbidrag (visited 2017-05-03).
[48] SITA 35:6.
[49] SITA 35:5.
[50] SITA 35:3.
[51] See case C-123/11, *A OY*
[52] Case C-446/03, *Marks & Spencer*, paragraph 59.

led to several rulings in the SAC[53] and the implementation of the rules regarding intra-group deductions.[54]

2.3 Intra-group deductions and the right to deduct final losses

The rules regarding intra-group deductions are found in chapter 35 a of the SITA and grants a Swedish parent company the right to deduct a final loss in a foreign subsidiary if the parent owns more than 90% of the subsidiary and the subsidiary is located in the EU/EEA. In regards to the ownership these rules, thus, equals the rules regarding intra-group contributions.[55]

However, according to the Swedish rules, a loss is not final unless the subsidiary have been liquidated and the liquidation procedure have been finished.[56] It is noticeable that a merger means dissolving a company without going into liquidation making these rules inapplicable. Nonetheless, the STA has published an official statement, stating that in practise the rules regarding final losses shall apply by analogy to mergers the same way as they apply to companies going into liquidation.[57] Thus, the rules on final losses are practically available in mergers, despite the lack of representation in the legislation.

A loss is final when a loss cannot be utilised in the subsidiary or ”another” in the state of the subsidiary and the reason that it cannot be utilised is not based on their being a *de jure*-limitation in the usage of such loss nor that this loss usage is limited in time.[58]

The rules are also further restricted by limiting the deduction to the lowest amount that would be concluded based on the calculation in both the involved states and up to a maximum of the profits made by the parent company.[59]

Based on this, it can be noticed that the Swedish merger rules, apart from putting limits on the loss utilisation of foreign subsidiaries, also put foreign subsidiaries in a situation where they can never be treated better than Swedish subsidiaries, but can be treated worse.

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[53] See among others, Rå. 2009 ref. 13
[54] See Prop. 2009/10:194, p. 2
[55] See part 2.3.
[56] SITA 35 a: 5 (1).
[57] The STA official statement, *Avdragsrätt för slutlig förlust hos överlåtande företag vid gränsöverskridande fusion*, Dnr: 131 422133-13/111.
[58] SITA 35 a: 6.
[59] SITA 35 a: 7.

2.4 Summary of the Swedish law as it stands

In Sweden mergers were introduced at the adoption of the MD and the term was divided into two classifications. A qualified merger is a merger where the criteria set out in the MD and the transposed Swedish legislation are fulfilled. In those situations, tax continuity is applied. However, the criteria practically eliminate foreign subsidiaries from the rules. This is because the transposed Swedish rules are limited to subsidiaries who are, at least in part, taxable in Sweden. Mergers which do not meet the criteria of being qualified become unqualified mergers.

Unqualified mergers are mergers where the general business taxation scheme applies rules regarding intra-group contribution apply. In connection to this set of rules the rules regarding intra-group deductions apply. These rules were invented to comply with EU law as the rules regarding intra-group contributions do not apply to companies established outside of Sweden.

The rules regarding intra-group deductions allows for the deduction of final losses. Even though the Swedish legislation does not apply to mergers *per se*, the Swedish authorities applies these rules to merger per analogy.

However, for a loss to be final it must fulfil certain criteria and the deduction cannot exceed the profits in the parent company.

Thus, to be able to determine whether the Swedish rules can be deemed compatible with the TFEU, it must be analysed where EU law sets its' limits in regards to cross border mergers, domestic tax consolidation systems as well as for final losses.

3 Treaty Access and Justifications

3.1 Access to the Applicable Freedoms and whether a discrimination or restriction exists

3.1.1 TFEU or the Merger Directive

Before a complete analysis of the compatibility of the Swedish merger rules with EU law can take place, it must be ascertained whether the rules should be analysed in the light of the fundamental freedoms or in the light of the Merger Directive from which the rules have been adopted.

In the judgement *Euro Park Service*[60] the CJEU stated how to draw a distinction between these two legal acts. The case regarded the anti-shopping clause in the MD, which had been transposed by France into their domestic tax law. The first question of the case regarded whether a provision, adopted based on a directive, should be analysed in the light of the directive or primary law i.e. the TFEU and the fundamental freedoms therein. The court stated that ”*any national measure in an area which has been the subject of exhaustive harmonisation at the level of the European Union must be assessed in the light of the provisions of that harmonising measure, and not in the light of the provisions of primary law*”.[61]

However, the court went on to state that said provision in the directive was part of no such exhaustive harmonisation. Furthermore, when no further guidance on the implementation of a directive provision exists, the state should, taking into account the principle of proportionality, determine how to adopt the provision for the purposes of applying the article in the directive. The court also stated, that when such legislation is not part of an exhaustively harmonized area the provision comes into the scope of the fundamental freedoms of the TFEU.[62]

AG Kokott clarifies the meaning of exhaustively harmonized in her opinion on *Holcim.*[63] She states, in essence, that when a measure neither obliges Member States to introduce the specific measure, nor defines any exhaustive

[60] Judgment of 8 March 2017, *Euro Park Service,* C-14/16, EU:C:2017:177.
[61] *Ibid.*, paragraph 19.
[62] *Ibid*., paragraphs 24-26.
[63] Opinion of Advocate General Kokott delivered on 19 January 2017, *Eqiom and Enka – “Holcim”*, C-6/16, EU:C:2017:34.

objective to interpret against, then a rule is not part of such an exhaustive harmonized area.[64]

As the Swedish rules regarding qualified mergers are based on the MD, it would, therefore, seem correct to compare them to the provision of that directive. The criterion under scrutiny is "taxable according to the SITA" found in 37:11 of the SITA, and the only equivalent article in the directive is article 3, which states that "a company, according to the directive, is a company which is resident for tax purposes within a Member State according to the laws of that Member State".[65] It is evident that the Swedish criterion is not compatible with that provision of the directive and it could also be argued that said article could constitute an exhaustively harmonized provision. However, it was also stated in *Euro Park Service* that Member States, when adopting directives into national legislation, must rely on the principle of proportionality in doing so. As we have also seen from the decision in the BATR, the board held that this criterion was proportional taking into account the legislation on intra-group contributions and intra-group deductions.

In connection to this, the author agrees with the BATR in the conclusion that, because of the fact that Sweden essentially have two co-acting merger legislations, the rules regarding intra-group contributions and intra-group deduction must also be taken into account to properly determine the compatibility of the criterion found in 37:11 of the SITA. However, as these rules are found in other parts of the Swedish legislation, and, according to the author not part of the exhaustive harmonized area of the MD, these rules cannot be exclusively scrutinized towards the MD. Thus, the entire merger legislation must also be scrutinized in the light of the fundamental freedoms.

3.1.2 Applicable freedoms and the right to access them

In order to make an assessment of the Swedish rules compatibility of EU law, it must be ascertained whether the legislation falls within the free movement articles of the TFEU. There are in particular two freedoms which have impact on companies doing business in the EU. The freedom of establishment found in art. 49 of the TFEU and the free movement of capital found in art. 63 of the TFEU.

The freedom of establishment mainly protects the equal treatment of foreign nationals in the host state. However, the freedom also prohibits the Member State of origin hindering establishments in another Member State, thus the protection of the freedom applies both to situations where a taxpayer is

[64] Opinion of AG Kokott, C-6/16, *Holcim*, paragraph 35
[65] See *Merger Directive*, Council Directive (EU) 2009/133/EC, article 3 (b).

hindered in establishing abroad by the state of residence as well as when the taxpayer is hindered by rules in the state of the foreign establishment.[66]

The free movement of capital, art. 63 TFEU, states that any restriction of the movement of capital, and any restrictions to payments, between Member States, as well as between Member States and third countries, are prohibited.

Essentially the treaty freedoms stipulate the equal treatment of businesses with residency in other states compared to domestically resident businesses and the equal treatment of capital movements, in comparison to an equivalent domestic capital movement.

Which freedom that is applicable is in general determined based on what freedom that fits the purpose of the legislation the most.[67] Determining which freedom that applies is of great importance as a very important distinction exists between the freedoms. The freedom of establishment applies only to situations between two citizens of the EU, while the free movement of capital includes situations where one party is a citizen of the EU and the other is resident in a state outside the EU.[68]

The distinction between the freedoms is also important when it comes to the potential justifications of a discriminatory of restrictive legislation. When the free movement of capital applies, Member States may apply harsher criteria towards residents in third countries, for instance based on securing the payment of taxes, than would be possible if the situation would have been under scrutiny of the freedom of establishment.[69]

When both freedoms can apply to a situation, the CJEU makes a distinction between which freedom to apply by looking at whether the legislation demands a certain level of influence over the other party. When the legislation aims at situation where one company exercises a decisive influence over the other, the freedom of establishment applies alone. [70]

As we have seen above, a merger is a particular way of terminating the existence of a legal person and when the legal personality is lost, the benefits of the treaty is generally lost as well. However, the CJEU has made it clear that a merger, no matter the motive, is a necessary method of restructuring for companies in the EU and essential for the functioning of

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[66] See for instance, Judgement of 21 December 2016, *Masco Damixa*, C-593/14, EU:C:2016:984, paragraph 24.
[67] See for instance, Judgement of 21 January 2011, *Test Claimants in the FII Group Litigation 2*, C-35/11, EU:C:2012:707 (”*FII GLO 2”),* paragraph 90.
[68] See for instance, Judgement of 24 November 2016, *SECIL*, C-464/14, EU:C:2016:896 paragraph 42.
[69] *Ibid.* paragraphs 63-64.
[70] Judgement of 12 December 2006, *Test Claimants in the FII Group Litigation,* C-446/04, EU:C:2006:774 (”*FII GLO”)*, paragraph 37.

the internal market.[71] Thus, even though a merger dissolves a legal personality the merger falls under the protection of the treaty and the fundamental freedoms.

Furthermore, in the same case the CJEU provides for one more important distinction regarding mergers. The court states that a merger is essentially the opposite to establishing a subsidiary abroad, and as such it is part of a taxpayers right to establish itself freely within the EU.[72]

3.1.3 Discrimination or restriction

The next step that must be ascertain is to determine whether the Swedish rules cause a discrimination or a restriction. For a restriction or discrimination to exist a difference in the treatment of comparable situations must exist. As stated earlier, this entails either that the same rules are applied to taxpayers in different situations or that different rules are applied to the taxpayers in the same situation.[73] Furthermore, a discrimination can either be direct or indirect. A direct discrimination distinguishes a situation based on the nationality of the parties involved. Indirect discrimination occurs when a legislation does not at the outskirts treat different nationals differently, but where the rules in practise only applies to cross border situations. Thus, creating a difference in treatment anyways.[74]

In general, the CJEU seems to make no difference between a discriminatory legislation or a restrictive legislation even though it is a question being debated by scholars.[75] Furthermore, the CJEU only looks at one tax subject at the time to determine whether a discrimination or restriction exists.[76] However, a restriction to the freedom of establishment has sometimes been found even in cases where there is no obvious discrimination. In *Krankenheim* and *Deustche Shell* there seem to be a combination of the treatment of both states which causes the taxpayer to end up in a worse situation than a comparable domestic situation. [77] Even when the treatment of the Member State of resident is legitimate in itself.[78] Johansson discusses thoroughly whether *Krankenheim* creates an obligation for the taxpayers and the Member States to analyse the legislation of both Member States

[71] See for instance, case C-123/11 *A OY*, paragraph 24.
[72] *Ibid.*, paragraph 25.
[73] See the reference to C-279/93, *Schumacker*, in part 1.1.
[74] See for instance, C-279/93, *Schumacker*, paragraph 26.
[75] Johansson, J, 2016, *EU-domstolens restriktionsprövning - i mål om de grundläggande friheterna och direkta skatter*, p. 47.
[76] *Ibid.*, p. 65.
[77] See Judgement of 28 February 2008, *Deutsche Shell*, C-293/06, EU:C:2008:129 and Judgement of 23 October 2008, *Krankenheim Ruhesitz,* EU:C:2008:588.
[78] Wattel, P, *Non-Discrimination á la Cour: The ECJ's (Lack of) Comparability Analysis in Direct Tax Cases, European Taxation,* 2015, p. 548.

concerned and to take both into account when determining whether a restriction exists or not. However, he concludes that there is no possibility to draw any such conclusion based on the case as the arguments of the CJEU are lacklustre and vague.[79]

In *Masco Damixa*, which was decided after the publishing of Johansson's thesis, the CJEU appears to correct their confusing restriction analysis found in *Krankenheim* in favour of Johansson's conclusion. The case regarded a Danish parent company with a subsidiary in Germany. The subsidiary in Germany paid interest on a loan from the Danish parent company, an interest payment that was being treated worse for tax purposes than interest payments from subsidiaries resident for tax purposes in Denmark. Having *Krankenheim* in mind, the treatment in Germany could, hypothetically, affect whether the Danish rules caused a restriction on the freedom of establishment or not. However, the court argued that even if the freedom of establishment does not oblige Member States to draw up rules that removes any disparities between domestic treatments, a different treatment of a foreign subsidiary compared to a domestic subsidiary in a comparable situation constitutes a restriction no matter the treatment in the other state.[80] Thus, the treatment in Germany was of no importance in the restriction/discrimination analysis of the court. Based on this, it is the view of the author that the potential misconception found in the previous case law is corrected by the court, even though they do not make any explicit comment about it.

Another aspect of the restriction analysis that has been brought into light by the CJEU is restriction based on *de facto* discrimination. In *FII GLO* and *FII GLO 2* the CJEU dealt with the British rules regarding cross border dividends. In the UK, dividend payments between domestic companies are subject to a participation exemption, meaning that they are not deductible for the payer nor taxable for the payee. At the same time the UK had implemented the PSD[81] in such way that taxes on foreign dividends were subject to a credit against the corporate tax in the UK, instead of being subject to the exemption that was being applied to domestic dividends. At the outskirts of the legislation *de jure*, there seemed to be no difference in treatment.

However, the applicants in the proceeding stated that foreign dividends were *de facto* treated worse than national dividends. One reason for this was that even if the domestic company receiving the dividend had no obligation to

[79] Johansson, J, 2016, *EU-domstolens restriktionsprövning - i mål om de grundläggande friheterna och direkta skatter,* p. 170-171.
[80] See C-593/14, *Masco Damixa*, paragraphs 40-43.
[81] See Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States.

pay corporate income tax, the dividend would still be subject to the participation exemption and, thus, ”tax free”.[82] In the equivalent situation with a foreign subsidiary the tax free company would have no corporate tax to offset the foreign tax against. Thus, leading to a *de facto* worse treatment for foreign dividends.

The CJEU stated that when the receivers of domestic and foreign dividends are in comparable situations an effective i.e. *de facto* difference in treatment constitutes a restriction incompatible with EU law.[83] The only time such treatment did not amount to a restriction was if the situations at hand were ancillary. Thus, when determining whether a restriction or discrimination exists both the legislation itself as well as the application of the legislation must be analysed.

3.1.4 Whether the Swedish rules create a restriction on the fundamental freedoms

A taxpayer exercising its right to carry out a cross border merger is despite the loss of legal personality of one of the involved parties, protected by the free movement articles. From the Swedish perspective, there is also but one exercise of the treaty freedoms, that being the establishment abroad. As seen in *A OY* described in part 3.1.2, merging a subsidiary is considered part of the same treaty exercise as establishing abroad. Thus, when a Swedish parent company establishes a foreign subsidiary, which is then subsequently merged, the parent company is the one exercising their treaty rights. According to the author this entails that the restriction analysis must also be based on the view of parent.

When a Swedish parent company establishes a subsidiary the merger rules, the rules regarding intra-group contributions and intra-group deduction apply together. These rules require the parent company to own more than 90% of the shares in the subsidiary to be applicable. Such threshold must be deemed to pass the decisive or definite influence test set out by the CJEU in determining which freedom that should apply. A merger is also part of the same treaty exercise as establishing abroad and by also adding the treatment of the taxpayer in *A OY*, where equivalent rules for tax consolidation were under scrutiny for restricting the freedom of establishment, it can be concluded that the rules fall within said freedom.

In connection to this, it is true that in *A OY* the CJEU stated that rules separating taxpayer based on their residency can sometimes justify a difference in treatment. However, the court also stated, that if all rules could

[82] See C-35/11, *FII GLO 2*, paragraph 41.
[83] *Ibid.*, paragraphs 50-54.

be justified based on residency, it would deprive the freedom of establishment of its value.[84] Furthermore, the court also stated, that allowing a parent company to merge with a domestic subsidiary with tax continuity, but not allowing for the same treatment of foreign subsidiaries constituted a restriction as a parent company merging with a foreign subsidiary was in an objectively comparable situation to a parent company merging with a foreign subsidiary. Such difference in treatment did, therefore, infringe the freedom.[85]

Thus, in the analysis of whether the rules create a discrimination or restriction, the author believes the Swedish rules create an indirect restriction on the freedom of establishment in the following ways:

First, a Swedish parent company is excluded from the possibility of merging a foreign subsidiary into the Swedish business with tax continuity unless the subsidiary also carries on a PE in Sweden prior to the merger. No such limits exist for Swedish subsidiaries.

Secondly, when a merger is unqualified the rules regarding intra-group contributions and intra-group deductions apply. The intra-group contribution rules require both parties to be taxable in Sweden and Swedish subsidiaries are not at all targeted by the rules regarding intra-group deductions.

The rules regarding intra-group deductions also stipulate that when calculating the deductible amount only the lowest value accounted for by the Swedish and the foreign legislation should be chosen. The deduction can also not exceed the profits of the parent company. These limitations amount to a *de facto* difference in treatment as domestic subsidiaries have no limits in their deduction.

All of those restrictions makes it less attractive to establish a subsidiary in another Member State in comparison to establishing it in Sweden.

Consequently, it can be concluded that the Swedish merger rules, the intra-group contribution rules as well as the rules regarding final losses, separately as well as together, creates restrictions to the freedom of establishment.

Thus for the Swedish rules to be compatible with EU law, the rules must pursue a legitimate objective and they must be justified by an overriding reason in the public interest.[86]

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[84] See C-123/11, *A OY*, paragraph 34.
[85] *Ibid.*, paragraph 35.
[86] See for instance case C-446/03, *Marks & Spencer*, paragraph 35.

3.2 Justifications

3.2.1 Justifications in general

A restriction or discrimination found in domestic legislations can be deemed compatible with EU law if the restriction or discrimination can be justified. As seen above, there is a distinction between the justification of direct and indirect discriminations. Direct discrimination based on nationality can only be justified based on public policies, public health or public security[87], while indirect discrimination or restrictions can be justified by overriding reasons in the public interest.[88] The CJEU also allows for the application of several justifications at the same time.[89]

3.2.2 Cohesion of the tax system

The first justification found in the case law of the CJEU is "the cohesion of the tax system". The justification, which was stipulated in the *Bachmann*-ruling[90], tries to ensure that there is a symmetric tax treatment within one jurisdiction. Furthermore, for a legislation to be justified based on the cohesion of the tax system, said justification requires a direct link between a tax advantage and the offsetting of that advantage through a tax levy.[91] However, a legislation which leads to the existence of such a direct link only in regards to cross border situations cannot, nevertheless, be justified.[92]

3.2.3 Balanced allocation of taxing rights

The second justification method called the "balanced allocation of taxing rights" was introduced by the CJEU in the previously mentioned *Marks & Spencer*-ruling. In the case the CJEU stated that profits and losses must be treated symmetrically in the same tax system. This is in order to protect a balanced allocation of the power to impose taxes between different Member States.[93] Furthermore, the CJEU acknowledge that the preservation of that allocation might make it necessary to apply the tax rules of only one state in

[87] See for instance TFEU art. 45(3).
[88] See for instance case C-123/11, *A OY,* paragraph 33.
[89] See for instance, Judgement of 18 July 2007, *OY AA,* C-231/05, EU:C:2007:439.
[90] Judgement of 28 January 1992, *Bachmann,* C-204/90, EU:C:1992:35.
[91] See Judgement of 21 December 2016, *Commission vs Portugal*, C-503/14, EU:C:2016:979, paragraph 62.
[92] *Ibid*., paragraph 64
[93] See C-446/03, *Marks & Spencer*, paragraph 43.

respect of both profits and losses.[94] The court, in addition to this, also stated that a company should not have the right to choose in what state they want to be taxed as this could jeopardise the allocation of taxes.[95] Thus, the court essentially stated that the justification requires there to be a symmetric approach to profits and losses between Member States, as well as within a Member State.

3.2.4 Preventing the double use of losses

The second justification that the CJEU stipulated in *Marks & Spencer* was the justification of ”preventing the double use of losses”. The CJEU simply stated that rules which aim to prevent that situation must be accepted, and that extending the British rules to cover foreign losses could lead to such unwanted situations.[96]

It seems to the author that the justification for double use of losses and balanced allocation of taxing rights are more or less equivalent in their effect. As seen above, having a symmetric approach to profits and losses essentially covers that losses should not be used in more than one State.

3.2.5 Preventing tax avoidance

The last justification that was stipulated in the judgement was the justification to secure that the risk of tax avoidance was eliminated. Just like in the justification of preventing the double use of losses, the court held that by limiting the right to use losses to companies in the UK, that risk was effectively eliminated.[97]

However, the justification of preventing tax avoidance has been dealt with more extensively in the case *Cadbury Schweppes*.[98] In *Cadbury Schweppes*, the CJEU started by stating that even though taxpayers may not rely on EU law for fraudulent ends, that the freedom of establishment protects the right of the taxpayer to establish themselves abroad.[99]

However, the court also stated that domestic legislations with the purpose to prevent “wholly artificial arrangement, put in place only to circumvent the

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[94] *Ibid.*, paragraph 45.
[95] *Ibid.*, paragraph 46.
[96] See C-446/03, *Marks & Spencer*, paragraph 47.
[97] *Ibid.*, paragraph 49.
[98] Judgement of 12 September 2006, *Cadbury Schweppes plc and Cadbury Schweppes Overseas*, C-196/04, EU:C:2006:544.
[99] C-196/04, *Cadbury Schweppes*, paragraphs 35-38.

application of the domestic legislation", can yet be justified by the need to prevent tax avoidance.[100]

3.2.6 Justifying the Swedish rules

Looking at the Swedish rules as a whole, the Swedish rules regarding mergers, intra-group contributions and intra-group deductions are partly based on the idea of a symmetric taxation in Sweden. However, the criteria of the so called "direct link" might be harder to establish. That is in despite of the fact that the intra-group contribution rules stipulate that a contribution is only deductible for tax purposes for the payer if the contribution is taxable for the payee in Sweden. According to the author the criteria does not create a direct link since the transaction only amount to a cash flow advantage. As such, the author believes the rules would be hard to justify based on the cohesion of the Swedish tax system.

Nevertheless, the rules do make sure that there is a symmetric treatment of profits and losses in-between Member States. The limits of those rules also make sure that companies cannot choose in what Member State they want to be taxed, since the rules only apply in Sweden and thus contribute to a balanced allocation of taxing rights. They also put limits on the use of losses. Only losses in Sweden can be utilised freely and by not allowing for deduction of a loss which is not considered final the rules prevent the double use of losses.

Furthermore, the CJEU has previously dealt with similar rules in both the judgement *Oy AA*, which regarded the Finnish intra-group contribution rules (they seem to be very much like the Swedish ones) and the previously mentioned *A OY*, which regarded the Finnish merger rules (which also seem to work like the Swedish ones).

In the both cases the CJEU held that the rules created restrictions on the freedom of establishment, as the legislations treated foreign subsidiaries worse than domestic subsidiaries. However, in *Oy AA* the restriction could be justified based on the balanced allocation of taxing rights, as taxpayers should not have the right to freely choose in which Member State they want to be taxed and such rules could also lead to tax avoidance. Even though rules with the purpose to counter abusive behaviours should normally only prevent wholly artificial arrangements, a legislation as the Finnish one needs to be examined as a whole and several justifications taken together can justify such legislation towards combating tax avoidance. In *A OY* the rules could also be justified by a combination of several justifications. In that case

[100] *Ibid.*, paragraph 55.

by securing a balanced allocation of taxing rights, preventing the double use of losses and preventing tax avoidance.

As the Finnish and the Swedish tax consolidation rules serve similar purposes, being the utilisation of profits and losses within company groups, and because the Swedish and Finnish mergers rules seem to work in the same way, it must be concluded that it is most likely that the Swedish merger rules, intra-group contribution rules and intra-group deduction rules could be justified by a combination of balanced allocation of taxing rights, preventing double use of losses as well as preventing tax avoidance. The addition of tax avoidance is done by looking at the entire system as a whole.

Nevertheless, it must be ascertained whether the rules go beyond what is necessary.

4 Proportionality

4.1 The proportionality assessment in EU direct tax law

In the direct tax cases of the CJEU the last step in the evaluation of legislations is the proportionality assessment. The assessment stems from the principle of proportionality, one of the general principles of EU law stipulated in the founding treaties.[101] The principle must be respected in measures taken by both the institutions of the Union and by the Member States. Examples of when the principle must be respected include the evaluation of domestic legislations, in the adoption of directives or in the interpretation of EU legislations.[102]

In direct tax cases where the CJEU has found a difference in treatment that can be justified by an overriding reason in the public interest, the court goes on to examine whether the restriction is appropriate to ensure the purpose of the legislation and to make sure that the restriction in the legislation does not go beyond what is necessary.[103]

4.2 The proportionality requirements for merger rules

4.2.1 Symmetry, but the demand for final losses

In a previously mentioned case *Krankenheim*, which regarded the reinstatement of previously deducted foreign losses, the CJEU seem to establish the basis for any cross border proportionality assessment. The court held that the freedom of establishment does not demand Member States to draw up rules which in any situation removes disparities between tax legislations and justified that Germany reinstated losses from abroad when a exempt PE (from a tax perspective, essentially a subsidiary), started to make profits in the other state.[104] It was, according to the court, because the treatment was based on a symmetric treatment of profits and losses in

[101] See for instance, article 5 (4) of the TEU.
[102] See for instance, TEU article 5 and C-14/16, *Euro Park Service*, paragraph 24 and paragraph 69.
[103] See for instance C-35/11, *FII GLO 2*, paragraph 55.
[104] See case C-157/07, *Krankenheim,* paragraph 50.

Germany.[105] Lang states that the case is proof of the court trying to implement, as a breakthrough, symmetric taxation as a fundamental principle in EU law and the basis for the proportionality assessment of any measure in connection to the balanced allocation of taxing rights.[106] The author agrees with Lang, based on *Krankenheim* in conjunction with, for instance *Marks & Spencer* and newer cases such as *Damixa*, the CJEU tends to hold that symmetry and the symmetric treatment of profits and losses should primarily govern tax rules.

Nevertheless, in *Marks & Spencer* the court stated that a taxpayer should have the right to deduct a loss in a foreign subsidiary when the foreign subsidiary has exhausted all of its possibilities of ever taking that loss into account in the state of residence, either by the subsidiary or someone else in that state, also taking into account future or past periods.[107] Furthermore, in *A OY*, the CJEU stated stated that allowing for the deduction of losses from a foreign subsidiary in a merger does not in itself ("*a priori")* allow companies to freely choose where they want to be taxed and therefore does not jeopardise a balanced allocation of taxing rights,[108] and that such legislation goes beyond what is necessary when it does not allow for the deduction of foreign losses when the subsidiary abroad has exhausted all the possibilities of ever taking those losses into account in that state.[109] Thus, in *A OY* the court extended the *Marks & Spencer*-ruling to cover cross border mergers as well as tax consolidation systems, backing up the court's previous case law. In complete contradiction to what AG Kokott had suggested in her opinion.[110]

Based on these general observations it can be determined that in EU law profits and losses are, in principle, to be treated symmetrically. This means that if a state cannot tax the profits they should not, in principle, allow for the deduction of losses. However, EU law demands a way for the taxpayer to deduct final losses, both in regards to tax consolidation regimes as well as in cross border mergers. The Swedish rules regarding intra-group deductions serve to fulfil this demand. Despite that the rules *de jure* only applies to liquidations, the STA applies them *de facto* to cross border mergers as well. Thus, the application of the rules can be deemed to be carried out in an EU compatible way.

Nevertheless, it has been stated that the intra-group deduction rules are restricted in certain scenarios and it must thus be ascertained whether these criteria are also compatible with the *final loss*-doctrine.

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[105] *Ibid*., paragraph 42.
[106] See Lang, M., *Has the Case Law of the ECJ on Final Losses Reached the End of the Line?*, European Taxation, 2014, p. 538.
[107] See case C-446/03, *Marks & Spencer,* paragraph 55
[108] See case C-123/11, *A OY*, paragraph 48.
[109] *Ibid.*, paragraph 49.
[110] Opinion of Advocate General Kokott delivered on 19 July 2012, *A OY*, C-123/11.

4.2.2 **Final Losses**

The starting point in the *final loss*-doctrine can be found in paragraph 55 of the *Marks & Spencer*-ruling. There the CJEU states that losses are final when;

(1) *the non-resident subsidiary has exhausted the possibilities available in its State of residence of having the losses taken into account for the accounting period concerned by the claim for relief and also for previous accounting periods, if necessary by transferring those losses to a third party or by offsetting the losses against the profits made by the subsidiary in previous periods, and*

(2) *there is no possibility for the foreign subsidiary's losses to be taken into account in its State of residence for future periods either by the subsidiary itself or by a third party, in particular where the subsidiary has been sold to that third party.*

Following the *Marks & Spencer*-ruling, the CJEU has further explained their vague statement in several cases. Apart from *A OY* and *Krankenheim*, the most noticeable cases are *K*[111] and *Commission vs UK*[112]. However, final losses were also dealt with in *Lidl Belgium*[113] a case which extended the *final loss*-doctrine to cover exempt PEs as well.

In *A OY* the court had also to face two problems, apart from whether a merger constituted a treaty exercise and whether mergers were covered by the final loss doctrine, as seen above. In the case, which regarded a Finnish parent company with a Swedish subsidiary, the Finnish court asked the CJEU whether even the smallest income in the state of the subsidiary meant that the loss could not be seen as final. The court supposedly deals with this question in paragraphs 53 and 54 but does not provide for a clear answer. However, Danish. M. believes that the answer is affirmative and that it can be deduced from the context of the ruling. It seems as that she primarily bases her conclusion on the fact that the court leaves it up to the national courts to determine whether the subsidiary has truly exhausted all of the possibilities of taking their losses into account after pointing out that Sweden has an endless carry forward of losses.[114] Furthermore, the court also had to deal with the question of which rules that should govern the calculation of the loss. AG Kokott had in her opinion argued for the approach that the calculation should, in principle, be made applying the

[111] See case C-322/11, *K*.
[112] See case, C-172/13, *Commission vs UK*.
[113] Judgement of 15 May 2008, *Lidl Belgium*, C-414/06, EU:C:2008:278, paragraphs 46-49.
[114] Danish, M, *What remains of the Marks and Spencer Exception for Final Losses? – Examining the Impact of Commission v. United Kingdom (Case C-172/13),* European Taxation 2015, p. 419.

rules in the state of residence.[115] However, the court essentially answered that at the current state of EU law the freedom of establishment provides for no obligation of taking the laws of the foreign states into account when calculating the loss, neither does EU law require the resident state to only apply their own laws.[116] Nevertheless, the court also stated that EU law precludes methods of calculation which creates unequal treatment between domestic and foreign subsidiaries.[117] Thus, the court essentially leaves the question to the domestic laws to determine how to calculate such losses as long as the calculation is carried out in a non-discriminatory way.

The case *K,* also a Finnish case, regarded a Finnish national owning a real estate in France on which he had made a loss. According to the tax treaty between Finland and France, Finland had no right to tax any gain of the real estate and, thus, denied the taxpayer the right to deduct the loss allocated to France. Nevertheless, in Finland, a loss on a domestic real estate investment is deductible towards a taxpayer's overall income. Even though the difference in treatment could be justified, the taxpayer held that the loss should be considered final and, therefore, be deductible in accordance with the *Marks & Spencer*-criteria. However, in France on the other hand, losses on real estates are not deductible for tax purposes and the court held that when no possibility of utilising a loss exists in the state where the property is situated, the taxpayer can never end up in having exhausted all of the possibilities in that state.[118] The CJEU also stated that when no possibility of taking a loss into account ever exists, that fact cannot form part of a proportionality analysis.[119] These two statements seem, to the author, to be contradictory. Nevertheless, the author interprets the overall ruling as meaning that when a loss actually does not exist in the state where the loss has occurred, a loss in the state of residence cannot be deemed final.

In *Commission vs UK* the court had a chance to develop their reasoning from *K* and *A OY*. In the case the Commission held that the British legislation did not practically fulfil the *Marks & Spencer* criteria. In the case the court clarified that losses cannot become final simply because the laws of another Member State put limits on such losses, such as through limited carry forward.[120] Then the court also clearly expressed, that even a minimal income in the state where a loss making subsidiary is situated is enough to keep losses from becoming final.[121] Thus, the case proves that Danish were right in her conclusion regarding the minimal income in *A OY* and also, seemingly, confirming the author's interpretation of the *K* case.

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[115] See AG Kokott, *A OY*, C-123/11, para 73.
[116] See case C-123/11, *A OY*, paragraph 58.
[117] *Ibid*., paragraph 59.
[118] See case C-322/11, *K*, paragraphs 76 & 77.
[119] See case C-322/11, *K*, paragraph 81.
[120] See case C-172/13, *Commission vs* UK, paragraph 33.
[121] *Ibid*., paragraph 36.

Evidently, the *final loss*-doctrine of the CJEU demands a possibility for the taxpayer to deduct losses that are *de facto* final. Losses are *de facto* final if they are not limited by the legislation in the state of the subsidiary. Examples of this are, if there is no right to deduct a loss in the first place or if the carried forward of losses is limited. Furthermore, losses in a subsidiary cannot be final if the loss can be offset even against the smallest of income in that state.

However, when a *de facto* loss exists, the loss shall be calculated in a way which creates equal treatment between domestic and foreign subsidiaries.

4.3 The proportionality of the Swedish rules

4.3.1 Qualified mergers

As described in part 2, Sweden has decided to separate mergers into two groups, qualified and unqualified mergers, but that an analysis had to be undertaken looking at the rules as a whole.

Nevertheless, the MD was implemented by the Council as a way to harmonize cross border mergers within the EU, to reduce disparities between member states and to make cross border restructurings easier. The implemented Swedish rules do not contribute to this purpose.

Thus, despite the fact that the Swedish rules should be looked upon as a whole, there is nothing in the jurisprudence of the CJEU that seem to justify denying foreign subsidiaries the benefits of the MD, in relation to mergers where that directive should apply.

According to the author, that part of the legislation is, therefore, incompatible with EU law and the only way to make the legislation compatible with EU law is to include foreign subsidiaries by rephrasing the criterion. No less restrictive measure would suffice, and removing the "taxable according to the SITA"-criterion would not seriously jeopardise the balanced allocation of taxing rights.

This conclusion prevails, despite the fact that the CJEU tend to be strict in their defence of cross border mergers, as it is hard to see that the court would allow rules which contradicts the purpose of a unifying measure taken at the community level without that measure also contradicting the case law of the court.

Instead, it would be less restrictive to introduce limitations to the recognition of the tax continuity. For instance, by limiting foreign untaxed values to only be taken into account for ones, being at the time of the

merger. That would most likely be justifiable by not allowing for losses to be used twice.

4.3.2 Unqualified mergers

When looking at the unqualified mergers, the rules regarding intra-group deductions apply as a proportional measure to the intra-group contributions.

The first limitation of the Swedish final loss rules regards the limits of taking a final loss into account because of a *de jure*-limitation in the other state, such as limited carry forward. This builds upon the idea that the Member States in the EU are not obliged to ”heal another states treatment” as stipulated in the Swedish SAC. The CJEU clearly stated that in the *Commission vs UK* that this is the way the *Marks & Spencer*-ruling should be read. Thus, it is completely in line with EU law to limit the deduction of losses to losses that are *de facto*-losses.

The third limitation of the Swedish final loss rules is the demand for only taking the lowest value of the states involved into account. This also builds upon the idea that the Member States are not obliged to ”heal another states treatment”. In connection to this the Swedish legislation also limits the deduction of final losses up to the level of the profits in the parent company.

First of all, the author believes that the Swedish rules regarding the calculation and the limits to the profits of the parent company are incompatible with EU law.

The reason for this is that the author believes that EU law demands Sweden to apply their legislation the way AG Kokott argued in *A OY*, taking into account the loss as it would have been calculated in accordance with Swedish rules. The author agrees with AG Kokott, who essentially stated, that the only way to achieve equal treatment between domestic and foreign subsidiaries is applying the laws of the parent company to the losses in the foreign subsidiaries.[122] Having a legislation which *de facto* treats foreign subsidiaries in comparable situations worse, was also deemed incompatible with EU law in *FII GLO* and the same reasoning can be applied here. However, it is true, as Lang states, that had the CJEU completely agreed with the AG in *A OY*, the court would have cited the AG without rephrasing their answer.[123] Nevertheless, the court does not disregard the opinion of the AG either. By looking at the statement of the court, in the context of the cases *K* and *Commission vs UK*, the author believes it is possible to explain why the court responded in such way. According to the author, the reason

[122] See AG Kokott, *A OY*, C-123/11, para 73.
[123] See Lang, M, *Has the Case Law of the ECJ on Final Losses Reached the End of the Line?*, European Taxation, 2014, p.533.

for this was to not create a misconception that the rules of the parent state should always guiding, for instance when a loss is limited by the laws in the other state.

Furthermore, a connection to exit taxes and step-up values, which essentially is the opposite to the deduction of final losses, can be drawn. Applying different step-up values, or not applying any step-up at all, in different Member States lead to equal issues, essentially broadening the tax basis of Member States' and in turn double taxation.[124] Applying the Swedish calculation on loss deduction to step-ups i.e. applying the lowest value as step-up, calculated based on the exporting and importing state, would, effectively, lead to double taxation. That is because the importing Member State could increase their tax basis to include values not accrued on their territory. According to the author, that is the same situation as regards intra-group deductions in Sweden, because Sweden essentially taxes non-accrued values when the deductible amount is lower in the other Member State than according to Swedish rules and Sweden only takes into account for the former amount. Despite the fact that the CJEU has refrained itself from dealing with double taxation, the effects are contradictory to the purpose of the internal market.

According to the author, the conclusion also aligns more with the idea of analysing a restrictive situation from the perspective of one taxpayer rather than every party involved, something which was discussed in part 3.

Furthermore, this conclusion also entails that the loss cannot be limited to the profits in the parent company. The reason behind this is because the Swedish rules allow intra-group contributions even when it creates losses for the payer. Thus, limiting the deduction to the profits of the parent would once again lead to a *de facto* difference in treatment which goes beyond what is necessary.

Another argument in favour of the author's conclusions can be found in *Krankenheim,* and also in *Damixa,* where the CJEU essentially states that recognising the tax treatment, and thus, essentially, the tax laws, of another Member State is not demanded by EU law.[125]

Consequently, the Swedish rule requiring a loss to exist according to the legislation in the other Member State is proportional and compatible with EU law. Nevertheless, limiting the losses to the lowest value of the states involved and to a maximum of the profits in the parent company go beyond what is necessary and these limitations are incompatible with EU law.

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[124] See van den Hurk, H, van den Broek, H and Korving, J, *Final Settlement Taxes for Companies: Transfer of Seats, Interest Charges, Guarantees and Step-Ups in Value*, Bulleting for International Taxation, 2013, p. 264.

[125] Case C-157/07, *Krankenheim*, paragraph 50 or case C-593/14, *Damixa*, paragraphs 40-41.

5 Summary and Conclusions

5.1 Summary

Mergers are transactions which entail the dissolution of one company through the overtaking of assets and obligations by another. The tax rules regarding mergers include two different kind of mergers, qualified and unqualified mergers. Some of these rules apply to the same situations.

When a merger fulfils the criteria of being qualified, tax continuity applies. However, the Swedish rules regarding qualified mergers create a difference between foreign and domestic subsidiaries as the rules practically excludes foreign subsidiaries.

When a merger is not qualified, it is instead unqualified. In those cases, the Swedish rules regarding tax consolidation apply as an unqualified merger can be carried out without tax consequences anyways if the tax consolidation rules apply. Nevertheless, these rules are only applicable to companies established in Sweden, but allows for foreign losses to be deducted if they are considered final. To be considered final the loss cannot be limited by laws in the other country. Furthermore, when a loss is final the deduction is limited to the lowest value calculated based on other states involved and up to a maximum amount of the profits in the parent company.

Both set of rules are aimed at substantial ownership and therefore create restrictions on the freedom of establishment. Even though parts of the rules are based on a directive, they fall within the scope of the fundamental freedoms as the rules must be looked upon as a whole. The rules cause a restriction from the view of the parent company, because a company establishing a subsidiary abroad is treated worse than a company establishing a subsidiary in Sweden, and the merger of a foreign subsidiary is part of the same treaty exercise as establishing abroad.

Rules which treat taxpayers from different Member States worse can be justified if they serve a public interest and do not go beyond what is necessary to reach that goal. Looking at the merger rules as a whole, the rules can be justified as they contribute to a balanced allocation of taxation, making sure that losses cannot be used twice and to hinder tax avoidance.

Nevertheless, not allowing foreign subsidiaries to benefit from the tax continuity of qualified mergers goes beyond what is necessary, as less

restrictive measures could be enacted, such as limiting the utilisation of losses or re-valuations so they cannot be used more than ones.

Rules for mergers falling out of the Merger Directive must at least allow for the deduction of final losses but can be allowed certain restrictions. It is allowed to not deduct a loss because another state has put legal limits on that loss or because even the smallest chance of using a loss exists in the other state. The Swedish rules are thus proportional in that regard. Nonetheless, when a loss is deemed to be final, such loss cannot be calculated in a discriminatory way, meaning that it is not allowed to only deduct the lowest amount of the loss calculated based on the rules of the states involved or limiting the deduction up to the amount of profits in the parent company. In those regards, the Swedish rules go beyond what is necessary.

5.2 Conclusions on the compatibility of the Swedish rules

The Swedish rules have been found to be in part compatible and in part incompatible with EU law.

According to EU law:

- It is prohibited to deny foreign subsidiaries access to the benefits of the MD
    - Paragraph 11, chapter 37 of the SITA is, thus, incompatible with EU law
- It is prohibited to not allow for a deduction of final losses in cross border mergers and, therefore, rules cannot be limited to certain types of restructuring (such as liquidations)
    - Paragraph 5 (1), chapter 35 a of the SITA is, thus, incompatible with EU (However, it is not practically applied this way)
- It is proportional to have rules which denies a deduction of final losses which are limited through the foreign legislation
    - Paragraph 6 (2), chapter 35 a of the SITA is, thus, compatible with EU law
- It is prohibited to only deduct the lowest value calculated based on the Member States involved
    - Paragraph 7 (1), chapter 35 a of the SITA is, thus, incompatible with EU law
- It is also prohibited to only allow for a deduction of final losses up to the level of profits in the parent company

- Paragraph 7 (2), chapter 35 a of the SITA is, thus, incompatible with EU law

5.3 The pending case before the Swedish Supreme Administrative Court – the Conclusion

Going back to the pending case before the SAC, the author will provide for a comment on the case at hand.

First of all, the case regards a Swedish Parent company with German subsidiary who could not qualify for tax continuity based on not being taxable in Sweden. As it has been concluded that this requirement is incompatible with EU law, the subsidiary should be allowed tax continuity on that point. Nevertheless, when reading the decision of the BATR it can be deduced that the subsidiary will not be transformed into a PE after the merger. Thus, the merger would not fulfil the criteria required to benefit from the favourable tax treatment of the MD and the directive is inapplicable. Evidently, Sweden should now allow for tax continuity in this particular case anyways.

Based on the previous, the merger is an unqualified merger. The author agrees with the board that the full extent of the rules regarding intra-group contributions can be limited to mergers between Swedish companies and that they are not applicable. The author also agrees with the opinion of the STA stating that the rules regarding final losses found in chapter 35 of the SITA should be guiding.

The legislation in Germany does not allow for the transfer of losses in a national merger. This would, thus, allow Sweden to deny the deduction of any potential loss, as it can be argued that such loss cannot be considered to be final according to the settled case law from the CJEU. Nonetheless, it is also the view of the author that the jurisprudence of the CJEU does not provide for complete answer to the question on whether not allowing for a loss to be carried over through a merger falls within the "legal limitations scope". However, it seems as if the CJEU is moving towards a limitation of the final loss doctrine rather than the opposite. Based on this, the author believes that the majority of the BATR has reached the correct conclusion in regards to the deductibility of the losses.

However, the author would also like to provide for another aspect to the situation. If Germany does not allow for the transfer of losses in mergers, even if the losses are deemed to fulfil the requirement of being final, it would create a situation where the German legislation *could* be incompatible with EU law. If the German legislation would indeed be incompatible with

EU law and Germany should allow for such losses to be deducted, then the situation could, in turn, lead to the existence of a deductible loss from a Swedish perspective.

Despite that, the *Krankenheim* judgement indicates that even if a restriction exists, but that restriction is allocated to the other state, then the state of residence should not bear the consequences of that restriction. Thus, Sweden should, nonetheless, not be obliged to step in and ”heal” the unfavourable German treatment.

Evidently, the majority of the BATR has come to a correct conclusion. Despite that, the author would also suggest that the SAC uses the case to request a preliminary ruling from the CJEU. The case would be a good indicator for all Member States on determining how national loss utilisation regimes should co-exist with cross border restructurings in the EU.

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