



Business restructurings in the downturn: Austrian tax points

This briefing sets out the key Austrian tax issues in respect of business restructurings. In summary, they normally take the form of asset or share transactions. The transfer of a business, a merger or a demerger may be tax neutral or benefit from capital duty or stamp duty exemptions or reductions of real estate transfer tax under the Austrian Re-organisation Tax Act. The transfer of a business in exchange for other (debt) instruments is not eligible for special treatment under the Act; it is viewed as a sale. Furthermore, restructurings in cases where a fiscal unity exists, debt remains outstanding or a subsidiary is liquidated may have additional tax consequences. Companies will need to look carefully at their circumstances before taking action.

Introduction

This briefing is of a general nature and does not purport to present a complete picture of all Austrian tax issues that could be relevant to a specific business restructuring. It sets out in general terms some potentially relevant key Austrian tax points that may arise in business restructurings that are taking place because of the current economic climate. These restructurings could entail internal re-organisations in order to extinguish intra-group debt, sales of businesses to third parties in order to raise liquidities or even transfers of businesses to third parties in repayment of debt.

The 'downturn factor' does not lead to special rules being applicable. However, the focus on the relevant tax effects will change, as loss planning and liability issues become more prominent.

General

Business restructurings normally take the form of share or asset transactions. The principle is that combined transactions are split into separate steps, priced at fair market value. This means, for instance, that if debt is repaid through the transfer of a business (whether in the form of assets or shares) and the creditor accepts full repayment in exchange for (part of) the business, the difference between the fair market value of the business (shares) transferred and the principal amount of the debt released as a result of such transfer constitutes a profit that will lead to its own Austrian tax consequences.

Currently, tax losses can be carried forward without time limit. As a rule, loss carry-forwards can be set off against only 75 per cent of current annual income. However, excess losses can be carried forward to subsequent tax years. This 75 per cent limitation does not apply to losses and profits resulting from, among other things, the sale of businesses and partial business divisions. The Austrian tax regime does not provide for a carry-back of losses.

Rules intended to combat tax loss 'trafficking' may lead to the expiry of all available tax losses in cases of a change of control in connection with the termination of or a major reduction in business activities. Also, for certain holding, financing and portfolio investment activities, there may be baskets of taxable result that prevent compensation of profits by losses in another basket.

In fiscal unity situations, tax losses belong to the group's top company. When a tax group is established, a group member's losses resulting from periods before the formation of the tax group may be offset only against the subsequent taxable profits of this group member. The 75 per cent offset limit for loss carry-forwards does not apply to group members but does apply to the group parent. Unlike group members, though, the group parent may also offset losses resulting from periods before the formation of the tax group against the group's profits. In addition, it is possible to use the tax losses of foreign group members directly held by Austrian group members. The use of foreign tax losses is only a temporary benefit in Austria because they will be recaptured against foreign group member profits or when the foreign group member leaves the tax group.

Share transactions

Corporate income tax

A restructuring through the transfer of more than 10 per cent of shares in a foreign subsidiary that has existed for a minimum holding period of one year should normally be exempt from income tax on the capital gain because of the international participation exemption. This means that no taxable result (and therefore no loss) would be recognised. However, losses realised on the liquidation of the foreign subsidiary are tax deductible to the extent that they exceed the previous five years' tax-free dividends.

Although selling shares in operating foreign subsidiaries in most cases does not give rise to taxable profits or tax-deductible losses as a result of the application of the participation exemption, the alienation of substantial domestic shareholdings is not exempt from corporate income tax. This is because the national participation exemption (for dividends) does not extend to capital gains and liquidation proceeds.

The contribution of shares to a company and demergers of companies generally trigger recognition of gain or loss as if the relevant assets (eg shares) have been transferred, unless the transactions are covered by the Austrian Re-organisation Tax Act. This Act provides for a tax-neutral transfer of qualifying shareholdings (minimum of 25 per cent) in exchange for shares in the receiving company. No shares must be granted in certain situations – eg if the transferring company is the sole shareholder of the receiving company.

Restructurings that lead to changes of control over entities with tax losses may lead in certain situations (eg a substantial change of the shareholders, substantial change in the organisation or substantial change in the economic structure) to those losses no longer being available for compensation. However, the loss carry-forward is not lost if the change is made on the occasion of a re-organisation designed to save a substantial number of jobs. But loss carry-forwards may be lost in corporate re-organisations if the assets to which the losses relate materially no longer exist on the effective date of the re-organisation.

If the shares in a company that is a member of a fiscal unity under the Austrian group tax regime are

transferred, this group member leaves the group and will pay taxes on its own income in the future. However, as a rule the tax group will not be terminated unless the leaving group member is the last member of the group apart from its group parent. If a domestic group member leaves the group within the three-year minimum holding period (as a member of the tax group), tax losses of the leaving group member that were used within a tax group are subject to a loss recapture upon leaving the group. There is no time limit for loss recapture for foreign group companies.

Special rules apply if the group parent of a tax group is transferred by means of a merger, demerger or conversion to another non-group member. According to the view of the Austrian tax administration, such transactions will normally cause the dissolution of the tax group and the normal tax consequences of a termination of a tax group will apply. This view is disputed, however, in Austrian reports on the subject. Although a merger will normally cause the dissolution of the tax group according to the strict interpretation of the Austrian tax administration, the tax group may continue to exist in the event of a 'downstream-merger' of the group leader into an existing group member.

Transfer tax

Real estate transfer tax is levied at a standard rate of 3.5 per cent on legal and economic transfers of real estate in Austria; it also applies to the consolidation of shares in a company holding real estate in the hands of a single shareholder or the transfer of shares of such a company. This provision is applicable to both domestic and foreign companies if the company owns domestic real estate. In the event of a consolidation of shares into the hands of a sole shareholder, the tax base is three times the assessed value of the domestic real estate (*Einheitswert*). A reduced tax basis (twice the assessed value of domestic real estate) is available in cases of income tax-neutral share transactions under the special regime of the Austrian Re-organisation Tax Act.

Capital duty and stamp duty

An exemption from capital duty and stamp duty is available under the Austrian Re-organisation Tax Act if at least 25 per cent of the interest in the company is transferred in return for shares in the receiving company and the shares transferred have been held for more

than two years by the transferring entity. Generally, the transfer of shares should not trigger stamp duty anyway.

VAT

The transfer of shares is exempt from VAT under the Austrian VAT Act. Mergers, demergers and conversions effected under the Austrian Re-organisation Tax Act are also exempt from VAT.

Asset transactions

Corporate income tax

In an asset transaction, the transfer of a business will lead to the recognition of a taxable result on the difference between the fair market value and the carrying value, unless the beneficial rules of the Austrian Re-organisation Tax Act are available. These beneficial rules would be available only in the case of a transfer of a complete business (or an independent part thereof) in exchange for shares issued, provided the business remains subject to Austrian taxation and the acquirer records the business at the original carrying value.

The Austrian Re-organisation Tax Act provides for the ability to transfer loss carry-forwards from a transferor to a transferee if certain criteria are met. So in a case where the transferor has losses available, these losses may be transferred to the transferee if:

- the losses materially belong to assets that should be transferred;
- the assets exist on the appointed date;
- the assets to which the losses relate exist to a comparable extent as on the date of the creation of the losses; and
- the assets will be actually transferred to the transferee at the original carrying value.

Losses that cannot be transferred to the transferee because they do not relate to the assets transferred remain with the transferor and are available for compensation against the transferor's profits.

Transfer tax

The legal and economic transfer of real estate in Austria will trigger real estate transfer tax at a standard rate of 3.5 per cent. The tax base is three times the assessed value of the domestic real estate (*Einheitswert*). A reduced tax basis (twice the assessed value of domestic real estate) is

available if real estate forms part of an income tax-neutral transfer of a business under the special regime of the Austrian Re-organisation Tax Act.

Capital duty and stamp duty

An exemption from capital duty and stamp duty is available for asset transactions under the Austrian Re-organisation Tax Act if the transferred assets have been held for more than two years by the transferring entity.

VAT

No VAT is due in the case of transfer of a business or an independent part of it under the Austrian Re-organisation Tax Act. The alienation of a business outside the special regime of the Austrian Re-organisation Tax Act is subject to VAT.

Asset transactions in repayment of debt

Unlike in some jurisdictions the transfer of a business in exchange for (debt) instruments is not generally eligible for relief under the Austrian Re-organisation Tax Act; this is considered a sale.

A key issue in restructuring indebtedness is to establish whether, and to what extent, a debt instrument for tax purposes also qualifies as regular debt and whether the proposed restructuring could change that qualification. A related-party situation, in which an independent creditor would not have granted a loan under the same circumstances, leads for example to the denial of interest deduction for the debtor and, if interest is paid, may lead to dividend withholding tax being due. It could also lead to different tax treatment for the creditor.

If debt is still outstanding after a business restructuring and is subsequently waived, such partial or full waiver of the principal amount of a debt instrument (and/or accrued interest) will lead to a taxable profit for the third party debtor. If the creditor is related to the debtor and it can be shown that the waiver would not have been granted by an unrelated creditor (ie in principle the waiver is of a recoverable receivable), the amount waived would be considered for tax purposes an equity contribution (informal capital) and should not lead to profit recognition or the reduction of available tax losses for the debtor. However, to the extent that the waived receivable is not recoverable, the waiver made by a shareholder of the debtor leads to a taxable profit for the debtor.

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