

CMS Adonnino Ascoli & Cavasola Scamoni CMS Albiñana & Suárez de Lezo  
 CMS Bureau Francis Lefebvre CMS Cameron McKenna LLP CMS DeBacker CMS Derks Star Busmann  
 CMS Von Erlach Henrici CMS Hasche Sigle CMS Reich-Rohrwig Hainz



# CMS Tax Connect

## Contents

<b>Progress in Europe</b>	<b>3</b>
The Cartesio Case (ECJ, Grand Chamber, 16 December 2008, C-210/06): A New Approach to the Transfer of the Seat of a Company?	
1. Austria	5
2. Belgium	6
3. Bulgaria	6
4. France	6
5. Germany	7
6. Hungary	7
7. Italy	8
8. Netherlands	9
9. Poland	9
10. Spain	9
11. United Kingdom	10
<b>Austria</b>	<b>12</b>
Corporate tax	

<b>Belgium</b>	<b>14</b>
Corporate tax	
<b>Bulgaria</b>	<b>16</b>
Corporate tax	
<b>China</b>	<b>18</b>
Corporate tax	
<b>France</b>	<b>22</b>
Corporate tax	
<b>Germany</b>	<b>25</b>
Corporate tax	
Inheritance Tax	
<b>Hungary</b>	<b>27</b>
Corporate tax	
<b>Italy</b>	<b>30</b>
Corporate tax	
VAT	
<b>Maghreb</b>	<b>32</b>
Corporate tax and VAT	
Morocco	
Algeria	
<b>Netherlands</b>	<b>37</b>
Corporate tax	
<b>Poland</b>	<b>39</b>
Corporate tax	
<b>Russia</b>	<b>41</b>
Corporate tax	
VAT	
<b>Spain</b>	<b>44</b>
Corporate tax	
VAT	
Wealth tax	
<b>Switzerland</b>	<b>46</b>
Corporate tax and VAT	
Wealth Tax	
<b>United Kingdom</b>	<b>49</b>
Corporate tax	

## Progress in Europe

## The Cartesio Case (ECJ, Grand Chamber, 16 December 2008, C-210/06):

### A New Approach to the Transfer of the Seat of a Company?

**By Daniel Gutmann**

Of-counsel CMS Bureau Francis Lefebvre,  
daniel.gutmann@cms-bfl.com

The judgment delivered by the Grand Chamber of the ECJ in the *Cartesio* case is definitely an important step in the case law concerning the transfer of the seat of a company within the European Union. To what extent does this judgment affect tax rules governing such a transfer? This is a tricky question which may only be answered after first considering the judgment.

#### 1. The judgment

*Cartesio* was a limited partnership established in accordance with Hungarian law. After moving its seat to Italy, it filed an application with a Hungarian commercial court for registration of the transfer of its seat in the commercial register. The goal was to retain its status as a company governed by Hungarian law. This application was rejected on the ground that the Hungarian law in force did not allow a company incorporated in Hungary to transfer its seat abroad while continuing to be regulated by Hungarian law. Such a transfer would require, first, that the company cease to exist and, then, that the company re-incorporate itself in compliance with the law of the country where it wishes to establish its new seat. Is Hungarian law contrary to the freedom of establishment?

According to the ECJ, the answer is no. First, a company established in accordance with a domestic legal system enjoys legal existence only through the rules of that system. It is only logical that the law which provides for the conditions of legal birth of the company also provides for the conditions of its legal death. Second, the connecting factors to the territory of individual Member States vary widely from one country to another, which is not contrary to Community law.

‘ The Cartesio case: A New  
Approach to the Transfer of  
the Seat of a Company? ’

As the Court observes, Article 58 of the EEC Treaty (now Article 48 EC) "placed on the same footing, as connecting factors, the registered office, central administration and principal place of business of a company" (par. 106). Consequently, Member States also define in very different ways the conditions required to transfer the company seat abroad. As the Court put it, "a Member State has the power to define both the connecting factor required of a company if it is to be regarded as incorporated under the law of that Member State and, as such, capable of enjoying the right of establishment, and that required if the company is to be able subsequently to maintain that status. That power includes the possibility for that Member State not to permit a company governed by its law to retain that status if the company intends to reorganise itself in another Member State by moving its seat to the territory of the latter, thereby breaking the connecting factor required under the national law of the Member State of incorporation" (par. 110).

The Court however states that the legal power granted to the Member State of incorporation is not absolute. "It cannot, in particular, justify the Member State of incorporation, by requiring the winding-up or liquidation of the company, in preventing that company from converting itself into a company governed by the law of the other Member State, to the extent that it is permitted under that law to do so. Such a barrier to the actual conversion of such a company, without prior winding-up or liquidation, into a company governed by the law of the Member State to which it wishes to relocate constitutes a restriction on the freedom of establishment of the company concerned which, unless it serves overriding requirements in the public interest, is prohibited under Article 43 EC" (par. 112 and 113).

## 2. The impact of the judgment

The *Cartesio* judgment is obviously an important contribution to the case law governing the Member States' obligations on the transfer of a company's seat.

From the perspective of company law, the main interest of the judgment is the confirmation that the principles stated in the *Daily Mail and General Trust* case (ECJ, 27 September 2008, 81/87) are still applicable insofar as Member States maintain the power not to recognize the transfer of a company's seat without infringing the freedom of establishment. This confirmation is all the more notable as more recent cases had cast uncertainty on the actual scope of the *Daily Mail and General Trust* doctrine and led some practitioners to the conclusion that the ECJ had conferred a virtually

unlimited power upon companies to establish and move their seat wherever they liked (see in this respect *Centros*, 9 March 1999, C-212/97; *Überseering*, 5 November 2002, C-208/00; *Inspire Art*, 30 September 2003, C-167/01). Even the Advocate General in *Cartesio*, as well as the European Commission, had implored the Court to answer that Hungarian law was not compatible with Article 43 EC (see Opinion delivered by AG Poiares Maduro on 22 May 2008). It is therefore significant that the Court, far from reversing its *Daily Mail* doctrine, maintained most of it while acknowledging that there were limits to a Member State's power to prevent a company from keeping its legal personality after the transfer of its seat.

This somewhat conservative standpoint taken by the Court makes it difficult to analyze its actual impact on tax matters. On the one hand, the *Cartesio* case does not have anything to do with tax law. It may therefore not be considered as relevant as the *de Lasteyrie du Saillant* and *N* cases (ECJ, 11 March 2004, C-9/02; 7 September 2006, C-470/04) where the Court held that an exit tax on natural persons moving their residence to another Member State did not comply with Article 43 EC. This is the opinion of the European Commission which states that "the interpretation of the freedom of establishment given by the ECJ in *de Lasteyrie* in respect of exit tax rules on individuals also has direct implications for Member States' exit tax rules on companies". It adds that "it follows from *de Lasteyrie* that taxpayers who exercise their right to freedom of establishment by moving to another Member State may not be subject to an earlier or higher tax charge than taxpayers who remain in one and the same Member State" (Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee, Exit taxation and the need for co-ordination of Member States' tax policies, 19 December 2006, COM (2006) 825 final, pp. 5-6).

On the other hand, however, the reasoning in the *Cartesio* judgment might well be extended to the tax environment. Up to now, Member States have not harmonized the factors which connect companies to the tax jurisdiction of a country. Some States adopt a territoriality principle while others predominantly prefer a worldwide taxation system. Among countries which apply worldwide taxation, no harmonization exists as far as the definition of residence is concerned. Neither do Member States agree upon the conditions to be fulfilled for a transfer of seat to be neutral from a tax perspective. This legal situation is only slightly affected by the existence of certain provisions governing the transfer of seat in the Merger

directive, since they only deal with the transfer of the registered office of a European Company (SE) or a European Cooperative Society (SCE). The reasoning conducted in *Cartesio* could therefore drive the Court to the conclusion that Member States are free to determine the conditions under which a company falling within the scope of their tax jurisdiction loses its taxpayer status upon a transfer of its seat abroad.

If that were to be the actual impact of the *Cartesio* judgment, this would put an end to the debate on the question whether Member States may require the company transferring its seat to retain a permanent establishment in the country of origin in order to benefit from tax neutrality. While such a condition is extremely questionable under the *de Lasteyrie du Saillant* doctrine, it might be justified according to the *Cartesio* judgment.

However, it remains to be seen to what extent the *Cartesio* judgment might be interpreted in a more "EU-friendly" way. Let us point out again that, according to the judgment, a Member State cannot prevent a company from being governed by the law of another Member State (to the extent permitted by the other Member State) by requiring the winding up or liquidation of the company. From a tax perspective, the problem certainly does not really arise in this way: even where the Member State of departure levies an exit tax, this cannot prevent the company from being subject to the tax jurisdiction of the Member State of arrival for the future. Nevertheless, it could be argued that the *Cartesio* judgment makes it impossible for the Member State of departure to deter a company from transferring its seat to another Member State where that transfer is lawful under the law of both states.

Considering the ambiguity of the *Cartesio* judgment, how the Court will actually deal with the tax problems raised by the transfer of a company's seat is still an open question. Overall, there remains scope for arguing that the decision in *de Lasteyrie* can be extended so as to apply also to an exit charge applied to a company transferring its seat to another Member State.

## 1. Austria

### **Does national legislation permit a company to transfer its seat to another Member State and continue to be governed by its national law?**

A company incorporated under Austrian law is not allowed to transfer its seat abroad whilst continuing to retain its status as a company governed by Austrian law. Such a transfer would require (i) the liquidation and dissolution of the Austrian entity and (ii) the re-incorporation under the laws of the Member State where the new seat is based. The Austrian company would cease to exist and a new company would be established in the other Member State.

### **Does an exit tax arise on the transfer of its seat to another Member State?**

As a result of the liquidation and dissolution of the Austrian entity, the hidden reserves contained in the business assets are revealed and subject to 25% corporate income tax.

### **If there is an exit charge can it be avoided?**

Exit tax could only be avoided by a cross-border merger of the Austrian entity, as the transferring company, with an EU company, as the absorbing company. Such a cross-border merger may be tax neutral provided that Austria's taxation right in respect of the hidden reserves contained in the transferred assets is not restricted, where for example a permanent establishment continues to exist in Austria. However, the effect of a merger is not comparable to a transfer of seat as the Austrian entity would cease to exist.

#### **Johannes Reich-Rohrwig**

CMS Reich-Rohrwig Hainz  
johannes.reich-rohrwig@cms-rrh.com

#### **Sibylle Novak**

CMS Reich-Rohrwig Hainz  
sibylle.novak@cms-rrh.com

## 2. Belgium

### **Does national legislation permit a company to transfer its seat to another Member State and continue to be governed by its national law?**

In Belgium, the relocation of a legal entity from one Member State, which retains its legal personality, to another Member State may only be implemented in accordance with the laws of such States.

In the event of relocation, Belgian law may not continue to govern a company which is no longer established in Belgium and is henceforth established in another Member State. It is explicitly provided that in such circumstances the legal entity shall be governed by the law of the host Member State with effect from the relocation.

### **Does an exit tax arise on the transfer of its seat to another Member State? If there is an exit charge can it be avoided?**

The relocation of the registered office of a Belgian company in another Member State is treated as liquidation. As a result, all deferred taxes shall be immediately liable for payment.

It may be possible to get round immediate tax liability in the event where the items to which such deferred taxes relate continue to be invested in a Belgian establishment of the newly foreign company.

#### **Olivier Querinjean**

CMS DeBacker  
olivier.querinjean@cms-db.com

## 3. Bulgaria

### **Does national legislation permit a company to transfer its seat to another Member State and continue to be governed by its national law?**

Bulgarian companies cannot transfer their seat to another EU Member State without losing their capacity as legal entities under Bulgarian law. The Bulgarian company shall first be dissolved and liquidated in Bulgaria and subsequently reincorporated in the EU Member State of destination under the laws applicable therein.

### **Does an exit tax arise on the transfer of its seat to another Member State?**

Bulgarian tax legislation does not provide for any exit tax. As mentioned above, relocation of the company's seat outside of Bulgaria is only possible subject to dissolution and liquidation in Bulgaria. Companies in liquidation are subject to the standard 10% corporate tax. Upon liquidation, all assets are deemed to be disposed of at market prices and the temporary differences are recognized under standard accounting rules.

### **If there is an exit charge can it be avoided?**

In general, no tax is due upon the dissolution of a company which is merged with a company in another EU Member State. Such merger would be tax neutral as long as the assets remain within the Bulgarian tax jurisdiction. This would be the case of assets forming part of a permanent establishment or giving rise to the existence of a permanent establishment in Bulgaria.

#### **Gentscho Pavlov**

CMS Reich-Rohrwig Hainz  
gentscho.pavlov@cms-rrh.com

#### **Valentin Savov**

CMS Reich-Rohrwig Hainz  
valentin.savov@cms-rrh.com

## 4. France

### **Does national legislation permit a company to transfer its seat to another Member State and continue to be governed by its national law?**

No, a company governed by French law, which relocates abroad, is no longer governed by French law.

### **Does an exit tax arise on the transfer of its seat to another Member State? If there is an exit charge can it be avoided?**

Strictly speaking, no exit tax exists but the relocation of a company's registered office abroad theoretically triggers the right to collect all taxes owed in the event of liquidation (tax on the liquidation profit, including unrealized gains). Such liability can be avoided in the event where the company relocates to another Member State, provided that such company retains or creates a

permanent establishment in France subject to corporate income tax and the assets assigned to the French operations and, in the case of a holding company, the securities of group subsidiaries are recorded in the balance sheet.

The law also provides for another exception which is presently purely theoretical. By law, joint-stock companies are authorised to change nationality without being subject to immediate taxation where such change and relocation of the registered office abroad are decided by an Extraordinary General Meeting. However, in this case, it is necessary that the host country has concluded a treaty with France authorising the company to acquire the nationality of the country to which it is relocating its registered office whilst retaining its legal personality. It is currently impossible to fulfil this condition as no such treaty has yet been concluded by France.

**Emmanuelle Féna-Lagueny**

CMS Bureau Francis Lefebvre

emmanuelle.fena-lagueny@cms-bfl.com

## 5. Germany

**Does national legislation permit a company to transfer its seat to another Member State and continue to be governed by its national law?**

On the basis of the German Act to Modernise the Law on Private Limited Companies and Combat Abuse (MoMiG), since 1 November 2008 a German corporation with limited liability (GmbH) established under German law can separately transfer its administrative seat abroad (and not only to other EU Member States) whilst maintaining its registered seat in Germany, without even taking into account the *Cartesio* judgment.

However, the transfer of the administrative seat abroad is currently not possible for German partnerships. After the decision in the *Cartesio* judgment, it will not even be possible to argue against a mandatory winding-up or liquidation upon transfer of the administrative seat abroad based on infringement of the freedom of establishment. The case is only different if at the same time as the transfer of the administrative seat of a German partnership, it is registered with the Trade Register of the Member State to which the seat is transferred, since based on Article 48 EC, the principles of the *Cartesio* judgment are consequently relevant.

**Does an exit tax arise on the transfer of its seat to another Member State? If there is an exit charge, can it be avoided?**

As regards tax law, the German legislator continues to lag behind the requirements of EU law. The Merger Directive currently only contains provisions for tax-neutral cross-border transfers of the registered office of an SE and SCE. According to the *Cartesio* judgment, there is an urgent need to also extend these provisions to other national corporate forms which are covered by Article 48 EC. In this respect, the Commission must initially introduce the corresponding amendment of the Merger Directive as soon as possible, similarly as it did after the adoption of the SE Regulation (see Directive 2005/19/EC dated 17 February 2005).

Insofar as domestic tax law does not allow the transfer of the registered seat in a tax-neutral, identity-conserving manner, the existing companies should also refer to the basic freedoms to avoid taxation of hidden reserves based on the exit even before a corresponding amendment of the Merger Directive, even if individual assets after the exit can no longer be attributed to a permanent establishment in the exited State. The Commission has already launched proceedings against Sweden, Portugal and Spain for infringement of the corresponding treaty. It will not be authorised under any circumstances to impose – based on current civil case law – a liquidation tax on a company which transfers its registered seat to another EU Member State (see Bavarian Court of Appeal dated 7 May 1992 3Z-BR-14/92, DB 1992, 1400).

**Gerd Seeliger**

CMS Hasche Sigle

gerd.seeliger@cms-hs.com

## 6. Hungary

Although being one of the few Hungarian cases ending up at the European Court of Justice and having been eagerly awaited by the entire European legal community, most Hungarian legal practitioners fail to realise the actual significance of this case. The reason is that out of the four questions raised by the Hungarian court only the fourth is relevant from a corporate and tax law perspective. The first three concerned procedural issues on the functioning of Article 234 of the EC Treaty (on preliminary rulings) in relation to Hungary. We shall obviously only cover the fourth question with regard to the possibility of a Hungarian company transferring its seat to

another EU Member State whilst retaining its existence under Hungarian law.

As is apparent from the case, Hungarian law only recognises that a company is governed by Hungarian law if its seat is located in Hungary. This is popularly referred to as the “real seat theory”, although we doubt that much theoretical justification was ever provided in this respect. In any case, we now know for sure, that this cornerstone of Hungarian company law does *not* infringe the freedom of establishment as laid down by EU law.

At present, it seems that paragraphs 111-112 of the *Cartesio* judgment have caused the most head-scratching among Hungarian corporate lawyers. These deal with a theoretical situation (rather than the case at hand), where the seat of the company is transferred from the country of incorporation (e.g., Hungary) by converting itself to be governed by the laws of the host country (i.e., the country in which the new seat is located). The judgment states that in such cases the home country has no right to prevent a “conversion” (e.g., by requiring winding-up or liquidation of the company) and must allow the company to continue its existence under the laws of the host state. The problem is that unless it is an SE or SCE in its current state, Hungarian company law is not really prepared to tackle such a situation, i.e., to simply release a company from the scope of Hungarian law or to recognise its deletion from the relevant registers by conversion into a company governed by a different European jurisdiction. In practice, the winding-up of the company would most likely be required in such cases.

As regards *Cartesio*’s impact on Hungarian tax law, the picture is far from clear. In general, we should probably be cautious when drawing conclusions for the purposes of exit taxes from this judgment. The *Cartesio* case seems less significant for these purposes than the “*N*” case or the “*Lasteyrie*” case. At the same time, a few questions are raised. The Hungarian corporate income tax regime seems to be ahead of Hungarian company law in that it explicitly deals with the situation where a Hungarian company transfers its seat outside of Hungary or when it escapes the scope of Hungarian corporate income tax for any reason. Both actions are considered, for tax purposes, as dissolution without succession (not considering here SEs and SCEs). As we have seen, under Hungarian law, it is highly questionable whether a transfer of seat, without winding-up, would be possible. So, while there is no explicit exit tax in force in Hungary, the effects of a seat transfer would be very similar to dissolution by means of winding-up. This would

involve – *inter alia* – the taxation of “hidden reserves” (i.e., the positive difference between the market value and the book value of the company’s assets). Simply “escaping” the scope of Hungarian corporate income tax (e.g., by transferring the tax residence) would however not necessarily result in taxation of the “hidden reserves” as immediate taxation would only affect certain reserves for tax purposes, which would then need to be released.

These unwanted effects may not easily be avoided, although retaining a permanent establishment could be of relevance, if a company having its seat outside of Hungary but its place of effective management and thus – presumably, but subject to the relevant double tax treaty – being tax resident in Hungary, moves its place of effective management outside of Hungary. In such case, the company could not be said to escape from the scope of the Hungarian corporate income tax and the relevant rules on immediate tax liability might consequently not be fully applicable.

#### **Eszter Kalman**

Ormai és Társai CMS Cameron McKenna LLP  
eszter.kalman@cms-cmck.com

#### **Tamas Feher**

Ormai és Társai CMS Cameron McKenna LLP  
tamas.feher@cms-cmck.com

## **7. Italy**

### **Does national legislation permit a company to transfer its seat to another Member State and continue to be governed by its national law?**

A company set up in accordance with the rules of Italian civil law may transfer its seat to another Member State and continue to be governed by Italian law.

### **Does an exit tax arise on the transfer of its seat to another Member State?**

The transfer abroad of the (legal and administrative) seat of a company does not necessarily imply that the company is no longer fiscally resident in Italy. Indeed, a company continues to be fiscally resident in Italy if the entity’s main and substantial activities are carried out in Italy. This domestic rule is mirrored by the observation made by Italy with regard to the notion of “place of effective management”

contained in paragraph 25 of the Commentary on Article 4 of the OECD MC.

The transfer abroad of the fiscal residence of a company —no longer having either the legal and administrative seat in Italy or its main and substantial activities— gives rise to a taxable event since it is treated as a sale at market value of the business assets.

As a result, all accrued but not yet realized capital gains on these assets at the time of the transfer are subject to corporate income tax in Italy. Moreover, capital gains deriving from foreign permanent establishments are in any case considered realized at market value.

The same exit tax rules are applied to business assets transferred abroad from an Italian permanent establishment.

### **If there is an exit charge can it be avoided?**

The exit tax applied as a result of the transfer abroad of a company's fiscal residence is not applied if its business assets remain part of a permanent establishment in Italy.

Given this aim, tax-deferred reserves and provisions shown on the last balance sheet preceding the transfer should be reinstated in the balance sheet of that permanent establishment in Italy.

Losses realized by the company in the fiscal year preceding the year of the transfer of its fiscal residence abroad may normally reduce the taxable income of the Italian permanent establishment.

### **Carlo Romano**

CMS Adonnino Ascoli & Cavasola Scamoni  
carlo.romano@cms-aacs.com

## **8. Netherlands**

### **Does national legislation permit a company to transfer its seat to another Member State and continue to be governed by its national law?**

A company incorporated under Dutch law is not allowed to move its statutory seat to a different country. However, Dutch law allows a company to move its place of effective management abroad.

If a company which has been incorporated under Dutch law moves its place of effective management outside the Netherlands, it will

remain subject to Dutch law and taxation (subject to allocation rules under relevant tax treaties).

### **Does an exit tax arise on the transfer of its seat to another Member State? If there is an exit charge can it be avoided?**

If the place of effective management is moved abroad, an exit tax is applied to all hidden reserves. Such exit tax can be avoided by not moving the assets and/or liabilities that trigger such exit tax (i.e. the assets and/or liabilities with hidden reserves) and keeping such assets and/or liabilities as part of a permanent establishment in the Netherlands.

### **Jochem de Koning**

CMS Derks Star Busmann  
jochem.dekoning@cms-dsb.com

## **9. Poland**

### **Does national legislation permit a company to transfer its seat to another Member State and continue to be governed by its national law?**

From the perspective of Polish company law, a company incorporated in Poland cannot transfer its seat to another EU Member State and continue to be governed by Polish law. If a company governed by Polish law intends to move its seat abroad, it has to be dissolved or wound up.

### **Does an exit tax arise on the transfer of its seat to another Member State? If there is an exit charge can it be avoided?**

There is no exit tax under Polish tax legislation.

### **Arkadiusz Michaliszyn**

CMS Cameron McKenna LLP  
arkadiusz.michaliszyn@cms-cmck.com

## **10. Spain**

### **Does national legislation permit a company to transfer its seat to another Member State and continue to be governed by its national law?**

Generally speaking, this is not possible since in accordance with Article 26 of the Spanish

Corporate Income Tax Act, a company's tax period comes to an end when an entity resident in Spain becomes resident abroad.

Notwithstanding the foregoing, Article 8 of the Spanish Corporate Income Tax Act stipulates that entities satisfying any of the following requirements shall be deemed to be resident in Spain:

- "a) If they have been formed under Spanish law.
- b) If their registered office is in Spain.
- c) If their place of effective management is in Spain.

For these purposes, an entity shall be deemed to have its place of effective management in Spain if the management and control of its activities as a whole are located in Spain".

Taking into consideration the abovementioned Article 8 and considering this as an interpretation of the law (please note that this is not a clear issue), we could face the situation where a company moves its seat to another country but the effective place of management remains in Spain. In this case, our understanding is that the applicable law from a tax perspective would be Spanish law, as the company would be liable for taxation in Spain.

#### **Does an exit tax arise on the transfer of its seat to another Member State?**

When a company is relocated from Spain to another Member State, taxation should arise. Therefore an exit tax exists, as if liquidating the company.

#### **If there is an exit charge can it be avoided?**

Exit tax can be avoided on relocating the seat of these kinds of entities between EU Member States and the operation can be tax neutral if the company is converted into a European Company or European Cooperative Society, which has been possible since 1 January 2006. This relocation could be covered under the special reorganisation rules and no taxation should arise regarding the goods and rights located in Spain if they remain allocated to a permanent establishment in Spain.

#### **Beatriz García-Renedo**

CMS Albiñana & Suárez de Lezo,  
bgarcia@cms-asl.com

## **11. United Kingdom**

#### **Does national legislation permit a company to transfer its seat to another Member State and continue to be governed by its national law?**

Yes. Under British private international law, the connecting factor that determines the company law applicable to a company's formation, internal affairs and dissolution is the state of incorporation. Therefore, the transfer of a company's seat will not affect its governing law so that it will continue to be recognised as a company governed by UK company law.

#### **Does an exit tax arise on the transfer of its seat to another Member State?**

Section 185 Taxation of Chargeable Gains Act 1992 provides that when a company ceases to be resident in the UK it is deemed to have disposed of its assets (other than those that are to be used by it subsequently for the purposes of a trade carried on through a permanent establishment in the UK) at their market value and is required to pay the resulting tax on the unrealised gains. There is a requirement to notify HM Revenue & Customs of an intention to become non-resident and to agree arrangements for the payment of its tax liabilities.

#### **If there is an exit charge can it be avoided?**

As indicated above no exit charge arises in relation to any assets that are to be used for the purposes of a trade carried on through a permanent establishment in the UK. Where the company is a trading company or member of a trading group and has substantial holdings (10% or more of the ordinary share capital) in a trading company any gain arising from the deemed disposal will be exempt if the detailed conditions are met (including that the shares have been held for a continuous period of 12 months during the two years before the deemed disposal).

In addition, the tax charge can be deferred if the migrating company has a UK resident parent company that is to remain UK-resident. Under these provisions if the relevant assets are retained for at least six years after it ceases to be UK-resident, the tax will be payable only if it subsequently ceases to be a 75% subsidiary of its UK parent, or the parent ceases to be UK-resident. This treatment requires an election to be

made by the migrating company and the UK parent and, if the tax is subsequently triggered, it is payable by the UK parent.

**Mike Boutell**

CMS Cameron McKenna LLP  
mike.boutell@cms-cmck.com



## Austria

# Corporate tax

## Tax Reform 2009

The Austrian government recently presented a draft tax reform which shall become effective retroactively as from 1 January 2009 to boost economic recovery. The draft provides for tax relief for corporations, individuals and families with an estimated budget of €6 billion.

### 1. Investment incentives

In order to encourage investment in 2009 and 2010, 30% depreciation of the acquisition costs shall be allowed for some investments made in these years. The incentive is granted for investments in depreciable assets and investments in intangible assets, buildings, cars, aircrafts and used assets are excluded from the incentive. Corporations as well as individual entrepreneurs may benefit from the authorised depreciation which will reduce the taxable profit.

### 2. Reduction of income tax rates

Income tax rates for individuals shall be reduced retroactively with effect from 1 January 2009. However, the reduction will be moderate and lead to a maximum tax reduction of €1,350 per year for taxpayers with higher incomes.

### 3. Tax allowance on profits

For individual entrepreneurs, it will be of interest that a new tax allowance representing 13% of the annual profit (*Gewinnfreibetrag*) shall be granted as from 2010. An amount of €3,900 of the annual profit shall be tax-exempt in any case. A further amount of up to €96,100 of the annual profit shall be tax-exempt provided that an investment for such amount is made in depreciable fixed assets with a useful life of at least four years or certain securities.

The new tax allowance may be a considerable tax advantage for entrepreneurs. However, corporations shall not be granted the tax allowance.

‘ Tax Reform 2009 ’

#### **4. Tax relief for families**

The tax reform shall further provide for tax relief for families by various measures, e.g., childcare expenses shall become tax deductible and higher child allowances shall be granted.

**Johannes Reich-Rohrwig**

CMS Reich-Rohrwig Hainz  
johannes.reich-rohrwig@cms-rrh.com

**Sibylle Novak**

CMS Reich-Rohrwig Hainz  
sibylle.novak@cms-rrh.com



## Belgium

### Corporate tax

The European Parent-Subsidiary Directive of 23 July 1990 seeks to eliminate double taxation of dividends distributed between a subsidiary established in one Member State of the European Union and a parent company established in another Member State of the European Union.

In order to achieve this objective, the subsidiary's Member State must not levy any withholding tax at source on dividends distributed by the subsidiary and the parent company's Member State must not collect any taxation on the dividends received by the parent company.

Given this context, the parent company's Member State may opt for one of two methods:

- *the exemption method* whereby the beneficiary company is not taxed on the dividends;
- *the credit method* whereby the tax paid by the subsidiary on the dividends is credited to the tax owed by the parent company.

Belgium has opted for the exemption method... without achieving the result sought by the Parent-Subsidiary Directive!

Dividends received by a Belgian company are in principle exempt up to 95% as definitively taxed income provided that the following conditions are observed:

- The beneficiary company must have a holding representing at least (i) 10% of the distributing company's share capital or (ii) an investment of EUR 1.2 million;
- This holding must have been in place for at least one year (if this is not the case, a holding undertaking covering the same period must be made);
- The beneficiary company's holding must be recorded for accounting purposes as a long-term investment (as opposed to a short-term investment);
- The distributing company must be subject to standard tax rules (equivalent to Belgian corporate income tax).

However, this exemption shall only be effective if the beneficiary company's taxable base is adequate to cover the definitively taxed income (i.e., 95% of the dividends received). The calculation of a Belgian company's taxable base results from various successive stages. In this respect, first, the company's total income (including dividends) shall be calculated.

Exemption on dividends received by a Belgium company

Second, the exemption of these dividends shall be deducted from the definitively taxed income (i.e., 95% of the amount of the dividends) if the company has a net profit.

In the event where the net profit is not adequate, the deduction shall be limited to the amount of the profit and, if the company has not generated any profit, the deduction of definitively taxed income shall be fully and definitively lost. Economic double taxation would consequently result where and if the deductible dividends are higher than the taxable profit before the deduction of definitively taxed income.

Given these circumstances, the European Court of Justice recently ruled on the compliance of the Belgian rules with the provisions of the European Parent-Subsidiary Directive (cf. judgment of 12 February 2009, Cobelfret, C-138/07).

The Court logically ruled that the Belgian system of definitively taxed income does not comply with the Parent-Subsidiary Directive.

Therefore, Belgian parent companies need to check whether they are entitled to make a claim with regard to any surplus definitively taxed income, which has not be credited due to the lack of a positive taxable base. In theory, they may claim adjustments on taxation during the past five years.

**Olivier Querinjean**

CMS DeBacker

[olivier.querinjean@cms-db.com](mailto:olivier.querinjean@cms-db.com)



## Bulgaria

# Corporate tax

## 1. Incentives

The Ministry of Finance suspended the application of a tax holiday in the form of a five-year corporate tax exemption for income from investments in agriculture, processing, production, high-tech industry and infrastructure. The tax incentive will not become effective until it is approved by the European Commission in accordance with the regulations on state aid contained in the EC Treaty.

## 2. Tax developments

The Bulgarian tax system has recently undergone a series of reforms. Many of the reforms are a response to the infringement procedures relating to discriminatory taxation initiated by the European Commission against Bulgaria.

As from 1 January 2009, Bulgaria does not require a minimum participation and holding period in order to exempt dividends paid by Bulgarian subsidiaries from withholding tax to their EU parent companies. Currently dividends distributed by a Bulgarian subsidiary to its EU or EEA/EFTA parent company are not subject to withholding tax.

The most recent infringement procedures against Bulgaria concern:

- the discriminatory treatment of interest and discounts from EU or EEA/EFTA governmental, municipal and corporate bonds, where the income from Bulgarian governmental, municipal and corporate bonds is tax exempt; and

- the taxation on a gross basis of income derived by non-residents from interest, royalties, leases and other income from real estate, etc., where the same income derived by Bulgarian residents is taxed on a net basis.

Judging by the recent trends, the Bulgarian government will most likely extend the benefits of the tax exemption and accordingly provide for the net taxation of income from foreign bonds, respectively to non-residents.

As of the beginning of 2009, capital gains realized on regulated stock markets in the EU and EEA/EFTA States are tax exempt, as well as interest on bank deposits in EU and EEA/EFTA banks.

‘Bulgaria puts an end to many discriminatory tax measures’

### **3. Tax treaties**

As of 1 January 2009, the tax treaties with the USA, the United Arab Emirates, Jordan, Estonia and Azerbaijan became effective. Thus, the number of tax treaties Bulgaria is a party is approaching 70.

Bulgaria and Austria entered into a new tax treaty, which will replace the existing treaty concluded between the two countries in 1983. The existing treaty is one of the treaties which has been used the most for channelling investments to or from Bulgaria. The new treaty has not yet entered into force.

#### **Gentscho Pavlov**

CMS Reich-Rohrwig Hainz  
gentscho.pavlov@cms-rrh.com

#### **Valentin Savov**

CMS Reich-Rohrwig Hainz  
valentin.savov@cms-rrh.com



## China

# Corporate tax

## Tax measures introduced in January 2009

The Chinese tax authorities promulgated the interim measures relating to price adjustments by the tax authorities (the “Measures”) on 9 January 2009, which came into force with retrospective effect as from 1 January 2008 and replaced Circulars No. 59 of 1998 and No. 143 of 2004. The Measures now represent the most detailed and comprehensive fundamental regulations against tax evasion and transfer pricing manipulation in China.

The Measures govern transfer pricing in the scope of transactions between Chinese companies, foreign invested companies or offshore companies (in the event where one of the companies in the group is registered in China) and also all kinds of tax evasion laid down by the Enterprise Income Tax Law.

### 1. Declaration of affiliated relations

In accordance with a Circular of 18 December 2008, the Measures provide that “Chinese resident” enterprises and foreign enterprises with establishments located in China must submit nine forms (only two forms were previously required) on their transactions in conjunction with their annual tax return.

The definition of affiliated relations set forth by Article 9 of the Measures is wider than that previously laid down in the Circular No. 143. The Measures provide for eight cases of “affiliated relations”, including in particular control or holding [of shares] in a direct or indirect company equal or exceeding a 25% stake. For the purpose of assessing an indirect holding, the holding ratio between the parent company and the indirect subsidiary shall be treated as equal to the holding ratio between the intermediary company and the indirect subsidiary, provided that the parent company holds more than a 25% stake in the intermediary company.

### 2. Tax inspections

#### 2.1. Selection of enterprises to be inspected

The tax authorities are entitled to select at any time the enterprises to be inspected in relation to transfer pricing. The selection criteria are as follows:

China has just published detailed and comprehensive fundamental regulations against tax evasion and transfer pricing manipulation

- high volume or diversification of the types of transactions with an affiliated enterprise;
- continued losses, low losses or profits or fluctuations in the enterprise's profitability;
- profitability distinctly lower than the profitability of other enterprises in the same sector;
- incoherence between the profits and exposure undertaken;
- affiliated enterprises established in tax havens;
- failure to declare the existence of affiliated companies or missing documentation;
- violation of the arm's length principle.

In comparison to Circular No. 143, the new criteria implemented by the Measures are less precise and the text no longer limits the number of enterprises to be selected. The tax authorities consequently are vested with larger discretionary power in selecting enterprises.

## 2.2. Inspection by the tax authorities

Inspections conducted by the tax authorities are the more detailed investigation on transfer pricing issues. Such inspections must comply with a certain time limit to enable enterprises to provide the documentation. Moreover, the Measures allow the tax authorities to request disclosure of documentation not only to the target enterprises and affiliated enterprises, but also to comparable third party enterprises.

## 2.3. Transfer pricing adjustments

Transfer pricing adjustments resulting from a tax inspection may extend retroactively to a maximum period of ten years.

The tax authorities which decide to adjust the transfer price may apply the following methods to calculate the market price:

- comparable uncontrollable price method: reference to the price generally agreed by independent enterprises for identical or similar transactions;
- resale minus method: calculation of the cost of the margin generated on the sale of identical or similar products, services or intangibles;
- cost-plus method;
- transactional net margin method;

- profit-split method;

- profit estimation method. The tax authorities may also apply this method as provided for by the Enterprise Income Tax Law, although it is not mentioned in the Measures, especially where they consider that the documents are inadequate.

In comparison to Circular No. 143, the Measures are clearer relating to the scope of each method (sale, service, transfer of intangible assets, financing, etc.).

Moreover, the Measures now allow the tax authorities to use information which has not yet fallen into the public domain for the purpose of analysing the transfer price.

In addition, the Measures lay down the following principles which the tax authorities must take into account when carrying out the profit adjustment:

- enterprises whose activities solely involve manufacturing on behalf of one affiliated company and which do not undertake any exposure on the sale of products are profitable as a matter of principle;
- the tax authorities may call into question the offsetting of the parties' debts and obligations;
- the profitability ratio applied is higher than the average ratio for enterprises in comparable sectors.

The monitoring period by the tax authorities after an inspection has been extended to five years rather than three years.

## 3. Advance Pricing Agreements

The 2009 Measures replace the Regulations on the Application of Advance Pricing Agreements between Affiliated Enterprises of 2004.

An APA offers a means of securing the tax authorities' approval of a transfer pricing method, which reduces the risks of transfer pricing adjustments.

An APA is entered into for a period ranging from three to five years (rather than two to four years in the past). However, the Measures expressly provide that entering into an APA shall not remove the tax authorities' right to carry out an inspection relating to the years prior to the request to conclude an APA.

Only enterprises which fulfil the following criteria are authorised to conclude APAs:

- the annual amount of transactions is equal to or exceeds RMB 40 million;
- the obligation to declare transactions has been complied with; and

- the rules relating to preparing, preserving and disclosing documentation have been complied with.

## **4. Cost Sharing Agreements**

The Measures describe in detail the rules relating to cost sharing agreements introduced by the new Enterprise Income Tax Law. The tax treatment of cost sharing agreements implemented by the Measures is similar to the tax treatment provided for by the OECD.

Cost sharing agreements apply to the development or sale of intangible assets or the sharing of profits deriving from the provision of services. The costs provided for by the cost sharing agreements are deductible for income tax purposes.

Cost sharing agreements shall mainly include, in addition to the essential contractual clauses, the calculation of the projected profits and the determination of the cost sharing, an explanation regarding compliance with the arm's length principle, each contractor's accounting method, and the accession and exit rules.

A cost sharing agreement must be submitted within 30 days following its execution to the local tax authorities, which must forward the agreement after checking to the National tax authorities for record.

### **4.1. Principles**

The costs set forth in cost sharing agreements must be reasonable, determinable and foreseeable and must correspond to a reasonable commercial transaction in the scope of the normal running of the company.

### **4.2. Development and sale of intangible assets**

The intangible assets referred to by the Measures include in theory land use rights, copyrights, patents, trademarks, clientele, distribution networks, trade names, trade secrets, know-how, utility models and industrial designs.

### **4.3. Services**

In general, cost sharing agreements may only be concluded for services relating to supplying a group or marketing and promotion for a group.

### **4.4. Accession and exit rules for a cost sharing agreement**

In accordance with the Measures, a new contracting party must make a reasonable payment upon entering into the cost sharing agreement. An exiting party must transfer the results which it benefited from to the other contracting parties in consideration for compensation paid by the other contracting parties. Upon termination of the agreement, the existing results must be reasonably shared between the contracting parties.

## **5. Non-deductibility**

Payments carried out in the following cases are not deductible:

- no reasonable business reason or unrelated to business;
- violation of the arm's length principle;
- violation of the principle of coherence between the costs and profits;
- failure to submit or prepare the documentation;
- if the outstanding term of the contracting company is lower than 20 years on the date of the conclusion of the agreement.

## **6. Sanctions and penalties**

### **6.1. Criminal sanctions**

Chinese law does not provide any express provisions stipulating that an unusual transfer of profits constitutes the offence of tax evasion, which is sanctioned by criminal fines and, where applicable, imprisonment of the directors in the most serious cases.

### **6.2. Administrative sanctions**

Like the new Enterprise Income Tax Law, the Measures do not stipulate that transfer pricing manipulations or tax evasion constitute tax fraud. Therefore, no administrative sanctions are laid down in addition to any adjustment carried out by the tax authorities.

However, the tax authorities are entitled to impose late payment interest equal to the interest applied by the People's Bank of China during the same period plus 5% additional interest. However, this 5% additional interest cannot be imposed if the enterprise has duly prepared the documentation or if

the enterprise is exempted from providing such documentation and has duly provided the documents as required by the tax authorities.

Other administrative sanctions laid down by the Measures are relatively low. Failure to submit a declaration of transactions concluded between affiliated companies or failure to prepare the documentation is liable to a RMB 10,000 fine at most. Submitting inaccurate or incomplete documentation or refusing to submit documentation is liable to a RMB 50,000 fine.

However, a taxpayer who refuses to apply the tax adjustment decision must pay a fine ranging from 50% to 500% of the amount of the tax adjustment and a 0.05% penalty for each day of delay.

**Emmanuel Meril**

CMS Bureau Francis Lefebvre  
emmanuel.meril@cms-bfl.com



## France

### Corporate tax

The Finance Act has once again introduced many measures this year but the large majority of these measures do not call for commentary in this article. Therefore, we shall only highlight that:

- the reduced tax rate applying to capital gains on listed real estate companies and some real estate gains has been increased from 16.5% to 19% with effect from 1 January 2009,

- the annual flat-rate tax, which can represent EUR 110.000 per year and which is payable by all companies liable for corporate income tax, shall be gradually withdrawn over a three-year period,

- SMEs – employing less than 2,000 persons – may debit the losses recorded by their foreign subsidiaries held at 95% and their foreign branches from their French results, provided that they gradually recover these losses from the foreign entity's profits, or failing which, upon expiry of a five-year period. Only losses recorded in a Member State of the European Union or a State with which France has concluded a tax treaty providing for mutual assistance with regard to information exchanges and combating tax fraud and evasion are affected. Recovery of losses upon expiry of the five-year period, even if no foreign profits are recorded, may in some circumstances conflict with the Marks & Spencer case law.

The most significant measures were adopted in the scope of the economic stimulus plans. These measures enable French companies to obtain early refunds of credits owed by the State: mainly carry-back credits and research tax credits. We would like to take this opportunity to provide an overview of French research tax credits, which make France a form of tax haven for companies seeking to set up research centres.

#### **1. A high tax credit which is refundable immediately this year**

The research tax credit system was substantially improved last year and has been slightly improved again this year. Since last year (tax credit relating to 2008, deductible from the corporate income tax for 2008, which is payable in 2009), the amount of the tax credit is no longer limited and is calculated based on the costs incurred during the year. The research tax credit is comprised of a volume-based share (percentage of research costs during the year) and a variable share (a positive share if the amount of costs compared to previous years has increased or a negative share, which consequently reduces the total

‘ An overview of French research tax credits ’

research tax credit if the company incurred less research costs during the year compared to previous years). The variable share, upwards or downwards, which adds to the volume-based share of the tax credit and which made the calculation thereof particularly complicated, has been withdrawn.

In theory, the credit represents 30% of the research costs of the annual fraction of costs which do not exceed EUR 100M and 5% of the fraction of costs exceeding EUR 100M.

However, companies, which were not entitled to a tax credit during the previous five years, qualify for an even more preferential rate: 50% during the first year of application of the credit and 40% during the second year of application, provided that no affiliated company has benefited from the credit during the aforementioned five-year period.

In theory, the research tax credit reduces the amount of corporate income tax relating to the previous financial year and then successive financial years up until the third financial year. The outstanding balance is only refundable at the end of this period.

Article 95 of the Rectified Finance Act 2008 (Act of 31 December 2008) authorises immediate refunds on an exceptional basis as 1 January 2009 of:

- outstanding research tax credits owed to companies for 2005, 2006 and 2007;
- the tax credit resulting from research costs incurred in 2008 up to the fraction of this credit, which exceeds the corporate income tax relating to the result of the financial year ended on 31 December 2008 (or in progress on this date).

## **2. Tax credits cover all forms of research**

The definition of the scientific or technical research activities encouraged by the tax credit covers the three main areas of fundamental research, applied research and experimental development programmes carried out using prototypes or pilot installations. Therefore, a company needs only to carry out an operation falling within one of these areas to qualify for the research tax credit. In this respect, the tax authorities have specified that work intended to make technical improvements to a product or a process continue to fall within the scope of research. However, work no longer falls within the scope of research if the product or process is largely finalised and the main objective is to find prospects or improve productivity or profitability.

## **3. Territoriality of research costs**

In theory, tax credits are reserved for costs corresponding to research operations carried out in France, in another Member State of the European Community or in the European Economic Area (except for Liechtenstein).

However, patent protection costs and technological intelligence costs are taken into account even if they correspond to operations carried out in a State not included in the above list insofar as they are taken into account to calculate the taxable profit in France.

Moreover, a company is warranted in taking into account research costs incurred, even in the event where they are passed on, including abroad. A ruling by the Versailles Administrative Court of Appeals caused confusion by refusing to take into account such research costs in such circumstances, but advance ruling no. 2008/8 of 13 May 2008, which was incorporated in an administrative order of 2008 (documents produced by taxpayers which are enforceable against the tax authorities) dismiss the fears which could have arisen from the ruling in the case in point.

## **4. Costs taken into account**

The spectrum of costs taken into account is very wide, including in particular:

- depreciation allowance for newly purchased assets used for research,
- staff costs. Staff costs relating to newly qualified doctors employed under a permanent contract are taken into account at double the amount thereof for a period recently fixed at 24 months,
- costs relating to protecting patents and obtaining vegetable certificates, including costs incurred abroad insofar as they have an impact on the French results,
- subcontracting costs up to a limit of EUR 10M where the contractor is independent from the principal (or EUR 12M if the subcontractor is a public research body, university, charitable foundation in the accredited research sector), and within the limit of EUR 2M where the contractor is dependent on the principal,
- fashion collection costs for industrial companies in the textile, clothing and leather goods sector.

Public subsidies and refundable advances are deducted from the calculation base for the tax credit.

## 5. Assignments and grants of patents

In addition to this research tax credit, which is the main measure of the research incentive system, we would like to highlight that the taxation of assignments of patents, patentable inventions and industrial manufacturing processes amounts to only 15% since 2008 (instead of the standard rate of 33.33%), provided that there are no affiliated relations between the assignor company and the assignee company.

The same reduced rate taxation applies to grants of patents or patentable inventions. In this case, the fees paid are only deductible up to  $15/33\frac{1}{3}$  of the amount thereof if the payor company is affiliated to the grantor company (ratio between the reduced rate of 15% and the standard rate of 33.33%). It is normally in the interest of the patent holder to grant rather than assign a patent to an affiliated company since this operation qualifies for the reduced rate applying to grants and not to assignments of patents.

**Emmanuelle Féna-Lagueny**

CMS Bureau Francis Lefebvre

[emmanuelle.fena-lagueny@cms-bfl.com](mailto:emmanuelle.fena-lagueny@cms-bfl.com)



**Germany**

## **Corporate tax**

### **1. Losses incurred abroad**

With a view to preventing tax fraud, German taxable income could not be reduced by losses incurred abroad in primarily tax-driven models up until 2009.

As a result of the European Court of Justice's judgment in the *Rewe Zentralfinanzamt* case as of 29 March 2007 and following the European Commission's request of 18 October 2007 to Germany to bring the respective regulation in the German Income Tax Act in line with the principles of European tax law, through the "Jahressteuergesetz 2009", Germany has now implemented the tax deductibility of foreign losses in Germany provided the losses come from countries in the European Union and EFTA (excluding Lichtenstein). As a result, the restriction on the tax deductibility of foreign losses in Germany no longer applies in this respect.

### **2. Real estate investments in Germany by foreign corporations**

Foreign real estate investments may be affected considerably by an amendment implemented through the "Jahressteuergesetz 2009" according to which not only the sale but also rental income of foreign corporations will be qualified as trade income even if they have neither a permanent establishment nor a representative in Germany. For example, the profit accounting system and depreciation rates will change and may have considerable financial consequences.

### **3. Regulations with regard to foreigners who are subject to limited tax liability in Germany**

The German Income Tax Act includes a special provision with regard to foreigners who are subject to limited tax liability in Germany. This rule (§ 49 German Income Tax Act) was completely revised by the "Jahressteuergesetz 2009". Some of the amendments which may have considerable practical consequences are:

- it will be authorised to reduce the taxable income by the "Werbungskostenpauschbetrag" (lump-sum of expenses assumed to be connected with the taxable income) and the "Altersentlastungsbetrag" (tax reduction granted to all persons aged respectively over 60 and 65);

- up until 2009, the minimum tax rate for foreigners with German income was 25%: this regulation was deleted, so that the standard tax rate

Business Tax Reform 2009:  
Losses incurred abroad and  
real estate investments in  
Germany by foreign  
corporations

will apply irrespectively of whether they are subject to unlimited tax liability in Germany or limited tax liability;

- salaries, investment income or other forms of income received from individuals outside of Germany are subject to a lump-sum tax payment. This will also apply in the future, while the exceptions —compared with the situation up until 2009— have been extended. For example, a lower tax rate may apply if the individual is in a position to provide proof of expenses connected with the specific income.

#### 4. Tax compensation procedure

Income tax on for example artistic, sports, entertainment or comparable performances carried out in Germany by individuals living outside of Germany has to be withheld at source at a flat-tax rate of 20% up until 2009.

This tax rate is reduced to 15% as from 2009.

While doubts were raised as to whether this provision complies with European Community law in the light of the implementation of the European "Mutual Assistance Recovery Directive" as of 1 July 2002, the German Federal Tax Court decided in November 2007 that the German provision is in line with European law because up until now, the different regulations in the various European countries do not ensure that the country in which the performances are carried out receive the taxes due.

the relevant event *and* that the assets which are not necessary to run a business shall not exceed 50% of the total amount of the assets.

*Option 2:* Heirs continuing the business for a period of at least ten years will be tax-exempt for 100% of the fair market value of the business assets provided the total amount of salaries paid to the employees within this period is not less than 1000% of the average of the annual salaries paid to the employees in the five tax years before the relevant event *and* that the assets which are not necessary to run a business shall not exceed 10% of the total amount of the assets.

This preferential treatment is applicable to business assets held by individuals or partnerships, a shareholding in a corporation exceeding 25% or agricultural businesses.

It is clear that in the light of the inheritance tax reform, expert advice with regard to the possibilities of organising and optimising business activities is of great importance.

**Gerd Seeliger**

CMS Hasche Sigle

gerd.seeliger@cms-hs.com

## Inheritance Tax

As already mentioned in the previous CMS Tax Connect issue, Germany has implemented a new Inheritance Tax Act as from 1 January 2009. One of the key issues of the tax reform is the preferential treatment of business assets. As German inheritance tax law applies if either the decedent **or** the heirs live in Germany, this reform is also of importance for foreign individuals. Therefore, the two options of preferential treatment are described again as follows:

*Option 1:* Heirs continuing the business for a period of at least seven years will be tax-exempt for 85% of the fair market value of the business assets provided the total amount of salaries paid to the employees during this period is not less than 650% of the average of the annual salaries paid to the employees in the five tax years before



## Hungary

# Corporate tax

## Amendments to Hungarian tax law

Hungarian tax law undergoes significant changes at the beginning of each year and this year is no exception in this respect. We have highlighted below some of the most interesting changes, which will have the largest impact on taxpayers. Please note that this information is very general and often simplified, and is not meant to replace specific advice.

### 1. Tax amnesties

It has recently become more and more common for the Hungarian legislator to introduce full or partial tax amnesties in respect of income from dubious sources and/or affected by tax avoidance. Hence, two major tax amnesties have been introduced, one of which is also linked to encouraging investment in Hungarian State securities.

The first amnesty affects both individuals and corporations, though in a slightly different manner and is aimed at making income earned by controlled foreign companies ("CFC") transparent and channelling such income into Hungary. A CFC is a company having its seat in a low-tax jurisdiction with which Hungary has not concluded a double tax treaty. Dividend income received from a CFC is normally fully taxable and similar rules apply to individuals as well. However, according to the limited amnesty, such income could be subjected to only a limited effective tax rate, if repatriated, declared and partially converted into Hungarian State securities. The amnesty is a one-off possibility. In particular, it may only be applied to profits distributed from income that was booked by the CFC prior to 30 June 2008. Nonetheless, the amnesty may be applied in respect of profits distributed in both 2008 and 2009.

The second amnesty would mostly appeal to small, privately held, Hungarian companies (and their owners), and provides that dividend income paid to individuals out of profits derived from the cancellation of loans granted by the same owners is taxed at 10%.

### 2. Company car tax

The amendment of the motor vehicle tax act has reformed the taxation of company cars as from 1 February 2009.

The new company car tax is a tax on capital payable by non-individual car owners or by the lessee in the case of a financial lease. Furthermore, cars in respect of which tax-deductible expenses are recorded will

Two major tax amnesties have just been introduced in Hungary. Amendments to the real estate sector

also be subject to the tax even if owned by an individual. At the same time, income arising due to the private use of a company car will be exempt from personal income tax and healthcare or unemployment contributions will not be payable (as under the previous system). Finally, in order to eliminate economic double taxation, the entire amount of the already existing motor vehicle tax (payable to the local authorities) is deductible from the amount of company car tax.

The monthly rate per car will be HUF 7,000 (approximately EUR 24) in respect of the cylinder capacity of less than 1,600 cm<sup>3</sup> and HUF 15,000 (approximately EUR 50) above such limit (with separate limits for rotary engines).

The overall result of the new regulations is that the tax burden might be significantly lower for those who were already paying the company car tax, whereas the number of taxpayers might increase by several new taxable persons.

### **3. Amendments affecting the real estate sector**

The amendments include several changes which might be important for companies and businesses in the property market. In particular, the changes relating to transfer duties and local business tax should be highlighted.

The conditions of applying the 2% preferential rate (applicable if the newly acquired property is being resold within two years) of transfer duty applicable to traders have become stricter. Fulfilling the formal criteria of being registered as a real estate trader is no longer sufficient to apply the preferential duty rate, the majority of the annual net sales revenue should also derive from this activity. Real estate funds remain an exemption as they are entitled to apply the preferential rate regardless of their revenue.

The good news is that the procedural rules relating to applying the above-mentioned preferential rate will be slightly simplified. It will therefore be easier to meet the two-year deadline (i.e., the requirement that the property has to be resold within two years).

For real estate developers, it has been a long-term problem that while in the case of real estate developments purchased and resold as goods, or "re-invoiced" through a chain of contracting agreements, the cost of goods sold and the value of subcontractors' work was deductible from the net sales revenue (which is the base of the local business tax). Meanwhile, such tax base reduction was limited if the typically residential real estate constructed by subcontractors was subsequently

sold by a real estate developer. However, as from 1 January 2009, the above-mentioned value of subcontractors' work is deductible from the local business tax base as quasi-intermediate services, if they were used for construction of "newly" sold (i.e., sale before the operating licence becomes final, or the first sale thereafter) "housing".

The new rules on property transactions with "disproportionate remuneration" can involve significant duty-related risks. According to this rule, if the actual remuneration received in exchange for the sale of property is less than 50% of the market value of the property, then the difference between the actual remuneration and 50% of the market value will be classified as a gift and gift duty (up to 40%) becomes payable.

Although not an amendment initiated or even intended by the legislator, the Hungarian Constitutional Court quite recently abolished the possibility of calculating property taxes based on the approximated (deemed) value. This led to the complete abolition of the "luxury tax", which used to be a value-based property tax levied on high-value properties. Due to the unconstitutional nature of the calculation method of its tax base, the Constitutional Court deemed it was preferable to abolish this tax altogether.

### **4. Important amendments affecting individuals**

An important step towards eliminating inheritance tax has involved an abolition of tax on legacies with a value of up to HUF 20 million (approximately EUR 67,000) inherited by the closest relatives (mostly parent and child relatives and between spouses, etc.).

Another favourable amendment is the introduction of a 25% flat tax for individuals on dividend income received from non-listed securities and shares, i.e. the previous tax bracket of 35% has now been abolished. The tax rate for dividend income received from securities listed on stock exchanges in the EEA region will continue to be 10%.

### **5. More stringent sanctions**

As from February 2009, tax-related sanctions have become stricter, from which the Hungarian Government expects to collect increased tax revenues. In the future, certain serious misconduct causing shortfalls in tax revenues will be sanctioned by higher penalties (up to 75% of the shortfall in tax) than beforehand.

The amendment extends some sanctions to those who are not involved in the particular tax relationship, e.g., for failing to issue an invoice, even

the immediate supervisor of the employee obliged to do so may be penalised.

Another measure relates to the distribution of goods without proof of origin where the tax authority may impose a default penalty.

## **6. Elimination of cash payments**

As from 1 February 2009, several new regulations were introduced in order to eliminate and control cash payments. However, some of them have already been abolished or amended.

Previously, businesses were required to determine the maximum daily closing amount of their petty cash within the scope of their cash management policy. In the future this amount may not exceed 2% of the total gross income for the previous year.

## **7. Public procurements, public dues, outstanding tax liabilities**

The “saga” of Article 36/A of the Act on the Rules of Taxation concerning participants in public procurement related projects has now hopefully come to an end. The regulation was recently amended and the start of its application was again postponed up until 15 February 2009.

The main idea behind these new provisions is to make sure that no contractor or subcontractor is allowed to receive payments within the scope of a public procurement process (borne ultimately by the Hungarian State), which has accumulated public debts. For this reason, two compliance requirements were introduced to any contractor or subcontractor who has been informed, by its principal, that it is participating in a public procurement-related project. The first one is to pass on this information to its own subcontractor(s), the second one is to withhold all payments to its subcontractor(s) over the monthly net amount of HUF 200,000 (calculated net of VAT) unless the subcontractor provides a tax certificate stating no public debts, or, as a new possibility, unless its name is listed in the database on taxpayers without any public debts. Non-compliance with these requirements would have two consequences. First, a default penalty of up to 20% of the non-withheld payments could be levied for failing to observe the information requirement. Second, the payer (i.e., the principal) would be jointly and severally liable for all of the recipient’s public debts (the subcontractor) to the extent of the payments made.

## **8. More to come**

Although these amendments have just entered into force, further significant changes to the tax laws are expected as from 1 July 2009 and 1 January 2010 due to the effects of the economic crisis. According to current information, these may result in a decrease in income tax rates while significantly widening the tax bases, introduction of wealth tax, increase in the general VAT rate and the decrease in employment-related liabilities (social security type contributions for employees).

### **Eszter Kalman**

Ormai és Társai CMS Cameron McKenna LLP  
eszter.kalman@cms-cmck.com

### **Tamas Feher**

Ormai és Társai CMS Cameron McKenna LLP  
tamas.feher@cms-cmck.com



Italy

Measures against the economic crisis

## Corporate tax

In order to face the economic crisis, the Italian Government has adopted a Law Decree (No. 185 of 29 November 2008, converted into Law No. 2 of 28 January 2009) containing various tax reforms some of which are briefly summarised below.

### 1. Readjustment of tax basis

In some cases, companies applying IFRS/IAS may opt for the readjustment of the differences between the tax and civil value of the assets by paying a substitute tax at the rates of 12, 14 and 16%. In some cases, standard tax rates apply.

Under certain circumstances, companies which carried out mergers, de-mergers and contributions of going concerns may elect to increase the tax basis of the goodwill, trademarks and other intangibles by paying a substitute tax equal to 16%.

The readjustment is also provided for with regard to assets not comprised of goodwill, trademarks and other intangibles but different tax rates apply.

### 2. Revaluation of immovable property

Companies not adopting the IFRS/IAS may revalue immovable property, which is booked in the balance sheet for the tax year in progress on 31 December 2007 (the revaluation will occur in the balance sheet for the following tax year). Building areas and immovable property representing inventory (i.e. *immobili merce*) cannot be revaluated.

The revaluation can also be carried out for civil purposes only without any tax impact.

For the purpose of obtaining the tax recognition of the increased value, a substitute tax equal to 3% or 1.5% is due depending on the type of immovable property to which the revaluation is applied.

The equity reserve created to balance the increased asset values can be recognised by paying a 10% substitute tax.

The revaluation of the immovable property will have a tax impact as from the fifth tax year following the tax year during which the revaluation occurred.

### 3. Abuse of law

The Italian Supreme Court has recently expressed the view that any act and/or operation carried out by the taxpayer with the main purpose of obtaining a tax advantage is considered as an "abuse of law". This abuse, according to the Supreme Court, is contrary

to the fundamental duties prescribed by the Italian Constitution and enables any advantage obtained by the taxpayer to be disregarded (see, *inter alia*, Decisions No. 8772 of 4 April 2008; No. 10257 of 21 April 2008; No. 25374 of 17 October 2008; No. 30057 of 23 December 2008).

This view represents a development of some of the thoughts already expressed by the Supreme Court in the past on dividend washing operations (see, *inter alia*, Decision No. 20398 of 29 April 2005). Moreover, it has been pointed out that as a result of the above, the taxpayer's conduct is always questionable, i.e., whether or not it falls within the scope of a specific anti-avoidance provision, irrespective of the type of transaction/structure under scrutiny, regardless of the kind of tax in question. According to the Supreme Court, the courts may make a charge of "abuse of law" at any stage of the judicial proceedings even if not expressly challenged by the tax authorities.

## VAT

### Payment of VAT when the invoice is paid

As an exception to the general rule, if payment occurs after the invoice is issued, VAT on the sale of goods and on the supply of services becomes due when the invoice is paid. Such a rule is not applicable to transactions carried out with private consumers.

The entry into force of this rule – which is only applicable to taxpayers with turnover not exceeding €200.000 – is subject to the publication on the Official Gazette of a Ministerial Decree, already approved and further implementing the rule.

#### **Carlo Romano**

CMS Adonnino Ascoli & Cavasola Scamoni  
carlo.romano@cms-aacs.com

#### **Guido Zavadini**

CMS Adonnino Ascoli & Cavasola Scamoni  
guido.zavadini@cms-aacs.com



## Maghreb

# Corporate tax and VAT

## Morocco

### 2009 Finance Act

The 2009 Finance Act continues the harmonisation process of Moroccan tax legislation and aims to centralise all tax legislation in a single document: the General Tax Code. The following presentation is not exhaustive and covers only the main changes which were introduced.

#### 1. Tax reduction in the event of a capital increase

Companies incorporated in Morocco before 1 January 2009 benefit from a 20% corporate tax reduction on any capital increase made between 1 January 2009 and 31 December 2010.

Such reduction is subject to conditions relating to the type of contribution to the capital and on the stability of the capital over a period of five years.

This tax reduction is limited to companies whose turnover during the last four tax years was below MAD 50 million excluding VAT (approximately EUR 4.5 million).

#### 2. Clarification on the offshore holdings regime

The Finance Act specifies that companies benefiting from the Moroccan offshore holdings regime, which includes tax incentives, may only deal with foreign securities.

#### 3. Withdrawal of deduction on capital gains

Capital gains on the sale or withdrawal of tangible or intangible fixed assets of an enterprise no longer benefit from any deduction. This applies to corporate income tax as well as personal income tax.

#### 4. Irrevocability of the corporate tax option

In order to simplify tax return procedures, the choice of partnerships such as limited partnerships (*sociétés en nom collectif*) to opt for the corporate tax regime is irrevocable.

**Morocco:** The 2009 Finance Act continues the tax legislation harmonisation process

**Algeria:** significant amendments for foreign entities operating

## 5. Real estate

The 50% corporate tax reduction granted to real estate developers who conclude a convention with the Moroccan State for the construction of social housing is extended for two consecutive tax years from 1 January 2008.

In addition, in order to increase the number of potential beneficiaries of the tax reduction granted to real estate developers involved in building university accommodation, which includes taxation at the rate of 17.5% on lease revenues, the size of the eligible projects has been reduced from 250 rooms to 150.

Real estate access for individuals is facilitated by the possibility of deducting the interest on loans for the purchase or the construction of real estate as a main residence from their total revenue.

Initially, there was no time limit for the deduction of interest. As a result, the deduction was subject to the four-year statute of limitation.

This deduction is now limited to a period of seven years from the date on which the building permit is issued. After the seven-year period, if the tax authorities consider that the housing is not used as a main residence or the building has not been completed, the tax authorities can make a tax adjustment including penalties.

However, if the conditions are met, the individuals benefit from a tax reduction for the outstanding interest to be paid.

## 6. New personal income tax rates

The new personal income tax rates are fixed as follows:

Revenue	Tax Rate
Up to MAD 28,000	0
From MAD 28,001 to MAD 40,000	12%
From MAD 40,001 to MAD 50,000	24%
From MAD 50,001 to MAD 60,000	34%
From MAD 60,001 to MAD 150,000	38%
Above MAD 150,000	40%

## 7. Reduction of the scope of application of the simplified regime

Taxpayers whose annual turnover exceeds the following amounts are henceforth excluded from the possibility to opt for the simplified net regime for professional revenue:

- MAD 2,000,000 (EUR 180,000) for business professions, industrial or artisanal activities and fishing boat owners;

- MAD 500,000 (EUR 45,000) for service providers, self-employed persons' earnings or earnings which are repeated and cannot be considered as farming revenue or as securities revenue.

Taxpayers whose annual turnover exceeds the following amounts are henceforth excluded from the possibility to opt for the simplified net regime for profits:

- MAD 1,000,000 (EUR 90,000) for business professions, industrial or artisanal activities and fishing boats owners;

- MAD 250,000 (EUR 22,400) for service providers, self-employed persons' earnings or earnings which are repeated and cannot be considered as farming revenue or as securities revenue.

## 8. Value Added Tax

The exemption on domestic sales of pharmaceutical drugs with regulated prices and sugar no longer applies to taxpayers whose turnover exceeds MAD 2,000,000 (EUR 180,000).

Moreover, the VAT exemption for imports of pharmaceutical drugs is now granted for a larger number of drugs, in particular drugs to fight cancer and hepatitis.

## 9. Registration fees

The rate of registration fees is reduced with regards to the incorporation and capital increase of companies and Economic Interest Groupings from 1.50% to 1%.

## 10. Mandatory online tax return starting from 2010

Tax returns and tax payments will be required to be carried out online from 1 January 2010 for companies whose turnover exceeds MAD 100 million (EUR 8.96 million) and from 1 January 2011 for companies whose turnover exceeds MAD 50 million (EUR 4.5 million).

## 11. New auditing prerogatives relating to transfer costs

An obligation to provide information at the request of the tax authorities has been introduced. The aim is to obtain the following information:

- the type of relations with the company located outside of Morocco,
- the type of services provided or the products marketed,
- the method for determining the prices of operations performed between these enterprises and the applicable justifications,
- the tax regime and the tax rates applicable to enterprises located outside of Morocco.

## 12. Tax proceedings

Several modifications have been made concerning tax proceedings. In particular, the Finance Act provides that it is forbidden to bring action before a court while making a claim to the Local Taxation Commission or the National Tax Appeals Commission.

Moreover, the General Tax Code now expressly provides that the taxpayer can ask for additional time in the event of a tax adjustment, subject to sufficient guarantees.

## 13. Customs

The customs authorities can award "approved economic operator" status to those who meet the conditions to be defined by a decree.

This status aims to ease customs procedures and grant benefits.

### Frédéric Elbar

CMS Bureau Francis Lefebvre  
frederic.elbar@cms-bfl.com

### Wilfried Le Bihan

CMS Bureau Francis Lefebvre  
wilfried.lebihan@cms-bfl.com

# Algeria

The 2009 Finance Act has introduced several significant amendments especially for foreign entities operating in Algeria. These amendments create either a heavier tax burden on foreign investment or introduce additional procedural requirements. The following presentation is not exhaustive and covers only the main changes which were introduced.

## 1. Branch tax

The 2009 Finance Act has introduced a "branch tax" by inserting an Article 46 (9) into the Algerian Direct Taxation Code.

Prior to the new Finance Act, only dividends transferred from an Algerian company to a foreign shareholder were subject to a 15% withholding tax on dividends.

According to the new provision, profits transferred to a non-resident foreign company by its branch established in Algeria or any Algerian permanent establishment are considered as distributed profits subject to the same final 15% withholding tax.

## 2. Mandatory tax statement on any transfer of funds abroad

The 2009 Finance Act inserted Article 182 *ter* into the Algerian Direct Taxation Code which introduced a new section entitled "transfer statement".

Formerly, two separate provisions (one for corporate income tax, the other for personal income tax) provided that a debtor located in Algeria had to provide its bank with a tax clearance certificate from the tax authorities before any transfer of funds to a foreign enterprise.

The new statement requirement is more burdensome since it requires the debtor to provide a statement (declaration) to the tax authorities.

Indeed, all forms of transfers of funds to natural persons or legal entities, which are not resident in Algeria, are now subject to a prior statement to the territorially competent tax authorities.

A certificate confirming the tax treatment of the amount is then issued to the person making the statement at most seven days from the date of submission of the statement, in order to present it for the transfer demand. This seven-day period is not applicable if tax obligations are not met. In this case,

the certificate is issued after the tax situation has been sorted out.

In particular, the certificate includes the withholding taxes applied or the references to the laws and regulations granting the exemption or the reduction.

Since banks are required to request the above-mentioned certificate for all transfers, it will not be possible to transfer any funds abroad without such tax certificate.

It must be noted that the sums paid in consideration for import operations subject to the tax on banking domiciliation are not subject to this obligation.

### **3. Additional requirements for VAT refunds**

VAT refunds are subject to the following additional requirements:

- the request for a VAT credit must be made before the 20<sup>th</sup> of the month following the calendar quarter during which the credit is created;

- the tax credit for which a refund is requested cannot be offset. The credit must be annulled by the tax debtor as soon as the refund request is submitted;

- the amount of the tax credit for the period of three consecutive months for which the refund is requested must be equal or exceed DZD 30,000 (EUR 306).

### **4. Refunds of VAT credits when closing a business**

The refund of VAT tax credits in the event of closure of a business is now subject to the prior settlement of all other tax obligations.

### **5. Capital gains**

Capital gains on the sale of built or non-built real estate by individuals are no longer subject to taxation.

Capital gains on the sale of stocks and assimilated securities of companies listed on the stock exchange as well as shares in mutual funds (*Organisme de Placement Collectif en Valeurs Mobilières*) are exempt from corporate income tax and personal income tax for a period of five years from 1 January 2009. The same operations are exempt from registration fees.

Moreover, capital gains generated on sales of shares or stocks by natural persons or foreign legal entities are subject to final taxation at the rate of 20% in consideration for corporate income tax and personal income tax.

### **6. Penalties in the event of breach of conditions relating to tax incentives**

In the event where an investment benefits from tax incentives and the investment is not performed or if the conditions of approval of the incentives are breached, the investor shall lose said incentives. In addition, any tax, duty or royalty, which was avoided shall become immediately due and shall be increased by penalties for late payment calculated from the date on which the tax, duty or royalty should have been paid.

Such penalties also apply when the beneficiary of the tax incentive commits fraudulent acts and is held liable by a court.

### **7. Limitation of VAT deductibility**

If the deduction of VAT is to be carried out for the month or quarter during which the tax was paid, no VAT deduction can be performed in the event where the amount of VAT exceeds DZD 100,000 (EUR 1,020) per operation paid in cash.

### **8. Penalty in the event of a fraudulent act**

The penalty due in the event of a fraudulent act shall be reduced from 200% of the total tax amount to 100%.

### **9. Tax procedure and appeals**

Several changes were made to the Algerian Tax Procedure Code.

In the event of an audit of a tax return by the authorities, the agent who intends to rectify the tax return must send notification of the intended adjustment to the taxpayer including the tax basis and the applicable tax calculation. Without such notification, the tax procedure is null and void.

Moreover, final notification of the tax adjustment must be sent by registered post to the taxpayer.

It can be noted that the Tax Procedure Code now provides that the tax authorities can conduct an in-depth audit of the whole tax situation of a natural person, whether said person is a tax resident of Algeria or not.

The time limit for bringing an action before the tax commission to oppose a decision is extended. The Tax Procedure Code now provides that the taxpayer

has four months, instead of two, from the date of receipt of the authorities' decision on the claim to bring action before the competent commission (the scope of competence of the regional commission has been increased).

**Frédéric Elbar**

CMS Bureau Francis Lefebvre  
frederic.elbar@cms-bfl.com

**Samir Sayah**

CMS Bureau Francis Lefebvre  
samir.sayah@cms-bfl.com



## Netherlands

### Corporate tax

#### Proposed tax exemption for group interest and abolishment of dividend tax

##### **Dutch finance companies and real estate funds: new opportunities?**

The Dutch Ministry of Finance announced that it will investigate the possibility of amending tax legislation with regard to interest payments between (related) companies. Depending on the outcome, the Dutch corporate income tax act may be adjusted in a way which could have a significant impact on Dutch corporate taxpayers' position, and it may offer an interesting opportunity to set up a finance company or real estate fund in the Netherlands.

The Ministry of Finance will investigate if interest payments between companies can be eliminated, fully or partially, from the Dutch tax base. In other words, a company receiving interest from another company would not be taxable on that interest, whereas the company paying interest would not be able to deduct the interest paid. This would obviously only be relevant for companies which are liable for corporate income tax in the Netherlands.

It is yet to be determined whether this would apply to all interest payments or only to interest payments between related parties. No further details are known as yet. It is expected that a more detailed plan and possibly a proposed new law will be published before summer 2009.

The changes are expected to increase the overall tax base and thus the tax revenue. The Ministry of Finance wants to provide this benefit to Dutch corporate taxpayers in the form of tax cuts, probably by reducing the corporate tax rate.

Through these measures, the Ministry of Finance intends to enhance the investment climate in general and attract international finance business to the Netherlands. At the same time, it wants to stop eroding the tax base in domestic situations of highly leveraged share purchases.

The plan was initiated in response to an article by three Dutch tax professors published in a leading Dutch tax magazine in August 2008. This article drew considerable attention from Dutch tax and finance specialists. In their article, the three professors proposed certain legislative changes in order to improve the Dutch investment climate and simplify the corporate tax system. The article made it to the front page of a leading Dutch financial newspaper.

Dutch finance companies and real estate funds: new opportunities?

The proposal put forward by the three professors contains, *inter alia*, the following measures:

- inter-company interest payments are to be fully disregarded, i.e. interest received from a related party is not taxable and interest paid to a related party is not tax deductible;

- dividend withholding tax is to be abolished;

- the corporate tax rate is to be reduced from 25.5% to 20%.

If it would actually lead to an amendment in Dutch tax law so that taxation and the deduction of interest payments would be restricted or completely abolished in combination with a reduced corporate tax rate and possibly the abolishment of dividend withholding tax, it would offer an excellent opportunity to set up a finance company or international real estate fund in the Netherlands. A treasury or finance centre in the Netherlands will not pay any tax on interest received from related parties. A Dutch real estate fund investing in foreign real estate can benefit from deducting interest abroad while receiving the interest exempt from tax in the Netherlands (achieving a so-called double dip).

Hopefully, the Dutch government will take this opportunity seriously in order to enhance the position of the Netherlands in international tax structuring.

**Jochem de Koning**

CMS Derks Star Busmann  
jochem.dekoning@cms-dsb.com



**Poland**

## Corporate tax

Starting from 1 January 2009 a few crucial amendments to the tax law in Poland came into force. Generally, most of the changes are favourable for taxpayers.

### **1. Amendment to the Corporate Income Tax Act**

One of the major changes applicable from 1 January 2009 is the classification of incurred costs of discontinued investment projects as tax-deductible costs on the date of the investments' disposal or liquidation. In light of the previous provisions of the Corporate Income Tax Act, such costs were specified as non-tax deductible costs.

The other significant change provides that income from conversion of a company into a partnership is classified as revenue for the company's shareholders, which is subject to Corporate Income Tax at the rate of 19%. The previous regulations were unclear in this respect.

### **2. Amendment to the Personal Income Tax Act**

One of the main changes to the Personal Income Tax Act is the modification of the tax base and the rates for employees' remuneration. Until 1 January 2009, three tax rates (19%, 30% and 40%) existed under Polish tax law, depending on personal income. Starting from 1 January 2009 only two tax rates (18% and 32%) are applicable. According to the amended tax provisions, the entire income of natural persons is subject to Personal Income Tax at the rate of 18% unless the sum of their income does not exceed the amount of PLN 85,528.

Other changes concern joint taxation of spouses one of whom or both are non-residents of the Republic of Poland for tax purposes, but are residents of other EU Member States. Such persons are entitled to use the preferable conditions of taxation, provided that they make at least 75 percent of their incomes during the tax year on the territory of Poland. The preferable conditions of taxation mean the possibility to be taxed jointly on the total of the spouses' incomes sum. In that case, tax is assessed in the name of both spouses at the double amount of the tax calculated on half of the joint incomes (revenues) of the spouses. The aim of this change is to guarantee equality and non-discrimination of taxpayers within the European Union.

‘ Favourable changes for taxpayers ’

### 3. Amendment to the Civil Law Activities Tax Act

An amendment to the Civil Law Activities Tax Act (the “**CLA tax**”) implementing Directive 2008/7/EC of 12 February 2008 concerning indirect taxes on the raising of capital entered into force from 1 January 2009. The most significant change to be introduced by the amendment is exempting from CLA tax:

- shareholders' loans,
- increase of the share capital of a company in exchange for a contribution in kind of an enterprise or its organised part.

### 4. Amendment to the Goods and Services Tax Act

A few main amendments to the Goods and Services Tax Act came into force from 1 December 2008, other of them – from 1 January 2009. The major changes introduced by the amendment are:

- eliminating the sanction amounting to 30 percent of the amount by which output tax was lowered if it is found that a taxable person declared lower output tax than the amount actually due;
- introducing the institution of call-off stocks, which results in eliminating the obligation of registering foreign entities for VAT purposes in Poland owing to the obligation to recognise the intra-Community acquisition of goods in respect of a transfer of its own goods from another EU Member State to a warehouse located in Poland; in such a case, if some conditions are met, the intra-Community acquisition of goods is recognised by Polish contractors at the moment of collecting those goods from the warehouse;
- simplifying the procedure of the intra-Community supply of goods in respect of a transfer of goods from Poland to a warehouse located in another EU Member State; if the Member State envisages a call-off stock procedure, a Polish entity recognises the intra-Community supply of goods at the moment of collecting those goods from the foreign warehouse by a foreign contractor;
- exempting from taxation the supply of buildings, structures or parts thereof after the first occupancy. The exemption will be available if the sale was made two years after the first occupancy;
- introducing the possibility of deducting output tax derived from import of goods directly

in tax returns without the requirement of paying this tax at a customs office in case of using the “simplified customs procedure”;

- expanding the possibility to return the difference between output and input tax within 60 days instead of 180 days from the date of submitting a request by a taxable person;
- replacing a mandatory mechanism of transferring input tax to the following accounting period if a taxable person did not carry out taxable activities inside or outside of the territory of Poland during the given period by an optional mechanism which allows a taxable person to file a request for VAT return in the period when taxable sale was not effected.

### 5. Amendments to the Tax Ordinance Act

From 1 January 2009 the rules of performance of tax decisions issued by tax authorities have been substantially changed. Decisions are not final are not immediately enforceable as was the previous practice. However, there are a few exceptions in which the tax authorities can enforce non-binding tax decisions. Tax Ordinance Act lists the conditions under which the tax authorities may enforce non-binding decisions.

#### Arkadiusz Michaliszyn

CMS Cameron McKenna LLP

arkadiusz.michaliszyn@cms-cmck.com



## Russia

# Corporate tax

## Recent Amendments to Russian Tax Legislation

### 1. Recent amendments to Russian tax legislation

#### 1.1 Corporate income tax (profit tax)

Significant changes have been implemented to corporate income tax.

The tax rate has been reduced from 24% to 20% (the regional part is now 18% and the federal part 2%)

Possibilities for deduction of expenses have been extended.

- limitations on per diem allowances have been removed

- an amount of 6% (previously 3%) of the contributions made for voluntary medical insurance can be deducted from the payroll expenses and those payments made be fully deducted provided that such insurance is mandatory for the taxpayer's business activities under Russian law

- losses resulting from the alienation of property rights

- the list of educational expenses which are deductible is extended (including principal and additional educational programmes)

New depreciation rules

- immediate depreciation bonus is increased from 10% to 30% for fixed assets belonging to three to seven groups (useful life three to 20 years)

- possibility to change the depreciation method is extended

- The special adjustment coefficient of 0.5 is cancelled

- capital improvements of fixed assets received under a free-of-charge use agreement can be depreciated

- capital improvements by the lessor regardless of the reimbursement of the lessee can be depreciated

- fixed assets discovered during an inventory can be depreciated

R&D expenses included in a list approved by the Russian government are immediately deductible at a ratio of 1.5

Significant changes have been implemented to corporate income tax, including the reduction of the corporate tax rate and new depreciation rules

## 1.2 Personal income tax

As regards personal income tax, as from 1 January 2008, the deduction on the amounts paid by a taxpayer to invest in a new development project or to buy a new house is increased from RUR 1 million to RUR 2 million.

## 1.3 Tax Procedures

The federal law of 26 November 2008 implemented significant amendments to the Russian Tax Code which mainly aims to improve taxpayers' situations. In particular, from now on, the new provisions which are more favorable to taxpayers can enter into force from the day they are voted if the new law provides so. Previously, new laws entered into force only one month after their official publication.

Further advantages are provided to taxpayers at the time of tax audits. In fact, if a taxpayer submits a modified tax return before the completion of the tax audit, the tax authorities have to base their tax audit on this new tax return. (p. 9.1 Article 88 of the Russian Tax Code).

The tax authorities are not entitled to use evidence obtained through illegal methods

The Ministry of Finance provided for additional deferrals

- it refers to federal taxes only and respective fines and interest

- the period of deferral amounts to five years and possibly without any collateral

However, the decisions to grant such deferrals may only apply until 1 January 2010.

Rights of the taxpayers have been improved as the new law provides that a decision to cancel the freezing of taxpayer's accounts has to be submitted to a bank representative no later than the day following the decision.

On the other hand, sanctions for infringement of tax legislation have been increased where a bank does not inform the tax authorities of the existence of bank accounts and (or) on the account balance of the taxpayer and may be liable to a RUR 10,000 fine.

## 2. Tax aspects of forgiveness of debts held on subsidiaries

There were some developments on the interpretation of the tax treatment of a debt forgiven by a parent company to its subsidiary.

As a general rule, pursuant to paragraph 1§11 of Article 251 of the Russian Tax Code, if a parent

company holds more than 50% of the shares in the subsidiary, the transfer of assets (in cash or in kind) to the subsidiary should be exempt from taxation.

There are still many debates over the possibility of applying this rule to debt forgiveness but the tax authorities' position on the forgiveness of debt due under the loan is becoming more favourable.

For a long time, the Russian Ministry of Finance (MINFIN) considered that the debt forgiven could not be qualified as the transfer of assets for the purpose of the application of the above exemption and consequently that both the principal and the interest were taxable at the level of the subsidiary (letters from 2005 and 2007).

However, MINFIN recently changed its position and issued a position which provides that paragraph 1§11 of Article 251 may be interpreted whereby the principal may be tax exempt whereas interest is taxable as non-operational income.

Such position has been confirmed by a Decision of the Arbitrary Court in November 2008.

MINFIN confirmed that such position would also apply in case of debt forgiveness by a subsidiary to its parent company and that only the principal of the debt should not be taken into account for tax purposes (letter of December 2008).

Pursuant to some comments, there would also be some arguments to consider that the interest also has to be excluded from the tax basis but for the time being, such position would probably be challenged by the tax authorities.

## VAT

The import of some technical equipment (as provided for by a list approved by the Government of the Russian Federation) is exempt from VAT unless identical equipment is produced in the Russian Federation.

The regime for 0% VAT rate procedure which applies to exports has been mainly simplified. From now on, taxpayers only have to submit the references of customs tax returns (instead of submitting copies of the tax returns). Moreover, the period for collecting the documents confirming the application of the 0% VAT rate has been increased from 180 days to 270 days (however, only with respect to the sale of goods placed under the export regime during the period from 1 July 2008 to 31 December 2009).

Possibility for the tax authorities to simultaneously take two decisions as a result of the tax audit: decision to partially refund VAT and refusal for the

additional part. Previously, when the decision to refund VAT was challenged by a taxpayer, there was no possibility for a partial payment of the VAT refund agreed by the tax authorities while waiting for the final decision on the points under discussion.

VAT paid on advanced payments is now deductible from the tax return relating to the period of payment where an invoice is issued (VAT was not previously deductible before effective delivery of the goods) (p. 3, Article 168, p. 12, Article 171 of the Russian Tax Code).

The tax authorities changed their position concerning the deductibility by a tax agent of VAT withheld and paid at its own expense (Letters No. 03-07-08/47 dated 28 February 2008 and No. 03-1-03/908 dated 17 March 2008).

There were also changes in the payment proceedings. VAT has to be paid monthly in equal instalments no later than the 20th day of the third month following the appropriate quarter (taxpayers were previously obliged to pay VAT relating to a quarter no later than the 20th day of the month following the appropriate quarter).

**Grégoire Caulliez**

CMS Legal

gregoire.caulliez@cmslegal.ru

**Stanislav Tourbanov**

CMS Legal

stanislav.tourbanov@cmslegal.ru



**Spain**

## Corporate tax

### **Tax deductibility of salaries of members of the Board of Directors who are also employees**

The Spanish Supreme Court recently issued a couple of decisions on 13 November 2008 with regard to the tax deductibility of salaries paid by companies to individuals who are employees and also members of the Board of Directors.

The Spanish Supreme Court established in this decision that the commercial relationship as member of the Board of Directors “absorbs” the employment relationship as employee of the company and denies the deductibility of the salary expense for corporate tax purposes as the remuneration of a member of the Board of Directors must be set forth in the by-laws of the company, which should determine the exact amount of such remuneration.

After these resolutions were issued, it seemed possible that in the event of a tax inspection, the deductibility of the salaries paid to these individuals was denied, if the tax inspector claimed that due to the fact that the individual is a member of the Board of Directors, the relationship between the individual and the company is a commercial relationship and all the requirements stated in commercial law should be fulfilled.

In view of this situation, the Spanish Tax Authorities issued a resolution on this matter on 12 March 2009 stating that remuneration paid to members of the Board of Directors, who are also employees of the company, would be tax deductible according to the rules relating to Spanish corporate income tax, when the company’s by-laws establish that being a member of the Board of Directors is remunerated (in general), even if all the requirements laid down by the commercial rules applying to these payments are not fulfilled (i.e., the exact amount of the remuneration does not need to be established for tax purposes).

‘ Tax deductibility of salaries of members of the Board of Directors who are also employees ,

## VAT

### **New VAT regime regarding monthly refunds**

Law 4/2008 approved by the Spanish Parliament on 23 December 2008 amended Spanish VAT law in order to introduce the possibility of obtaining a VAT refund on a monthly basis. The general regime involving an annual VAT refund still applies, but the taxpayer can opt for the monthly VAT refund regime.

As this is a personal choice, the entity must select this option as otherwise the general regime applies.

For these purposes the following requirements (*inter alia*) must be fulfilled by the company:

- The choice should be made in November of the year before the year in which the monthly refund would apply.
- The choice should be made by submitting a 036 tax return.
- The company must be up-to-date with its tax obligations and not covered by the simplified VAT regime.

The inclusion in this regime would apply at least for one year.

In the event where the requirements are not complied with, exclusion from the regime would apply for three years.

Once the entity opts for this new regime, the following obligations must apply:

- VAT refunds must be filed online.
- VAT books must also be filed online on a monthly basis.

In view of the above information, we recommend in order to decide whether this new regime is better for companies, to consider if the reduction in financial costs obtained is higher than the costs derived from the increase in the applicable formal obligations.

## Wealth tax

### Spanish wealth tax abolition

Another amendment has been introduced under Law 4/2008.

A 100% reduction in the gross wealth tax payable has been introduced. This means that Spanish wealth tax is no longer applicable and no obligation to file any tax return applies. This modification applies for 2008. Therefore no wealth tax would be payable for 2008 and no tax return would need to be filed with the Spanish Tax Authorities.

#### **Beatriz García-Renedo**

CMS Albiñana & Suárez de Lezo  
bgarcia@cms-asl.com



**Switzerland**

## Corporate tax and VAT

### Struggling for the Swiss banking secrecy

The recent decision by the Swiss Financial Markets Supervisory Authority (*FINMA*) to release data of the major Swiss bank UBS in the course of an international administrative assistance procedure has triggered intense political discussions regarding Swiss banking secrecy in relation to the international tax disputes Switzerland is currently engaged in. The data provided concerns about 300 wealthy UBS clients, who, allegedly based on advice provided by UBS employees, set up offshore companies to hold US securities with the purpose of circumventing the Qualified Intermediary Agreement (QI).

The QI's concluded between various banks and the US tax authorities, the Internal Revenue Service (**IRS**), grant the applying banks the status as a qualified intermediary, allowing the bank to distribute earnings from US securities to its clients at the respective reduced rate of US withholding tax instead of the generally withheld 30% NRA (non-resident alien) withholding tax. Therefore, a QI enables banks to offer its clients with no US tax liability benefits from any applicable double taxation treaty (*DTT*) concluded by the USA without obliging the bank to disclose the identities of the relevant clients.

On the other hand, the QI agreements require banks to ensure that no person liable to US taxes invests in US securities without disclosing the identity of the US client to the IRS. By incorporating an offshore company, US residents may indirectly hold US securities without having to be reported to the IRS by the given qualified intermediary.

According to the IRS, these formations of “sham-companies” and any advice or support to implement such formations constitute tax fraud respectively abetting tax fraud. Therefore, the IRS requested to be provided with data on US clients held by UBS in the scope of an international administrative assistance procedure in mid-2008. After losing its patience with the administrative assistance procedural formalities, the IRS decided to set a deadline whereby if the data was not released by 18 February 2009, it would initiate criminal proceedings against UBS in the US.

Confronted with this threat, the *FINMA* decided to order the release of the data prematurely and without awaiting the outcome of the administrative assistance requests, which had been under examination by the Swiss Federal Tax Administration (*FTA*) and against which appeals had been lodged with the Swiss Federal Administrative Court.

Struggling for the Swiss banking secrecy

FINMA's decision is seen by many as an illegal breach of Swiss banking secrecy. Swiss banking secrecy—often regarded as a key factor of success of the Swiss financial industry—is one of several professional privileges such as attorney-client privilege or doctor-patient confidentiality and relates to provisions of privacy, data protection and contract law. However, bank secrecy does not offer absolute discretion and may be overruled, *inter alia*, by decisions taken by the Federal Office of Justice in the course of an international judicial assistance procedure at the request of another state. Switzerland provides, under certain circumstances, international judicial assistance based on the Federal Act on International Judicial Assistance to any state as well as international administrative assistance based on mutual agreements such as for example a double taxation treaty (DTT).

Switzerland grants judicial and administrative assistance only if the alleged facts represent a criminal offence under Swiss law, whereas Swiss law distinguishes criminal offences from simple breaches. This distinction is based on the punishable degree of incriminated behaviour.

Swiss tax delinquency thus distinguishes between tax fraud (e.g. by use of falsified documents) and tax evasion (omission to declare assets or revenue). Both cases are regarded as delinquency, but since the use of falsified documents implies a higher degree of criminal motivation than the simple omission to declare assets or revenue, tax fraud is regarded as an offence and is consequently punished more severely than tax evasion. Accordingly, requests for international judicial assistance in tax matters are only approved if the alleged acts qualify as tax fraud. This practice is reflected in the limitation of international administrative assistance in tax matters to tax fraud and the like, as provided by Swiss DTTs.

During the course of the administrative judicial assistance, the FTA stated explicitly that setting up offshore companies does not represent tax fraud under Swiss law, but found that the legal qualification of the alleged actions in the specific context of the QI exceeded ordinary tax evasion. Therefore, the FTA decided that the present cases qualified for international administrative assistance. The premature interruption of the proceedings by the FINMA could therefore not only have proven to be unnecessary but also be regarded as an unjustified infringement of Swiss banking secrecy.

Since Switzerland is aware of the foreign perception of Swiss banking secrecy as abetting tax evasion, Switzerland introduced various measures against tax evasion without forcing Swiss banks to disclose data on their clients to any tax authorities and thus upholding bank secrecy:

- Switzerland levies a 35% withholding tax on savings interest, interest on bonds issued by Swiss residents, dividends from shares in Swiss companies and certain distributions of Swiss insurance products such as for example annuities. The withholding tax may be recovered to a certain extent, depending on the applicable DTT, if the revenues are declared to the taxpayer's state of residence.

- Switzerland concluded the Taxation on Savings Agreement with the EU, which obliges all Swiss distributors of interest and investment funds to retain a withholding tax at an increasing rate of up to 35% and forward 75% of the respective amount to the receiver's state of residence. This agreement allows banking secrecy to remain in force while making Switzerland unattractive for tax evasion committed by EU residents.

- By signing the bilateral agreements II (Schengen/Dublin), Switzerland agreed to offer international judicial assistance in cases of tax evasion relating to indirect taxes and duties (e.g. VAT or customs), if the evaded amount exceeds €25,000.

## Wealth Tax

### 1. Personal Wealth Tax

The Swiss Tax Conference (union of all cantonal tax authorities) announced that it would not apply the provision of the revised directive for the valuation of shares with no stock market value (as mentioned in CMS Tax Connect, November 2008), according to which the substance value of shares with no stock market value represents the minimal value of the shares. The Swiss Tax Conference intended to apply this rule from 2011 as a modification to the so-called practitioner's method presently in use for determining the value of shares with no stock market value. It reads as follows:

$(2 \times \text{capitalized earnings value} + \text{substance value})/3$ .

The abandoned amendment of the practitioner's method was highly controversial, since it would dramatically raise tax values of companies with low earnings and high substance value, which applies to many small and medium-sized Swiss enterprises.

## **2. Personal Income and Wealth Tax**

The population of the Canton of Zürich decided in a public vote held on 8 February 2009 to abolish the lump-sum taxation of foreign individuals who do not exercise any gainful activities in Switzerland. Lump-sum taxation is provided for by the Federal Act on Tax Harmonisation as an option (but not as an obligation) for the cantons to offer an alternative simplified regime of assessing the taxable income and wealth of foreign nationals residing in Switzerland.

Since a reliable assessment of the worldwide taxable income of individuals eligible for lump-sum taxation is often very difficult, their taxes are determined based on their living expenses instead. As a minimum, the assessment basis must be equal to at least five times the annual accommodation costs. In addition, some cantons also levy lump-sum taxes on wealth. The effective tax is calculated by applying ordinary tax rates.

Lump-sum taxation may result in considerable tax discounts for high net worth individuals, because it does not require taxpayers to declare all their worldwide assets and income. As a result, the Swiss lump-sum taxation is seen to encourage, on the one hand, international tax evasion and is consequently challenged, for example, by denying treaty benefits under certain circumstances to Swiss residents subject to lump-sum taxation (France, Belgium, Austria, Canada, Italy, Norway, USA and Germany). Lump-sum taxation has also raised, on the other hand, domestic criticism and is contested by political advances. The referendum in Zurich is likely to strengthen the ongoing political movement against the lump-sum taxation in other cantons. However, other cantons with a longer history of lump-sum agreements, especially in the French speaking parts of Switzerland, are less likely to follow the trend initiated by the Canton of Zürich.

### **David Hürlimann**

CMS von Erlach Henrici AG  
david.huerlimann@cms-veh.com

### **Basil Peyer**

CMS von Erlach Henrici AG  
basil.peyer@cms-veh.com



**United Kingdom**

‘ Taxation of foreign profits  
review ’

## Corporate tax

### 1. Taxation of Foreign Profits

The Government first started to talk to Business about the possible reform of the taxation of foreign profits in 2006, which resulted in a Budget announcement in March 2007 that the Government would consult on proposals to introduce a package of measures in this area. A discussion document was duly published in June 2007 (see Tax Connect, November 2007 for an outline of the original proposals).

The most controversial aspect of the discussion document concerned the proposals for the replacement of the existing controlled foreign companies (CFCs) regime with a new controlled companies regime. The new regime would move away from the current entity based approach towards a system under which specified types of income (i.e. passive income) would be taxed. However, certain income that might be regarded by Business as active was to be treated instead as passive. Of particular concern was income derived from the ownership of intellectual property and other intangible assets as part of normal trading.

We reported in the last issue of Tax Connect (November 2008) that the Government had listened to Business and had signalled that the controlled companies proposals may not be workable and the question was whether the whole package of proposals would have to be postponed until after the next election (which must be held by May 2010).

The Government answered this by announcing in its Pre-Budget Report that draft legislation would be published in December 2008 with a view to it becoming law in Finance Act 2009. The main proposals covered by the draft legislation deal with the introduction of the dividend exemption, a worldwide cap on the level of debt and the extension of the anti-avoidance unallowable purpose rules in relation to debt and derivatives contracts. The replacement of the Treasury consents regime (see Tax Connect, June 2007) by a reporting regime is included and is uncontroversial.

It is thought that the Government is keen to introduce the dividend exemption in the hope that it curbs the number of UK holding companies actively considering re-domiciling (so far most of the groups that have re-domiciled have chosen Ireland as their preferred location). The dividend exemption is the aspect of the proposals that has been most welcomed by Business as it will bring to an end the foreign tax credit regime.

Importantly, CFCs do not form part of the proposals. Instead, during this year the Government will carry out work in developing new CFC rules, which it is thought, are unlikely to become law until 2011. The absence of CFCs proposals must bring into doubt whether these measures will persuade companies considering moving their domicile to stay. The current CFC regime seems to be the principal motivation behind migration (indeed, Ireland has no CFC rules) as most companies have found a way of avoiding UK tax on foreign dividends (for example, where it would otherwise have been payable funds might be repatriated by way of loan or in a capital form).

In this article we look at the proposals on dividend exemption and the worldwide debt cap rules, which have now taken on the mantle of the most controversial aspect of the proposals.

## 2. Dividend exemption

The draft legislation is structured so as to tax all income dividends received by large and medium sized companies unless the dividend falls within one of the five specified categories of exemption. So as to ensure compliance with EU law, the rules apply to dividends from both UK resident and non-resident companies. Although the exempt categories of dividend might appear overly complex, the rules have been generally well received and acknowledged to be attractive compared with dividend exemptions available in other countries. For example, there is no minimum period that shares in the dividend paying company must be held and no general minimum size of shareholding required to qualify for exemption.

The five categories of exemption are expected to ensure exemption for most income distributions. Broadly, the following will be exempt:

- distributions from companies controlled by the recipient;
- distributions on non-redeemable ordinary shares;
- distributions on portfolio holdings (i.e. 10 % or less of the class of shares);
- dividends where the distributed profits are not derived from transactions that were designed to achieve a reduction in UK tax; and
- dividends on shares accounted for as liabilities.

It is only necessary for a distribution to fall within one of the categories for exemption to be available. All intra-group dividends should be exempt under the first category. The third category should ensure exemption for most dividends on portfolio holdings. However, exemption for distributions on preference and/or redeemable shareholdings over 10% but not more than 50% will only be available under category four if there is, broadly, no tax avoidance involved. HM Revenue and Customs (HMRC) is not intending to provide a clearance facility so that if exemption is dependent on this category careful consideration may need to be given to whether exemption will be available. It should also be noted that the legislation contains special provisions defining preference, redeemable and ordinary shares. There are also anti-avoidance rules but in general, these are targeted to counteract specific known tax avoidance.

In general, multinational groups repatriating cash to the UK should no longer need to rely on doing so through making loans to the UK (which is discouraged under the world-wide debt cap rules outlined below) or otherwise returning cash in the form of capital and making use of the substantial shareholding exemption for capital gains.

However, one disadvantage that may arise is where a dividend is paid subject to a withholding tax and there is a relevant double tax treaty that requires the dividend to be subject to tax in the recipient's country if it is to benefit from a reduced withholding. HMRC recognise that the UK has entered into a number of treaties with those provisions and has indicated that it is considering offering an "option to tax" (i.e. the recipient can opt to be taxed on the dividend). This is only likely to be of use where the underlying tax and full withholding tax exceeds the tax in the UK.

## 3. Worldwide debt cap

The UK already has rules that operate to restrict relief for intra-group finance expense where it exceeds that which would have arisen on an arm's length basis or there is a tax avoidance motive. The proposed new rules are in addition to the existing rules and are designed to introduce an element of objectivity in that even though the intra-group finance cost may be on an arm's length basis and no tax avoidance motive exists, relief may nevertheless still be denied to the extent that the UK intra-group finance expense exceeds a sum computed by reference to the group's worldwide external finance expense. Thin capitalisation and advance transfer pricing agreements that have been entered into will not give automatic protection from these new rules.

The rules are concerned only with the restriction of intra-group finance costs in the UK so that third party finance costs are not caught although there are anti-avoidance rules that apply where back-to-back and conduit arrangements are entered into so as give the appearance of third party finance.

Broadly, intra-group finance expense (identified from the tax computations) will be disallowed to the extent that it exceeds the net external finance expense for the worldwide group (identified from the consolidated profit and loss account). It should be noted that the intra-group finance expense is "gross" (i.e. any intra-group finance income is ignored) whereas external finance expense is the net amount (i.e. reduced by the amount of any finance income) and does not include UK external finance expense.

Finance expense is not restricted to intra-group interest. Net costs under derivative contracts taken out to hedge intra-group debt, intra-group finance leases of plant and machinery and intra-group debt factoring can also be restricted.

The basic thrust of the rules is such that to avoid disallowance of intra-group finance expense in the UK, non-UK external debt should be maximised and intra-group finance expense minimised. One effect is to encourage non-UK group companies to be funded by external debt rather than equity. It also means that an event within the group wholly unconnected to the UK can result in the disallowance of intra-group expense in the UK (for example, a reduction in non-UK borrowing following the sale of a foreign subsidiary). The rules also tend to encourage a UK operating company to borrow directly from a third party rather than indirectly through a group company.

HMRC hope to see multinational groups that have previously made upstream loans to repatriate funds to the UK (rather than making dividends) restructuring them in a way that involves dividends being paid up to the UK.

There has been considerable criticism levelled at the proposals and HMRC has indicated that it has been listening and expects significant changes to the proposals to be made before they become law. Among the unintended consequences or areas that HMRC is reviewing with a view to change include the following:

As the rules apply to pure UK groups as well as multinational groups (so as to comply with EU law), where external borrowing is made at the level of the parent and pushed down to the subsidiaries, the effect of the way in which the rules work in a UK context is to push the expense

back up to the parent. This is because although the subsidiary suffers a disallowance, the parent is entitled to a "corresponding adjustment" that operates to remove from tax the intra-group finance income on the loans pushed down to the subsidiaries. This leaves the external finance expense with the parent. Unless the expense can be surrendered to a subsidiary as group relief in that year, relief for the expense may be, in effect, lost as the parent is unlikely to have sufficient profits of the type that the carry forward finance expense can be set against.

Temporarily cash rich groups (e.g. through the disposal of subsidiary) could trigger a disallowance of UK intra-group finance expense as a result of a reduction in external finance. HMRC is working on provisions to relieve this (e.g. disregard certain cash inflows for 12 months). However, this will not help those groups that are cash rich (with little or no external finance) that have made intra-groups loans into the UK.

The draft rules include recognition of all gains/losses on finance including foreign exchange gains and losses, which can cause some unintended results. HMRC has indicated that foreign exchange may be taken out.

The introduction of so-called "gateway tests" that will mean groups that satisfy the tests will not need to apply the detailed rules. Work is still being carried out on the formulation of these tests. For example, the test may allow a group to assume that the rules do not apply if the level of intra-group debt is less than a specified % (say, 75%) of worldwide debt.

Currently, the computation of external finance is to be based on IFRS. It is likely that HMRC will compile a list of acceptable local GAAPs to reduce the need for computations to be made on an IFRS basis even though the relevant accounts are not drawn up on that basis.

Businesses (eg banking and insurance) where debt finance is an integral part of their trade (as opposed to providing capital for their business) will be subject to special rules. Broadly, interest income or expense arising from debt entered into as part of a banking or insurance trade will be excluded. In house UK treasury companies will be affected although this is an area that is under review.

It was originally thought that this package of measures would come into effect on 1 April 2009. It is not expected that this will now happen. The start date is still very much unclear and it is not expected that we will see revised draft legislation before the Budget that is scheduled for 22 April 2009.

Given that it is expected that the revised draft will be materially different from the first draft it is hoped

that the Government will delay the start date so that businesses have sufficient time to digest the new rules and consider their application to their individual businesses as well as carry out any restructuring.

**Mike Boutell**

CMS Cameron McKenna LLP  
mike.boutell@cms-cmck.com

# Contacts

## Algeria - Algiers

CMS Bureau Francis Lefebvre  
T +213 213 666 86  
F +213 213 666 86  
Samir Sayah  
samir.sayah@cms-bfl.com  
Frédéric Elbar  
frederic.elbar@cms-bfl.com

## Argentina - Buenos Aires

CMS Bureau Francis Lefebvre  
T +54 11 4311 1008  
F +54 11 4311 8088  
Patrick Patelin  
ppatelin@cms-bfl.com.ar

## Austria - Vienna

CMS Reich-Rohrwig Hainz  
T +43 1 40 443 0  
F +43 1 40 443 9000  
Johannes Reich-Rohrwig  
johannes.reich-rohrwig@cms-rrh.com  
Sibylle Novak  
sibylle.novak@cms-rrh.com

## Belgium - Brussels

CMS DeBacker  
T +32 2 743 69 00  
F +32 2 743 69 01  
Olivier Querinjean  
olivier.querinjean@cms-db.com

## Brazil - São Paulo

CMS Bureau Francis Lefebvre  
T +55 11 3069 9430  
F +55 11 3069 9432  
Patrick Patelin  
ppatelin@cms-bfl.com.ar

## Bulgaria - Sofia

CMS Cameron McKenna EOOD / CMS  
Reich-Rohrwig Hainz EOOD  
T +359 2 921 99 10 / 21  
F +359 2 921 99 19 / 29  
David Butts  
david.butts@cms-cmck.com  
Gentscho Pavlov  
gentscho.pavlov@cms-rrh.com

## China- Shanghai

CMS Bureau Francis Lefebvre and CMS  
Hasche Sigle in alliance with CMS  
Cameron McKenna LLP  
T +86 21 6289 6363  
F +86 21 6289 9696  
Emmanuel Meril  
emmanuel.meril@cms-bfl.com

## Croatia - Zagreb

CMS Cralic in alliance with CMS  
Reich-Rohrwig Hainz  
T +385 1 4825 600  
F +385 1 4825 601  
Gregor Famira  
gregor.famira@cmslegal.hr

## Czech Republic - Prague

CMS Cameron McKenna v.o.s.  
T +420 296 798 111  
F +420 221 098 000  
Libor Kadlec, External Tax Advisor  
kadlec@ccsconsulting.cz

## France - Paris

CMS Bureau Francis Lefebvre  
T +33 1 47 38 55 00  
F +33 1 47 38 55 55  
Stéphane Austry  
stephane.austry@cms-bfl.com

## Germany - Berlin

CMS Hasche Sigle  
T +49 30 2 03 60-1801  
F +49 30 2 03 60 2000  
Wolf-Georg von Rechenberg  
wolf-georg.vonrechenberg@cms-  
hs.com

## Germany - Düsseldorf

CMS Hasche Sigle  
T +49 211 49 34 0  
F +49 211 49 20 097  
Thomas May  
thomas.may@cms-hs.com

## Germany - Frankfurt

CMS Hasche Sigle  
T +49 69 71 701-0  
F +49 69 71 701 40410  
Thomas Link  
thomas.link@cms-hs.com

## Germany - Hamburg

CMS Hasche Sigle  
T +49 40 3 76 300  
F +49 40 3 76 30 300  
Heino Büsching  
heino.buesching@cms-hs.com

## Germany - Munich

CMS Hasche Sigle  
T +49 89 2 38 07 0  
F +49 89 2 38 07 110  
Gerd Seeliger  
gerd.seeliger@cms-hs.com

## Germany - Stuttgart

CMS Hasche Sigle  
T +49 711 97 64 0  
F +49 711 97 64 900  
Björn Demuth  
bjoern.demuth@cms-hs.com

## Hungary - Budapest

Ormai és Társai CMS Cameron  
McKenna LLP  
T +36 1 483 4800  
F +36 1 483 4801  
Eszter Kálmán  
eszter.kalman@cms-cmck.com

## Italy - Milan

CMS Adonnino Ascoli & Cavasola  
Scamoni  
T +39 02 4801 1171  
F +39 02 4801 2914  
Federico Baridon  
federico.baridon@cms-aacs.com

## Italy - Rome

CMS Adonnino Ascoli & Cavasola  
Scamoni  
T +39 06 47 81 53 06/05  
F +39 06 47 82 31 39  
Giuseppe Ascoli  
giuseppe.ascoli@cms-aacs.com  
Carlo Romano  
carlo.romano@cms-aacs.com

## Morocco - Casablanca

CMS Bureau Francis Lefebvre  
T +212 522 22 86 86  
F +212 522 48 14 78  
Wilfried Le Bihan  
wilfried.lebihan@cms-bfl.com  
Frédéric Elbar  
frederic.elbar@cms-bfl.com.com

## The Netherlands - Utrecht

CMS Derks Star Busmann  
T +31 30 2121 111  
F +31 30 2121 133  
Jochem de Koning  
jochem.dekoning@cms-dsb.com

## Poland - Warsaw

CMS Cameron McKenna Dariusz  
Greszta Spółka Komandytowa  
T +48 22 520 5555  
F +48 22 520 5556  
Arkadiusz Michaliszyn  
arkadiusz.michaliszyn@cms-cmck.com

▮ **Romania - Bucharest**

CMS Cameron McKenna SCA  
T +40 21 528 0 800  
F +40 21 528 0 900  
Delia Dragomir  
delia.dragomir@cms-cmck.com

▮ **Russia - Moscow**

CMS Legal  
T +7 495 739 33 44  
F +7 495 739 33 55  
Stanislav Tourbanov  
stanislav.tourbanov@cmslegal.ru

▮ **Serbia - Blegrade**

CMS Reich-Rohrwig Hasche Sigle  
d.o.o.  
T +381 11 32 08 900  
F +381 11 30 38 930  
Tanja Unguran  
tanja.unguran@cms-rrhs.com

▮ **Slovakia - Bratislava**

CMS Reich-Rohrwig Hainz Joint office  
with CMS Cameron McKenna in  
cooperation with JUDr. Jaroslav  
Ruzicka  
T +421 2 544 33 490  
F +421 2 544 35 906  
Robert Janecek  
robert.janecek@ccsconsulting.sk

▮ **Spain - Madrid**

CMS Albiñana & Suárez de Lezo  
T +34 91 451 93 00  
F +34 91 442 60 45  
Santiago Diez  
sdiez@cms-asl.com  
Ana Jimenez  
anjimenez@cms-asl.com

▮ **Switzerland - Zürich**

CMS von Erlach Henrici  
T +41 44 285 11 11  
F +41 44 285 11 22  
David Hürlimann  
david.huerlimann@cms-veh.com

▮ **Ukraine - Kyiv**

CMS Cameron McKenna LLC, Joint  
office with CMS Bureau Francis  
Lefebvre  
T. +380 44 391 3388  
F +380 44 391 3377  
Dmytro Ivanusa  
dmytro.ivanusa@cms-cmck.com

▮ **United Kingdom - London**

CMS Cameron McKenna LLP  
T +44 20 7367 3000  
F +44 20 7367 2000  
Mark Nichols  
mark.nichols@cms-cmck.com

▮ **United States of America  
New York**

CMS Bureau Francis Lefebvre  
T +33 1 47 38 44 10  
F +33 1 47 45 80 46  
Michel Collet  
michel.collet@cms-bfl.com

▮ **Uruguay - Montevideo**

CMS Bureau Francis Lefebvre  
T +598 2 623 4707  
F +598 2 628 7913  
Javier Bordaberry  
jbordaberry@cms-bfl.com.uy

CMS is the organisation of independent European law and tax firms of choice for organisations based in, or looking to move into, Europe. CMS provides a deep local understanding of legal, tax and business issues and delivers client-focused services through a joint strategy executed locally across 28 jurisdictions with 54 offices in Western and Central Europe and beyond. CMS was established in 1999 and today comprises nine CMS firms, employing over 2,400 lawyers and is headquartered in Frankfurt, Germany.

**CMS nine member firms are:** CMS Adonnino Ascoli & Cavasola Scamoni (Italy); CMS Albiñana & Suárez de Lezo, S.L.P. (Spain); CMS Bureau Francis Lefebvre (France); CMS Cameron McKenna LLP (UK); CMS DeBacker (Belgium); CMS Derks Star Busmann (Netherlands); CMS von Erlach Henrici Ltd. (Switzerland); CMS Hasche Sigle (Germany); and CMS Reich-Rohrwig Hainz (Austria).

CMS offices and associated offices:

**Amsterdam, Berlin, Brussels, London, Madrid, Paris, Rome, Vienna, Zurich,** Aberdeen, Algiers, Antwerp, Arnhem, Beijing, Belgrade, Bratislava,

Bristol, Bucharest, Budapest, Buenos Aires, Casablanca, Cologne, Dresden, Dusseldorf, Edinburgh, Frankfurt, Hamburg, Kyiv, Leipzig, Ljubljana, Lyon, Marbella, Milan, Montevideo,

Moscow, Munich, New York, Prague, Sao Paulo, Sarajevo, Seville, Shanghai, Sofia, Strasbourg, Stuttgart, Utrecht, Warsaw and Zagreb.

[www.cmslegal.com](http://www.cmslegal.com)

The members of CMS are in association with The Levant Lawyers with offices in Beirut, Abu Dhabi, Dubai and Kuwait-City.