



# Taxation of cross-border mergers and acquisitions

**Sweden**

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# Sweden

## Introduction

The Swedish tax environment for mergers and acquisitions (M&A) has changed fundamentally in recent years, and change is expected to continue. The government has introduced various tax laws and proposals to minimize possibilities for using tax havens to avoid taxation and to comply with developing European Union (EU) law.

This section explains how these changes are likely to affect approaches to M&A transactions. The balance of this report addresses three fundamental decisions facing a prospective purchaser:

- What should be acquired: the target's shares or its assets?
- What will the acquisition vehicle be?
- How should the acquisition vehicle be financed?

Of course, tax is only one part of transaction structuring. Company law governs the legal form of a transaction, and accounting issues are also highly relevant when selecting the optimal structure. These areas are outside the scope of this report, but some of the key points that arise when planning the steps in a transaction plan are summarized.

## Recent developments

The following summary of recent significant Swedish tax developments is based on tax legislation and proposals as at the end of December 2015.

### Swedish interest deduction limitation rules

Under the main rule, interest payments on loans from affiliated companies are not tax-deductible as of 1 January 2013.

The new rules cover all debt to affiliated companies, and there is no grandfathering provision, which means that all interest payments on such loans from 1 January 2013 are covered by the new rules. The rules set two limitations on interest deductibility; for more information about the limitation rules, see choice of acquisition funding.

## Review of the Swedish corporate tax system

The government is conducting a review of the Swedish corporate tax system. A June 2014 report that proposed revised rules for interest deduction was broadly criticized. This led to a revision of the proposal, and new amended rules on interest deductibility will likely result. The results are expected to be implemented at the beginning of 2017 at the earliest.

### Reduction in corporation tax

As of 1 January 2013, the corporate income tax was reduced to 22 percent (from 26.3 percent). The reduced tax rate applies to companies with financial years starting on or after 1 January 2013.

## Asset purchase or share purchase

An acquisition in Sweden is more often effected through a share purchase rather than a purchase of the company's assets because capital gains on the sale of shares may be tax-exempt.

However, the benefits of asset acquisitions for the purchaser should not be ignored, particularly given that purchased goodwill benefits from tax deduction. Some of the tax considerations relevant to each method are discussed below. The relative advantages are summarized at the end of the report.

### Purchase of assets

A purchase of assets usually results in an increase in the base cost of those assets for both gains tax and capital allowances purposes (i.e. step-up in value), although this increase is likely to be taxable to the seller. In addition, historical tax liabilities generally remain with the company and are not transferred with the assets.

### Purchase price

There are no statutory rules on how the purchase price should be allocated between the purchased assets, although it is recommended that the total consideration should be apportioned among the assets acquired to the greatest extent possible. The remaining part of the consideration that cannot be allocated is booked as goodwill for the acquirer.

Under certain circumstances, it is also possible to dispose of assets at tax-residual values, leading to no gain for the seller and no step-up in value for the purchaser. This could be useful in a pre-sale restructuring.

## Goodwill

Goodwill paid for a business (assets) may be depreciated. The rules for depreciation of goodwill are the same as those for machinery and equipment (see below).

## Depreciation

Most tangible and intangible assets may be depreciated for tax purposes under the same rules that apply to machinery and equipment. Two major exceptions are land and shares, which are non-depreciable.

The two main depreciation methods are the declining-balance method, where a maximum depreciation allowance of 30 percent of the aggregated book value is allowed, and the straight-line method, where assets are depreciated by 20 percent annually.

Buildings are depreciated straight-line by approximately 2 to 5 percent annually, depending on the building.

## Tax attributes

Tax attributes, such as tax losses, remain with the selling company and are not transferred with the assets.

## Value added tax

Generally, value added tax (VAT) is levied on all commercial supplies of goods or services made within Sweden, unless specifically exempt from VAT. The standard rate of VAT is 25 percent. Certain supplies are subject to reduced rates of 12 or 6 percent. Goods and services exported from Sweden are zero-rated (i.e. no output VAT is charged, but full input VAT is recoverable). VAT is levied on the supply of goods or services within a group. It is possible to register certain companies as a VAT group so that intragroup supplies are VAT-exempt.

Financial and insurance services are exempt from VAT (without input VAT recovery possibilities, except for VAT on costs relating to financial services supplied to a buyer outside the EU).

The transfer of assets belonging to a business is also VAT-exempt where the assets are transferred in conjunction with the transfer of an entire business or line of business liable for VAT. The purchaser must continue to run the business; otherwise the exemption is not applicable. Where the transfer is VAT-exempt, the purchaser assumes the obligations and entitlement to adjust input VAT on capital goods.

Where the exemption is not applicable to the transfer of assets, the purchaser of the assets has the right to recover input VAT, provided the purchase is for a business subject to VAT. Where input VAT exceeds output VAT in a VAT return, the tax authorities repay the excess.

Share transfers are always VAT-exempt.

Transfers of land and buildings also are always exempt from VAT. Where land or buildings are being sold, professional advice should be sought, as additional documentation requirements must be fulfilled.

Foreign companies not liable for VAT in Sweden may receive a refund of input VAT incurred in Sweden by submitting an application to the tax authorities in their country of establishment (companies based in the EU) or directly to the Swedish Tax Authority (non-EU-based companies).

Recent developments show that the Swedish Tax Agency is becoming more restrictive in its approach toward VAT recovery on transaction costs and holding structures. Acquisition structures and future divestments can be taken into consideration when determining possibilities to recover VAT on transaction costs at the time of acquisition. To mitigate VAT leakage, a careful examination of acquisition structures and post-closing activities is recommended.

## Transfer taxes

A stamp duty land tax is levied on transfers of real property. The duty, payable by the buyer, is 1.5 percent of the purchase price for individuals and 4.25 percent for corporate buyers. Stamp duty is not charged where shares are transferred in a company holding real property.

The stamp duty on transfers of real property between companies within a group may be deferred until the property in question is sold to an external party, the companies no longer belong to the same group, or one of the companies ceases to exist due to liquidation or bankruptcy. Hence, the purchaser should be aware of any deferred stamp duties within the target company or group because the acquisition or a later reorganization may crystallize any deferred stamp duty.

There is no stamp duty or transfer tax on security transactions, formations of companies and branches, or expansions of capital.

## Purchase of shares

The purchase of a target company's shares does not result in an increase in the base cost of that company's underlying assets. Hence, there is no step-up in the basis for tax depreciation purposes and the buyer cannot deduct the difference between the underlying net asset values and the consideration for the shares.

Transactions costs, such as advisory costs, associated with purchases of shares may only be tax-deductible where the deal is not closed.

Sales or transfers of shares are VAT-exempt. Input VAT on costs related to share purchases may be recoverable, provided certain conditions are met. Input VAT on costs related to share sales is currently not recoverable in Sweden.

## Tax indemnities and warranties

In a share acquisition, the purchaser is taking over the target company, together with all related liabilities, including contingent liabilities. Therefore, the purchaser normally requires more extensive indemnities and warranties than in the case of an asset deal. An alternative approach is to transfer the target's business to a newly formed subsidiary

with a view to the purchaser taking over a clean company. However, such pre-structuring transactions may result in taxable income for the seller.

With large and medium-sized negotiated acquisitions, it is common for the seller to open the books of the target company to the prospective purchaser for a due diligence review. A normal part of the due diligence process involves an in-depth review of the tax affairs of the potential target company by the purchaser's advisors.

Reassessment of final tax returns by the Swedish Tax Agency is possible until the end of the year following the assessment year. However, in the case of incorrect and/or omitted information in the tax returns, the period for reassessment is extended to 5 years.

### **Tax losses**

Under Swedish tax rules, tax losses may be carried forward indefinitely. Tax losses carried forward may be transferred with the company. However, following a change of control in a company (i.e. where another enterprise has obtained a decisive influence over the company), the right to deduct losses may be restricted. In this case, any tax loss carried forward from the year prior to the acquisition year exceeding 200 percent of the cost to acquire the decisive influence over the company may be forfeited (the so-called 'amount limitation rule').

Where equity injections (e.g. unconditional shareholder contributions and any proceeds from a rights issue) have been made during the year in which the change of ownership took place (up to the change of control) or in either of the 2 preceding years, the consideration must be reduced by the corresponding amount when calculating any surviving tax losses.

In addition to the amount limitation rule, any tax loss carry forward that survives the change of control is restricted in time for 5 years following the year in which the change of control took place. During this period, the acquired company may not offset those losses against profits in any company belonging to the buyer's group (the so-called 'offset restriction rule'). However, where the company itself generates a profit after the change of control, the company may offset its tax losses against those profits. No limitations apply to losses incurred in the year of acquisition or later years.

### **Transfer taxes**

There is no stamp duty or transfer tax on security transactions, formations of companies and branches, or expansions of capital.

### **Tax clearances**

It is not possible to obtain a clearance from the Swedish Tax Agency giving assurance that a potential target company has no tax arrears or that it is not involved in a tax dispute.

## **Choice of acquisition vehicle**

Several potential acquisition vehicles are available to a foreign purchaser, and tax factors often influence the choice. As noted, there is no capital duty on the introduction of new capital to a Swedish company or branch.

### **Local holding company**

Profits and losses within a Swedish group of companies may be equalized by means of group contributions. Group contributions may be made between a parent company and its subsidiaries where more than 90 percent of the share capital is owned for both the parent's and the subsidiary's entire financial year or since the subsidiary started to conduct business (qualifying period).

Group contributions can also be made between such subsidiaries, subject to certain other conditions. Group contributions are tax-deductible for the payer and taxable for the recipient.

Group contributions between Swedish subsidiaries of a foreign parent company are granted under Swedish law, provided the foreign company is situated in an EU country, Norway, Iceland or Liechtenstein.

### **Foreign parent company**

The foreign purchaser may choose to make the acquisition itself, perhaps to shelter its own taxable profits with the financing costs. This should not cause any tax problems in Sweden because the capital gains of non-residents disposing of Swedish shares are not taxed in Sweden.

The purchaser may also choose to buy the Swedish shares through a foreign holding company. Sweden has tax treaties with over 80 countries, including all industrialized and almost all important developing countries, and it is common for purchasers to review them for favorable withholding tax (WHT) clauses. Sweden levies WHT on dividends but not on interest or royalty payments. In practice, WHT is often eliminated under domestic rules or EU directives. Note that royalty payments may imply a Swedish permanent establishment for the receiver and, as such, be taxed at the statutory income tax rate of 22 percent. This WHT is often reduced or eliminated under a tax treaty.

### **Local branch**

As an alternative to the direct acquisition of the target's shares, a foreign purchaser may structure the acquisition through a Swedish branch. Sweden does not impose additional taxes on branch profits remitted to an overseas head office. A branch is subject to Swedish tax at the same standard corporate rate as a subsidiary, currently 22 percent. Although the choice of the legal form of an enterprise should be determined on a case-by-case basis, certain factors should

always be considered from a tax viewpoint. These factors include the following:

- Profits of a branch are currently taxed in Sweden (source country) as well as in the home country (the source country tax is normally credited against the home country tax unless an exemption applies). Profits of a subsidiary are taxed in Sweden only. Where profits are distributed by a subsidiary, the dividend taxation of the owner must be examined separately in each case.
- Tax is not withheld on branch profits in Sweden, but distributions from a Swedish subsidiary can be subject to WHT, which is often reduced or eliminated under Swedish law or a tax treaty.
- Subsidiaries and branches are not subject to net wealth tax.
- The disposal of a branch is taxed in Sweden, but the disposal of shares is not.
- Filing requirements are generally more extensive for subsidiaries than for branches.

## Joint venture

No special tax legislation applies to joint ventures.

## Choice of acquisition funding

A purchaser using a Swedish acquisition vehicle to carry out an acquisition for cash needs to decide whether to fund the vehicle with debt or equity.

## Debt

Interest on loans is normally deductible for the purpose of calculating the net profits from business activities and where the loan is taken out for the purpose of acquiring shares from an external party. The deduction is made on an accrual basis. Sweden has no thin capitalization rules. As of 1 January 2013, Sweden has new interest deduction rules, discussed below.

## Deductibility of interest

Broadly speaking, a company's accounting treatment of interest is followed for tax purposes. However, there are a number of situations in which deductibility of interest can be denied. Under Swedish transfer pricing regulations, an arm's length interest rate must be charged for intragroup debt. The Swedish transfer pricing regulations apply where the parties to an international transaction are related. In particular, deductibility can be partially denied where the interest rate charged by a foreign entity to a Swedish entity is higher than the arm's length interest. Where both parties to the transaction are Swedish entities, transfer pricing regulations are normally not relevant since group relief schemes can be applied where more than 90 percent of the capital is held the entire year (see group relief/consolidation).

Under Sweden's new interest deduction rules, as of 1 January 2013, tax deduction for interest payments on all loans from affiliated companies may be denied. An affiliated company is a company that, directly or indirectly, through ownership or otherwise, has a significant influence over the other company. Affiliated companies also exist when companies are primarily under joint management. The restriction also applies on back-to-back loans; that is, where the loan is routed through a third party, related or unrelated. There are two exemptions to this restriction of interest deduction:

1. One exemption applies where the beneficial owner within the community of interest is taxed on the interest income at a rate of at least 10 percent, and the debt arrangement has not been established primarily to obtain a significant tax benefit ('10 percent test'). Where the main purpose of the debt arrangement is to obtain a significant tax benefit, the interest is not deductible even though the corresponding interest income has been subject to 10 percent tax or more.
2. A second exemption applies where the beneficial owner is taxed on the interest income at a rate lower than 10 percent (i.e. not passing the 10 percent test) but it can be shown that the debt arrangement was established mainly for business purposes ('business purpose test'), the interest cost is still deductible. However, this possibility only applies where the beneficial owner of the interest is in the European Economic Area (EEA) or a country with which Sweden has a double tax treaty.

## Withholding tax on interest, dividend and royalty and methods to reduce or eliminate it

No WHT is imposed on interest payments from Sweden to a non-resident recipient, and there is no WHT or capital tax on repayment of debt.

Dividends paid from a Swedish company to a non-resident shareholder are generally subject to a WHT of 30 percent. However, many foreign companies are exempt from WHT under Swedish law. Dividends paid by a Swedish resident company to a foreign company on business-related shares are exempt from WHT. A foreign company is defined as a foreign legal entity subject to taxation in its country of residence similar to the taxation to which Swedish resident companies are subject — generally, where the foreign company is subject to a corporate tax rate of at least 10 percent to 12 percent on its profits calculated under Swedish tax rules. A foreign company covered by a tax treaty is always deemed to be a qualifying foreign company. The foreign company must also be deemed equivalent to a Swedish limited company, from both tax and civil law perspectives.

Unquoted shares are normally deemed to be business-related (and qualify for the exemption) where they constitute fixed

business assets. Quoted shares are deemed to be business-related where they:

- constitute fixed business assets of the non-resident company
- have been held by the non-resident company at the time of the dividend payment for at least 1 year
- represent at least 10 percent of the voting rights that have been held for at least 1 year in the resident company.

Where not exempt under Swedish rules, the WHT is normally reduced or waived under a tax treaty. Treaty reduction or exemption is normally given at the time of payment of the dividend (often subject to the filing of a form), but some treaties provide for a refund procedure.

Royalties paid from Sweden to a non-resident recipient are not subject to WHT. However, such income is deemed to be business profits derived through a permanent establishment in Sweden where the income is considered business income for the recipient. Thus, tax is levied on a net basis after a normal assessment procedure based on the recipient's tax return. In the course of the normal assessment procedure, treaty reduction or exemption is given on the application of the taxpayer in their tax return.

New WHT legislation took effect as of 1 January 2016. The amendments aimed to ensure Swedish legislation would comply with the revised EU Parent-Subsidiary Directive. The new rules include anti-hybrid measures linked to the tax treatment of the dividend payer. Income that otherwise would qualify under the participation exemption is no longer exempt if the dividend is tax-deductible to the payer.

The amendments also clarify that the Swedish general anti-avoidance rules (GAAR) within the WHT Act apply to any dividend within the scope of the EU Parent-Subsidiary Directive.

The purpose of the GAAR is to prevent the establishment of artificial arrangements in order to gain a tax benefit or exemption from WHT without valid commercial reasons reflecting economic reality. This applies to arrangements where the Swedish company is the dividend payer or recipient.

### **Checklist for debt funding**

The use of an external bank debt may avoid transfer pricing problems.

Further, in light of the restrictions on the deduction of interest expenses on all loans to an affiliated party, any debt structuring should be carefully monitored.

Claims and debts in foreign currency attributable to the business activities must be valued at the exchange rate prevailing on the balance sheet date. For companies,

exchange gains are fully taxable and losses are fully deductible. However, gains/losses are not taxable/deductible where hedge accounting is applied.

Waiver of third-party debt normally gives rise to taxable income for the borrower where the borrower is not considered insolvent. Waiver of external debt may also be considered as composition with creditors that will have an effect on any tax losses carried forward. Where considered a composition with creditors, any losses are forfeited up to the amount subject to composition.

### **Equity**

A feature of the Swedish tax system is that dividends and capital gains are tax-exempt in certain situations. Sweden has participation exemption rules for dividends and capital gains on shares held by companies for business purposes.

Dividends and capital gains on business-related shares can be received tax-exempt. All non-quoted shares in certain domestic companies (i.e. Swedish limited companies) or corresponding foreign companies are deemed to be business-related. Quoted shares are deemed to be business-related where these conditions are met:

- The owner holds at least 10 percent of the votes, or the shares are otherwise necessary for the business conducted by the shareholder or any of its affiliates.
- The shares are held for at least 1 year.

A Swedish limited liability company may issue different classes of shares, such as preferential rights to profit distribution, which should be considered when capitalizing a company. All classes of shares are subject to the same tax treatment.

In Sweden, tax-neutral mergers are available under certain conditions. Where these conditions are met, a so-called 'qualifying merger' is achieved. In this case, assets and liabilities together with all related rights and obligations are transferred from the transferring company to the receiving company and recorded in the books of the receiving company at the same taxable values as they had in the transferring company. Thus, no gain is recognized on the assets transferred. As no capital gain tax is triggered for the transferring company, no step-up in values is available for the receiving company.

### **Hybrids**

Convertible debentures can be an alternative method of raising capital. The convertible debentures may be converted into shares at the option of the holder within a certain period. Convertible debentures are treated as debt until converted into shares, so any interest paid is deductible under applicable rules. Once converted into shares, any distribution paid out is treated as a non-deductible dividend. The conversion does not give rise to any tax consequences. Restrictions on the use of hybrids in Sweden are expected in the future.

## Deferred settlement

An acquisition often involves an element of deferred consideration, the amount of which can only be determined at a later date on the basis of the business's post-acquisition performance. The tax treatment of deferred considerations normally follows the accounting treatment.

## Other considerations

### Concerns of the seller

A total closing-down sale involving all the assets of a company normally constitutes the last transaction of business activity. Accordingly, hidden reserves in various assets, including untaxed reserves, are dissolved and subjected to tax. Where hidden reserves exist, the inevitable consequence for the seller is a tax burden that the company cannot postpone.

The tax consequences arising on selling all the assets of a business carried on in corporate form can be divided into two stages:

- sale of the assets
- transfer of the remaining after-tax capital to the owner.

Normally, when all the assets of a company are sold, the entire gain is taxed. Where the company has unused tax losses, these losses may be used to reduce the taxable profits. Any remaining profits are taxed as business income at the corporate tax rate.

The stamp tax on the transfer of real property is payable by the buyer and is normally not a concern for the seller.

After the transaction is completed, the remaining capital may be distributed to the owner of the company by means of dividends, liquidation or sale of the shares.

Dividends paid to a parent company by its subsidiary are normally tax-exempt where the shares were deemed business-related.

Capital gains on business-related shares are tax-exempt. However, capital gains on other non-business-related shares are taxed at the normal corporate rate on the difference between the consideration received and the tax basis of the shares. No indexation allowance is granted.

Capital losses on business-related shares are non-deductible. Capital losses on other shares can be offset against capital gains on corresponding shares. The latter losses are also deductible against capital gains on corresponding shares within a group where tax-deductible group contributions are possible. Remaining capital losses may be carried forward indefinitely.

A foreign corporate seller is normally not taxed in Sweden on the sale of shares in a Swedish limited company.

When shares are sold, the seller cannot take advantage of unused tax losses from earlier years in the sold company. The buyer also normally finds it difficult to use such losses in the first 5 years after the acquisition.

The Swedish legislation contains rules on special taxation when disposing of shares in shell companies. A company is regarded as a shell company where the total amount of the liquid assets exceeds one-half of the consideration paid for all the shares. Where a company (Swedish limited company) disposes of shares in a shell company, the taxable amount is the consideration paid for the shares. To avoid taxation on the sale of shares in a shell company, the seller needs to prepare a special tax return and file it with the tax authorities within 60 days of the disposal. Where the company disposed of is a foreign company, shell company taxation may only arise where the foreign company is liable to tax in Sweden at the time of the disposal of its shares or where the foreign company holds a share, directly or indirectly, in a non-quoted Swedish limited company or Swedish economic association.

### Company law and accounting

The Companies Act prescribes how Swedish companies may be formed, operated, reorganized and dissolved. The tax law mostly complies with the Companies Act. Domestic mergers are common in Sweden, and both tax and civil law include rules for handling EEA cross-border mergers in line with developments within the EU. A Swedish merger is an amalgamation, as described below.

Amalgamation is a special form of merger in which two or more companies amalgamate into a single entity, which then holds all the property and rights and is subject to the same liabilities as the previous companies. The Companies Act differentiates between three forms of amalgamation:

1. absorption generally
2. combination
3. absorption of a wholly owned subsidiary.

In all forms of amalgamation, one limited company (the transferor) — or in a combination, several limited companies — assigns all its assets and liabilities to another limited company (the transferee), after which the transferor is dissolved without formal liquidation. Absorption of a subsidiary is the most common form of amalgamation in Sweden and is usually the last step in a takeover in which the acquirer does not wish the acquired company to continue as a separate entity. Where a parent company holds more than 90 percent of both the capital and voting power in a subsidiary, a compulsory purchase of the remaining shares is possible. This is also the easiest form of merger from administrative and merger accounting perspectives. Merger accounting is generally complex in Sweden.

It is also possible under the Companies Act to carry out a demerger of a company.

A demerger can take place in two ways:

- A limited company is divided into two or more limited companies.
- Some of a limited company's assets are transferred to one or more other limited companies (partial demerger).

In the first situation, one limited company (the transferor) assigns all its assets and liabilities to two or more limited companies (the transferees), after which the transferor is dissolved without formal liquidation. The second situation implies that some of a transferor's assets and liabilities are assigned to one or several other limited companies without the transferor being dissolved.

Another important feature of Swedish company law concerns the ability to pay dividends. Distributions of profit may be made only out of a company's audited unrestricted equity. A formal decision is made at the annual general meeting (or extraordinary general meeting) to distribute. Where all unrestricted equity has been distributed, the next dividend can first be made when the next year-end accounts have been audited. Hence, interim dividends are not possible.

Finally, a common issue on transaction structuring involves the provisions concerning financial assistance. Briefly, these provisions make it illegal for a target company to give financial assistance, directly or indirectly, for the purpose of acquiring that company's shares.

### **Group relief/consolidation**

Sweden does not have tax consolidation. However, the law allows for the transfer of profit within an affiliated Swedish group through group contributions. In the case of a qualifying group contribution, the company making the contribution deducts the amount from its taxable income and the recipient company includes the contribution as taxable income for the same financial year.

A profit-making company can also make a group contribution to another profit-making company, thereby pooling taxable profits in one company.

Companies giving and receiving contributions must fully disclose the contributions in their tax returns for the same year. There is no requirement that the group contributions must be paid in cash; it is sufficient that the companies involved book the contribution in the accounts as a claim or receivable. However, it is important to recognize the transfer of value in the books.

The main condition for an allowable group contribution is that the parent holds more than 90 percent of the shares of the subsidiary for both the parent's and the subsidiary's

entire financial year or since the subsidiary started to conduct business (qualifying period).

### **Transfer pricing**

Where the acquisition is financed by intragroup debt, the interest should be set at arm's length. However, this should not apply between Swedish companies that can tax-consolidate. Failure to comply with the arm's length principle could result in transfer pricing adjustments in the relevant jurisdiction. However, where an adjustment is imposed on a company in one jurisdiction, the counterparty should be able to request a corresponding adjustment under the mutual agreement clause in a tax treaty or the EU Arbitration Convention, where applicable.

On 22 December 2015, the Swedish Tax Agency commented on the report issued by the Organization for Economic Co-operation and Development (OECD) under its Action Plan on Base Erosion and Profit Shifting (BEPS) entitled *Aligning Transfer Pricing Outcomes with Value Creation*. The Swedish Taxation Agency declared the report merely clarifies the arm's length principle, so the report's guidance will directly and retroactively effect the interpretation of the arm's length principle in Sweden. Some of the guidance may have implications for the transfer pricing aspects of cross-border M&As. In particular, funding activities undertaken by so-called 'low-functioning entities' (entities lacking the substance to control the financing risk) may be under scrutiny in the future. According to the BEPS report, these entities would be entitled to no more than a risk-free return on their funding activities.

### **Foreign investments of a local target company**

Sweden introduced controlled foreign company (CFC) rules on 1 January 2004. A legal entity liable to tax in Sweden that holds, directly or indirectly, at least 25 percent of the capital or voting rights in a foreign legal entity at the end of the taxable entity's financial year is subject to CFC taxation, where the foreign legal entity is deemed low-taxed. The foreign legal entity is deemed low-taxed where its income is not taxed or is taxed at a tax rate below 12.1 percent. This tax rate is computed on the net income calculated using Swedish tax rules.

Legal entities resident in certain areas or countries mentioned in a white list are deemed not to be CFCs. Those legal entities do not have to fulfill the criterion of being taxed at a rate of at least 12.1 percent. However, certain activities in some areas/countries are not covered by the white list, such as banking, financing, other financial activities and insurance. Any activities of this kind excluded from the white list in areas or countries within the EEA are excluded only where conducted intragroup.

In 2008, Sweden eased the CFC rules slightly and excluded companies within the EEA, even where low-taxed, provided substance can be proved.

## Comparison of asset and share purchases

### Advantages of asset purchases

- The goodwill element in the purchase price can be depreciated or amortized for tax purposes.
- A step-up in the cost-base for capital gains tax purposes is obtained for certain fixed assets.
- No previous liabilities of the company are inherited.
- Possible to acquire only part of a business.
- Greater flexibility in funding options.
- Profitable operations can be absorbed by loss companies in the acquirer's group, thereby effectively gaining the ability to use the losses.

### Disadvantages of asset purchases

- Possible need to renegotiate various types of external agreements.
- A higher capital outlay is usually involved (unless debts of the business are also assumed).
- May be unattractive to the seller, especially where a share sale would be tax-exempt, thereby increasing the price.
- 4.25 percent transfer tax applies where real property is included (corporations).
- Benefit of any losses incurred by the target company remains with the seller.

### Advantages of share purchases

- Likely more attractive to the seller, especially where a share sale would be tax-exempt. May benefit from tax losses of the target company (but there are many exceptions).
- May gain benefit of existing external contracts.
- No capital or transfer duties payable on net assets acquired (where the assets consist of real property).

### Disadvantages of share purchases

- Liable for any claims or previous liabilities of the entity.
- No deduction for the goodwill element in the purchase price.
- Losses incurred by any companies in the acquirer's group in years prior to the acquisition of the target can only be offset against any profits made by the target company after 5 years.



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