

ALLEN & OVERY



Global Tax practice

Inbound acquisitions at a glance

Update 2014

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Introduction

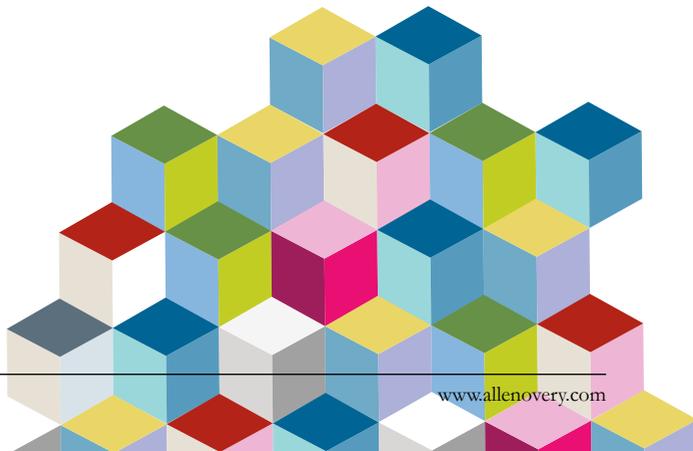
We are delighted to provide you the third edition of our “Inbound acquisitions at a glance” brochure.

In today’s increasingly complex business environment, awareness of the tax environment in relevant jurisdictions is crucial, especially when it comes to acquisitions of foreign companies. Local tax requirements such as the preservation of tax losses, the deductibility of acquisition costs and the taxation of dividends and capital gains are usually decisive factors in the successful structuring of such transactions.

Members of our Global Tax practice have updated our concise overview of the most relevant tax considerations for inbound acquisitions in jurisdictions such as Australia, France, Germany, Italy, Spain, the United Kingdom, the United States, Benelux and important Eastern European countries. For each jurisdiction, our local tax experts not only outline the respective transaction taxes (stamp and capital duties, if any, real estate transfer taxes, capital gains tax, etc) but also share the key knowledge that will enable you to structure inbound acquisitions in the most tax-efficient way.

We hope you find this brochure useful as a general guide to prospective acquisitions in the markets described. It goes without saying that every transaction requires tailor-made advice. Your usual Allen & Overy contact and our local tax experts would be more than happy to assist and support you in the structuring of any type of business transaction. Contact details may be found in this brochure.

Gottfried Breuninger
Global Head of Tax



Australia

Transaction taxes

In this section we identify taxes that will be imposed on the vendor and the acquirer upon a transfer of assets or upon a transfer of shares, as well as other tax implications of a transfer of assets or shares.

STAMP DUTY ON THE TRANSFER OF SHARES AND UNITS

0.6% stamp duty on transfers of shares that are registered in New South Wales or South Australia. In addition, land-rich or landholder duty can apply at rates of up to 6.75% if the company or unit trust either directly or indirectly owns land in Australia (the thresholds vary between the States and Territories but are ordinarily around AUD2m). Certain exemptions and concessions may be available, including corporate reconstruction relief for transactions between members of the same 90% or more owned group.

CAPITAL DUTY PAID ON THE CONTRIBUTION OF CAPITAL

Nil.

REAL ESTATE TRANSFER TAX

Stamp duty of up to **6.75%** is charged on the higher of the consideration paid or payable, and the unencumbered market value of the land transferred. As for share transfers, certain exemptions and concessions may be available, including corporate reconstruction relief for transactions between members of the same 90% or more owned group.

OVERVIEW OF AUSTRALIAN TAXATION OF RESIDENTS AND NON-RESIDENTS

Key issues: residence and source.

Residents:

- Australia taxes residents on income and capital gains from all sources.
- Worldwide taxation, with participation exemption system for certain foreign gains and dividends and credits for certain foreign taxes paid.

Non-residents:

- Generally only taxed on income sourced in Australia and capital gains in relation to “Taxable Australian Property”.

Taxable Australian Property broadly means:

- direct and indirect interests in Australian real property (eg land, lease of land and mining, quarrying and prospecting rights); and
- assets used in carrying on business in Australia through a permanent establishment.

It will also depend on whether resident of a country that has entered into a Double Tax Agreement (**DTA**) with Australia. The Australian Tax Office (**ATO**) has recently indicated that it will closely examine cases of Treaty Shopping.

As a result, it is important for non-residents to determine whether they hold an asset connected with an investment into Australia on **revenue** or **capital** account, and if held on revenue account, what the **source** of any gain is.

REVENUE VERSUS CAPITAL DISTINCTION

Whether an asset is held on revenue or capital account will depend on the facts and circumstances of the particular case and each case should be determined on its own merits.

For example, a share trader who buys shares with the intention of selling at a profit is generally treated as holding the shares on revenue account (ie profit-making intention) whereas an investor who buys shares with the intention of holding the shares long-term and deriving dividend income will generally be treated as holding the shares on capital account (ie any gain is from the mere realisation of a capital asset).

CAPITAL GAINS TAX ON THE SALE OF ASSETS HELD ON CAPITAL ACCOUNT (AUSTRALIAN VENDORS)

Corporate vendor – Capital gains are generally subject to tax at the corporate rate of 30%. Capital losses can only be utilised against capital gains (and not other income). In certain cases, the gain may be exempt if it relates to carrying on active business through a foreign permanent establishment. Discount capital gains tax treatment is not available to companies.

Industrial vendor – The net amount of capital gains (after applying capital losses) is added to other items of assessable income and tax is imposed at marginal rates (max rate is currently 46.5%). Capital gain may be eligible for 50% discount if underlying asset was held for at least 12 months. Important for individuals to determine whether held on revenue or capital account and ATO (revenue authority) applies strict capital versus revenue account test.

Trustee vendor – The net amount of capital gains (after applying capital losses) is added to other items of assessable income of the Trust. Trusts are generally transparent and beneficiaries are taxed at their marginal rates on their share of the assessable income of the Trust (certain trusts, eg trading trusts, may be taxed as companies). Certain beneficiaries may be entitled to discount capital gains tax treatment in relation to capital gains allocated to them if underlying asset was held for at least 12 months by the Trustee (discount is 50% for individuals and 33.3% for superannuation funds). Subject to certain conditions, non-Australian resident beneficiaries may be exempt from capital gains tax if the asset is not Taxable Australian Property (see discussion above) or the capital gain is not attributable to sources in Australia. Certain Managed Investment Trusts (**MITs**) can make an irrevocable election to treat eligible assets on capital account.

CAPITAL GAINS TAX ON THE SALE OF SHARES HELD ON CAPITAL ACCOUNT (AUSTRALIAN VENDORS)

Corporate vendor – Same as above for the sale of assets. A capital gain in relation to shares in foreign resident companies carrying on active businesses can be reduced in certain cases, subject to certain requirements (such as holding period rules).

Individual vendor – As above for the sale of assets.

Trustee vendor – As above for the sale of assets.

DEFERRAL OF CAPITAL GAINS TAX

Transfers within a tax consolidated group are ignored.

Rollover relief may be available for:

- certain scrip for scrip transactions and demerger transactions;
- transfers between onshore and offshore members of wholly owned groups; and
- certain group restructures, eg top-hatting.

PRESERVATION OF TAX LOSS CARRIED FORWARD

Revenue losses can generally be carried forward (but not back under current law) indefinitely subject to satisfying either a continuity of majority ownership test (greater than 50%) or same business test. Capital losses can also be carried forward indefinitely on a similar basis; however they can only be offset against capital gains (not other income).

Losses of one member of a tax consolidated group can be used by another member. Special rules apply to losses of a company when it transfers into a tax consolidated group to limit the utilisation rate.

NON-AUSTRALIAN VENDOR

A non-Australian resident vendor should not be subject to Australian tax on any capital gains arising from the sale of shares in an Australian company, whereas the sale by an Australian subsidiary of its business/assets may result in an Australian tax liability on any gains. However, the exemption from capital gains tax liability in relation to the sale of shares may not be available where:

- the Australian subsidiary directly or indirectly invests in Australian real property or the shares are connected with an Australian permanent establishment (see above in relation to Taxable Australian Property); or
- the shares are held on revenue account by the Vendor. Issues to consider in these circumstances are: the source of the gain (Australian versus foreign); the terms of any applicable DTA (business profits article and whether connected with a PE in Australia); and possible application of anti-avoidance rules if structured to obtain a tax benefit (eg treaty shopping or structuring source of gain to be foreign).

There are proposals for a non-final withholding tax to apply to the disposal proceeds of taxable Australian property.

VALUE ADDED TAX/GOODS AND SERVICES TAX

Goods and Services Tax (**GST**) may be charged on a supply of goods or services at a flat rate of 10%. Under the GST legislation, GST is the liability of the supplier but is ordinarily passed on to the recipient. Supplies of business assets (other than certain residential accommodation) will generally attract GST whereas supplies of shares and other securities will not. Where GST applies, the supply may qualify for GST-free treatment including supplies made offshore, or as part of a going concern.

Opportunities and threats

In this section an overview is provided of opportunities to maximise relief for acquisition costs (such as financing costs), as well as other items which require attention when designing an efficient tax structure.

STEPPING-UP ASSET VALUES

- Asset Purchase: The allocated portion of the purchase price of assets can be treated, as the case may be, as the basis for depreciation (capital allowances) and/or the cost base of the asset for determining the amount of any capital gain. If the sale price is not allocated to assets in the sale contract, then a reasonable apportionment based on market values will be required.
- Amortisation of goodwill is generally not deductible. Depreciation/capital allowances may be available for some intangible assets. Goodwill is generally treated as a separate asset for capital gains tax purposes.
- The cost of certain assets (eg work in progress) may be deductible immediately.
- Care should be taken with the treatment of debtors as deductions may not be available for debts that subsequently go bad.
- Share Purchase: Generally, there is no step-up in the cost of the assets of a stand-alone target company; nor is there an increase in any depreciation on allowances available to the stand-alone target company.

However, if the target company becomes a member of the purchaser's tax consolidated group, then there are detailed rules that apply to allocating the purchase consideration to the underlying assets of the target company.

TAX CONSOLIDATION RULES

Wholly owned groups (including multinationals with a number of entry points into Australia) can elect to form a tax consolidated group. In effect, all members of the group are treated as a “single entity” (ie as a part of the head company) for tax purposes and intra-group transactions are ignored. All members are jointly and severally liable for group tax debts if the head company defaults. Care should be taken by purchasers who acquire a subsidiary from a consolidated group, to ensure that the purchaser does not inadvertently become liable for tax liabilities of the target’s former tax consolidated group. Generally, this will require a purchaser to review the tax sharing agreement (**TSA**) and tax funding agreement (**TFA**) of the target’s tax consolidated group and obtain an appropriate release for the target upon payment of an exit amount.

DEBT/EQUITY RULES

Generally, the debt/equity rules determine the classification of an instrument as either debt or equity for tax purposes and whether payments/distributions are deductible (Debt: deductible; Equity: non-deductible, but may be frankable (carry imputation credits)).

Generally, an instrument is classified as debt if there is an “effectively non-contingent obligation” to repay an amount equal to the issue price (nominal amounts used if term is less than ten years, otherwise values calculated in present value terms). An instrument may be treated as equity if returns are discretionary or contingent on economic performance or it is convertible into equity.

The debt/equity rules may provide opportunities for tax-efficient cross-border financing structures.

THIN CAPITALISATION RULES

Interest and other debt deductions are subject to the entity not being thinly capitalised. Rules depend on the type of entity (eg Bank, FI, corporate) and whether it is inward or outward investing. Applies to all debt and not just related party debt. Some of the gearing levels available are:

Safe Harbour Tests:

- Default position: 3:1 debt-to-equity ratio (currently proposed to be changed to 1.5:1)
- Financial Entities: gearing ratio of up to 20:1 available (currently proposed to be changed to 15:1)
- Banks: Safe Harbour Capital Amount of at least 4% of Australian risk weighted assets (currently proposed to be changed to 6%)

Arm’s Length Test:

Notional calculation of the maximum arm’s length debt funding that could have been received or, for a bank, an arm’s length capital amount.

DISALLOWED AND DEFERRED INTEREST (OTHER THAN DEBT/EQUITY RULES)

Deductibility of interest may be limited/denied in the following circumstances:

- For returns paid on an equity interest (see above).
- The application of the thin capitalisation provisions (see above).
- Interest withholding tax is not remitted to the ATO.
- Where transactions are not on arm's length terms, with related and unrelated parties (ie transfer pricing rules).
- Where interest is incurred for non-income producing purposes, or in deriving capital gains or in deriving exempt income (although some debt deductions incurred in deriving foreign dividend income that is exempt under the participation exemption may be deductible under current law).
- Under various anti-avoidance rules, including Part IVA.

We also note that deferred interest securities (eg zero coupon bonds) may be subject to special timing rules for deductions (see below).

CONSEQUENCES OF GUARANTEES FROM A RELATED PARTY FOR THIRD PARTY DEBTS

The Thin Capitalisation rules apply to all debt, related party and third party debt (ie third party debt is relevant regardless of whether or not there is a related party guarantee).

It may also be necessary to consider the Transfer Pricing rules where the loan would not have been made at all to the borrower or exceeds the amount which would have been lent in the absence of the guarantee.

Depending on the terms of the loan agreement and guarantee, and any applicable DTA, the amount of any guarantee fee paid by/to a non-resident may be subject to a special type of withholding tax.

If interest payments are subject to interest withholding tax, then a payment by the guarantor in relation to defaulted interest may also be subject to withholding tax.

HYBRID LOANS

Loans with certain equity features may be classified as equity for tax purposes resulting in the denial of interest deductions and the possible need to frank distributions (attach imputation credits).

Legal form equity (that is not classified as tax debt) is used for most of the grouping tests, such as the tax consolidation provisions. Legal form debt that is classified as equity for tax purposes would not generally cause degrouping.

TAX CREDIT OR EXEMPTION TO AVOID DOUBLE TAXATION

Foreign Income – Participation exemption or credit

Australia typically applies an exemption method for “active” (immobile) income, including gains on sale of shares and dividends and a credit method for “passive” (mobile) income.

Where foreign tax has been paid on the foreign income, foreign tax credits may be available and are limited to the Australian tax payable on foreign income (with no refund for excess credits and no carry-forward).

To the extent that Australia’s participation exemption applies to gains on shares in foreign companies and/or dividends received from foreign companies, the conduit provisions should generally ensure that such gains pass through Australia with no additional income tax or withholding tax.

Australian Income – Full Imputation system

Aim is to prevent the economic double taxation in Australia of company profits. Australian tax at the company level is imputed to shareholders. Dividends paid out of Australian taxed company profits are generally “franked dividends” and dividends paid out of untaxed company profits are generally “unfranked dividends”. Franked dividends are generally exempt from withholding tax (see below). Franking credits are subject to a number of anti-avoidance rules.

TAXATION OF DISTRIBUTIONS RECEIVED BY AUSTRALIAN COMPANY FROM SUBSIDIARIES

- Dividends received from a subsidiary that is a member of the same tax consolidated group: ignored.
- Franked Dividends: included in taxable income but franking credits offset against tax liability and no tax should be payable.
- Unfranked Dividends: fully taxable.
- Foreign Dividends: participation exemption or credit for foreign tax may be available (see above).

CONTROLLED FOREIGN COMPANY LEGISLATION

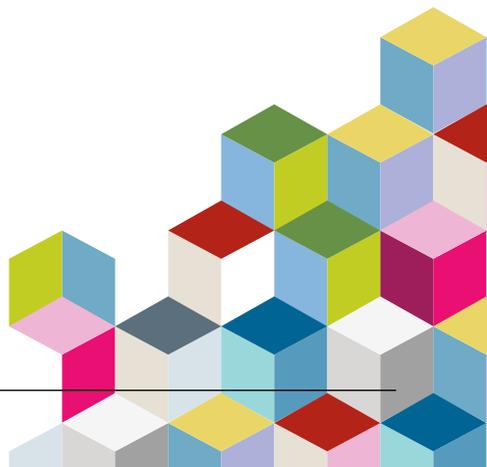
The Australian-controlled foreign companies (**CFC**) rules can cause a proportion of the undistributed profits of an Australian-controlled, foreign resident company to be attributed and taxed directly to the Australian resident holders. The rules are undergoing review and revision. Exemptions apply for active income, while credits are available for foreign income tax paid by the CFC.

TRANSFER PRICING/ANTI-AVOIDANCE RULES

The arm's length principle is included in Australian tax legislation and applies to all cross-border, and some domestic transactions and regardless of whether the parties are related or unrelated.

The General Anti-Avoidance Rule (**GAAR**) in Part IVA has wide application and can apply to a scheme where the "dominant" purpose of the scheme was to obtain a tax benefit. Tax benefits can include: amount not included in assessable income which otherwise would have been; a deduction that would not have been otherwise allowable; claiming a foreign tax credit; and avoiding withholding tax where it would have otherwise been payable. Part IVA can also apply to franking credit schemes.

Value shifting rules can also apply where value is directly or indirectly shifted between entities through transactions that are not otherwise taxable (eg share value dilutions), which recognise notional transactions.



RESIDENCE

A company is a resident of Australia for tax purposes if:

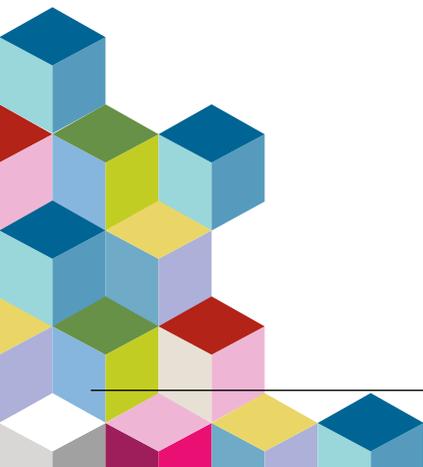
- it is incorporated in Australia; or
- it carries on business in Australia and has either:
 - its central management and control in Australia; or
 - voting power controlled by residents of Australia.

A subsidiary company that is incorporated in Australia will generally be treated as a resident of Australia for Australian income tax purposes.

If a non-resident company conducts business in Australia through an Australian branch, then income connected with the branch will generally be taxed in Australia on a similar basis to the principles applying to an Australian resident company (with certain modifications).

Where the place of effective management is located in a treaty jurisdiction and the tie breaker in the DTA gives tax residence to that other jurisdiction based on the place of effective management, Australia will continue to treat the company as an Australian tax resident and tax it based on its worldwide income subject to the terms of the applicable DTA, participation exemption for some gains and dividends and credit for some foreign taxes (see above in relation to participation exemption and credit for foreign taxes).

There are also some integrity measures and anti-avoidance rules that can apply to certain dual resident companies (eg not eligible to be a member of a tax consolidated group).



Other

This section describes other opportunities and threats that should be taken into account when structuring tax-efficient mergers and acquisitions.

REPATRIATION OF PROFITS AND WITHHOLDING TAXES

The main categories of income subject to withholding tax are:

- Dividends (see below).
- Royalties (subject to an applicable DTA, the default rate is 30%).
- Interest (see below).

If the income is effectively connected with a branch/permanent establishment of the non-resident in Australia, then withholding tax will not generally apply and the income will be taxed on a full assessment basis.

Dividends

Franked dividends – exempt from withholding tax.

Unfranked dividends:

- 30%, subject to an applicable DTA.
- Default rate under a DTA is generally 15%.
- However, the rate can be reduced further (to nil under some DTAs) where certain majority shareholding requirements are satisfied (eg under the United States DTA there is no city withholding tax where certain US shareholders own more than 80% of the Australian company).
- Exempt from withholding tax to the extent that the unfranked dividends consist of “conduit foreign income”. Aim is to effectively allow income from foreign investments to pass through Australia in an efficient manner.

Interest

Unless a relevant exemption applies, the following payments of interest are generally subject to interest withholding tax at the rate of 10%. Interest paid to a non-resident or foreign branch of an Australian resident by an:

- Australian resident (provided it is not connected with a foreign branch of the Australian resident); and
- Australian branch of a non-resident.

The main exemptions that are usually relevant are:

- Financial Institution exemption in some DTAs for interest paid to an FI.
- Section 128F exemption in relation to certain publicly offered debt interests.
- Interest paid by an Offshore Banking Unit (**OBU**).

Branch

There is no withholding or branch remittance tax in relation to repatriation of Australian profits of a branch.

Fund payments by MITs

Certain fund payments made by qualifying MITs to beneficiaries resident in certain countries (exchange of information countries) can be subject to a reduced rate of withholding tax of 15%. Does not apply to any part of the payment attributable to dividends, interest and royalties, gains from foreign (non-Australian) sources and capital gains in relation to an asset that is not Taxable Australian Property.

TAX SCHEME PROMOTERS

Promoters who devise and market certain tax avoidance and tax evasion schemes and arrangements may be subject to a civil penalty, injunction or enforceable undertaking.

TAXATION OF EMPLOYEES' AND DIRECTORS' EQUITY INCENTIVES

There are complex rules for the taxation of discounts on shares and rights acquired under an employee share scheme by employees and directors.

Fringe Benefits Tax – can apply to certain benefits provided to employees (current rate is 46.5%, ie top marginal tax rate).

TIMING OF TAX RELIEF FOR INTEREST COSTS

Generally, interest is deductible when it is incurred which is usually on a daily accruals basis.

Taxation of Financial Arrangements (TOFA)

There are special tax timing rules which may apply to financial arrangements. The rules mandatorily apply to certain entities and by election in relation to other entities. The rules specify the methods applicable in determining the gains and losses from financial arrangements and the time at which such gains and losses are to be brought to account for tax. Generally, interest on a financial instrument should be brought to account on an accruals basis under these rules. Elections are available to allow financial arrangements to be taxed in accordance with their financial statements for accounting purposes.

INTEREST TAX RELIEF UTILISATION

The tax consolidation regime has largely solved these issues for consolidated groups.

If it is not possible to form a tax consolidated group, then it will be important to consider how tax relief for interest costs will be utilised, in particular where the target is a corporate rather than a business, particularly given that it is no longer possible to transfer losses in such cases.

HIVE-UP

The tax consolidation regime has largely solved these issues for consolidated groups.

Otherwise, there are specific anti-avoidance rules that may apply where a taxable source of income is moved into a company in the structure which has deductions accruing and which is unable to utilise them.

TYPE OF BUSINESS ENTITY AND TAX TREATMENTS

Public Company (Limited/Ltd)	Corporate	30%
Private Company (proprietary limited/Pty Ltd)	Corporate	30%
General Partnership	Fiscally transparent	Partners taxed at marginal rate
Limited Partnership	Generally, the entity is taxed as a corporate	30%
Trust	Generally, fiscally transparent, but losses trapped	Beneficiaries taxed at marginal rate
Branch (foreign company can carry on business in Australia through an Australian branch/permanent establishment)	Generally, income attributable to the branch is taxed in Australia at the corporate rate	30%

FINANCIAL ASSISTANCE

Although not a tax issue as such, attention must always be paid to the Australian financial assistance rules which, broadly, make it unlawful for an Australian company whose shares are being, or have been, acquired (or for any of that company's subsidiaries) to give financial assistance for the purpose of that acquisition (Part 2J.3 of the Corporations Act 2001 (Cth)) unless certain exceptions apply.

MAIN REGULATORY BODIES

ATO	Australian Taxation Office	Commonwealth revenue authority
OSR	Office of State Revenue	Each State has its own OSR that is responsible for State taxes, including stamp duty, land tax and payroll tax
ASIC	Australian Securities & Investment Commission	Regulation of companies generally and financial services
APRA	Australian Prudential Regulation Authority	Regulates banks and financial institutions in relation to capital adequacy (equivalent of UK Financial Services Authority)
FIRB	Foreign Investment Review Board	Approval of certain investments by foreigners into Australia
ACCC	Deals with anti-competitive/anti-trust type issues, including takeovers and acquisitions	Deals with anti-competitive/anti-trust type issues, including takeovers and acquisitions

Contacts



Andrew Stals

Partner

Tel +61 2 9373 7857
andrew.stals@allenoverly.com



Angela Melick

Counsel

Tel +61 2 9373 7591
angela.melick@allenoverly.com



Ka Sen Wong

Counsel

Tel +612 9373 7858
kasen.wong@allenoverly.com

Belgium

Transaction taxes

In this section we identify taxes that will be imposed on the vendor and the acquirer upon a transfer of assets or upon a transfer of shares, as well as other tax implications of a transfer of assets or shares.

STAMP DUTY ON THE TRANSFER OF SHARES

- Not applicable.
- Tax on stock exchange transactions: 0.25% (capped at EUR740) per transaction and per party.

CAPITAL DUTY PAID ON THE CONTRIBUTION OF CAPITAL

Normally no capital duty is paid on the contribution of capital, however exceptions may apply, eg:

- for the contribution of residential real estate by individuals; or
- to the extent real estate is contributed together with the accompanying debt.

In these cases the contribution will be treated as a real estate transfer, subject to transfer tax.

REAL ESTATE TRANSFER TAX

- Registration duty of 10% (Flanders Region) or 12.5% (Brussels and Walloon Regions) charged on the value of the consideration or on the market value, whichever is higher. Relief is available, eg, in case of acquisitions by real estate professionals or in case of a resale within two years.
- Previously, registration duty could be mitigated through a “split sale” structure (separate transfer of leasehold, subject to 2% registration duty, and freehold, subject to 10% or 12.5% registration duty, to two different legal entities). Due to a new Belgian general anti-avoidance rule, these structures are now viewed as a tax abuse by the tax authorities (except if non-tax related reasons prompted the structure).

- Transfer of real estate may be exempt from registration duty and subject to value added tax (VAT) (normal rate of 21%) if the transferred building is “new” for VAT purposes.

CAPITAL GAINS TAX ON THE SALE OF ASSETS

Corporate vendor – Chargeable gains are generally subject to corporation tax (standard rate of 33.99%).

Individual vendor – For non-professional vendors, capital gains are generally tax exempt provided that they are realised within the normal management of the vendor’s private estate; otherwise a 33% tax rate applies. Professional vendors are generally subject to income tax at progressive rates (up to 50% plus local surcharges), but exceptions apply, eg a 16.5% rate applies to capital gains realised on tangible or fixed financial assets or other shares allocated to a professional activity for over five years or realised in the context of a termination of the professional activity.

CAPITAL GAINS TAX ON THE SALE OF SHARES

Corporate vendor – In principle, capital gains on shares held for at least one year are subject to a separate levy of 0.412%, unless the vendor qualifies as a “small or medium-sized enterprise”, in which case these capital gains are fully exempt. Capital gains subject to the 0.412% levy constitute a “minimum taxable basis” according to the tax authorities (ie they are immediately taxed, even if the vendor is in a loss position; the tax cannot be reduced using corporate tax deductions). Capital gains on shares held for a shorter period are taxable at a special corporate income tax rate of 25.75%. However, if the transferred shares do not meet the “subject-to-tax” test in the framework of the dividend participation exemption (eg, excluding capital gains on shares in companies not subject to corporate income tax), tax will apply at the standard corporate income tax rate of 33.99% regardless of the holding period. Capital losses are not deductible.

Special rules will apply to certain professional equity traders.

Individual vendor – As above for the sale of assets.

AVOIDANCE OF CAPITAL GAINS TAX

If certain requirements are met, a “rollover” regime may apply to the taxation of capital gains, subject to reinvestment of the amount received for the transferred asset. In such a case, the taxation of the capital gain will be spread over the depreciation period of the new reinvested asset.

PRESERVATION OF TAX LOSS CARRY-FORWARD

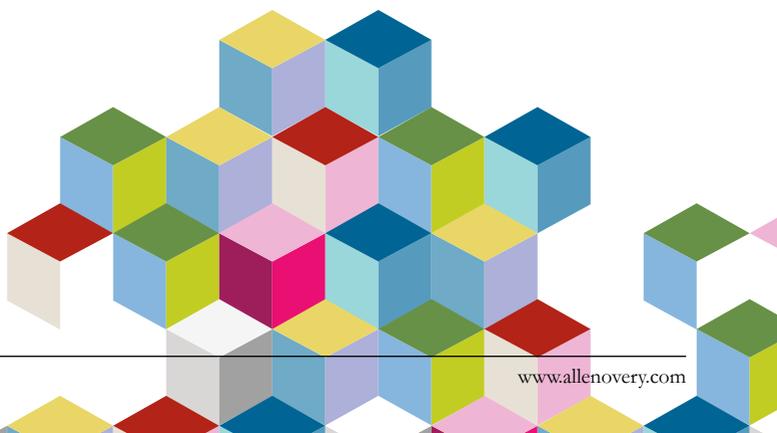
Generally, trading losses may be carried forward indefinitely and set off against future profits. However, a direct or indirect change of control of the company may result in the unavailability of all tax losses carried forward if the change of control does not reflect legitimate business needs. Moreover, loss limitation rules apply in the context of tax-neutral mergers, demergers, etc.

NON-BELGIAN VENDOR

A non-resident seller without a Belgian establishment (ie, not subject to Belgian corporate income tax) should generally not be subject to Belgian tax on any chargeable gains arising from the sale of shares in a Belgian company, whereas the sale by a Belgian subsidiary of its business/assets would result in Belgian corporate income tax being levied on any gains.

VALUE ADDED TAX

VAT may be charged on a supply of goods or services. However, there is no charge to VAT on a purchase of shares. Asset purchases are generally subject to VAT unless transfer of going concern (**TOGC**) relief applies.



Opportunities and threats

In this section an overview is provided of opportunities to maximise relief for acquisition costs (such as financing costs), as well as other items which require attention when designing an efficient tax structure.

STEPPING-UP ASSET VALUES

- The allocated portion of the purchase price of assets may in principle be treated as the basis for depreciation or as the base cost for the calculation of any chargeable gain or deductible loss.
- Amortisation of acquired goodwill and intangible assets is, in principle, possible.
- No relief is available on the acquisition of shares; there is neither a step-up in the cost of the assets of the target company nor an increase in any depreciation or allowances available to the target company.

TAX CONSOLIDATION RULES

Belgium does not have a tax consolidation regime (except for VAT purposes).

DEBT/EQUITY RULES

Payments to related parties and low-taxed lenders: A 5:1 debt-to-equity ratio applies in respect of borrowings (excluding publicly issued bonds and similar securities, as well as loans from, amongst others, EEA financial institutions and the EU Investment Bank) if the beneficial owner of the interest is either a related party or a low-taxed lender. Related parties are for these purposes expected to mean companies under the control of the borrower, companies controlling the borrower, companies which share a common management with the borrower and other companies controlled by any of the aforementioned companies; a shareholder is considered to have control when, *inter alia*, it directly or indirectly holds a majority of voting rights or is entitled to appoint a majority of directors. Lenders will be treated as low-taxed if they are not subject to income tax or are subject to a substantially more beneficial tax regime than the Belgian common law regime on the interest they receive. To the extent the ratio is exceeded, the excess interest will not be deductible for tax purposes. Exceptions apply to leasing and factoring companies and to SPVs executing a PPP project.

- Payments to non-resident corporate directors or to individual shareholders or directors: a one-to-one debt-to-equity ratio applies in respect of advances (including loans) granted by: (i) Belgian or foreign individual shareholders or directors (including managers, liquidators or individuals with a similar function); or (ii) non-resident corporate directors (including managers, liquidators or entities with a similar function). Insofar as the ratio is exceeded, the interest payable on the advances is classified as a dividend, which is by nature non-deductible and for which different exemptions apply.

DISALLOWED AND DEFERRED INTEREST (OTHER THAN DEBT/EQUITY RULES)

Interest expenses on a loan to finance the acquisition of shares or assets is typically deductible for Belgian tax purposes, provided that the interest rate and other terms and conditions are at arm's length.

The borrower must be able to demonstrate that the interest expenses are incurred or borne to generate or maintain taxable income, but the fact that future gains on the financed assets would be fully exempt (eg shares) does not affect the deductibility analysis. Furthermore, the interest charges must be incurred in the framework of the company's corporate purpose. In addition, the borrower must have the legitimate expectation that the financed assets will generate an income in excess of the expected interest expense.

Furthermore, specific rules may apply in respect of specific beneficiaries.

- A reversal of the burden of proof applies if interest is directly or indirectly paid to a non-Belgian low-taxed lender. The borrower will have to prove that the financing is both at arm's length and relates to a bona fide business transaction to qualify for a deduction of the interest.
- A specific tax return must be filed for payments to entities in jurisdictions with a nominal tax rate of less than 10% or that are on the list of non-cooperative countries established by the OECD during the entire taxable period in which the payments took place, if the taxpayer's total annual payments to such entities exceed EUR100,000. Furthermore, the debtor must prove that the payments relate to "real and sincere transactions" with "persons other than artificial constructions". If the debtor fails to file the return or to prove that the transactions are business-driven, the deductibility of payments will be disallowed for tax purposes.

CONSEQUENCES OF GUARANTEES FROM A RELATED PARTY FOR THIRD PARTY DEBTS

If a Belgian company grants a security interest over its assets, in order to guarantee or secure the obligations of a related company, it must receive arm's length consideration. The absence of appropriate consideration could trigger transfer pricing issues and could impact on the tax-deductibility of payments made by the Belgian company as a result of the enforcement of the guarantee.

Loans made by a third party and guaranteed by a related party (or funded by a related party which retains all or part of the lending risk) should be taken into account for the purposes of the new 5:1 debt-to-equity ratio currently being introduced (see above), to the extent the guarantee (or the funding) has tax fraud or tax evasion as one of its main aims.

INTERNATIONAL TAX ARBITRAGE

Belgium has traditionally had a positive attitude towards international tax arbitrage in the context of the cross-border financing of Belgian companies. Belgium's policy has always been to attract financing activities to Belgium by offering an attractive tax regime for these activities.

- Notional interest deduction: Belgium offers a tax incentive to all Belgian companies (with some limited exceptions) and all Belgian establishments: the notional interest deduction (NID). The NID regime is in fact a "structural" tax arbitrage technique. The NID generates a tax deduction for the Belgian company (to avoid discrimination between debt financing and equity financing), but does not re-characterise equity financing as debt financing. As a result, payments made to the parent company continue to be characterised as dividend distributions and are therefore often eligible for the participation exemption.
- Hybrid loans: Belgium has historically applied a "form-over-substance" theory to financing structures. If the Belgian company receiving the financing technically has a legal obligation to pay back the principal amount and to pay periodic compensation regardless of the availability of distributable reserves, the financing will generally be classified as debt financing, even if the investor's economic position is similar to that of an equity investor. Since the introduction of the new version of the Belgian general anti-avoidance rule in 2012, there is a certain level of uncertainty in relation to the tax treatment of hybrid loans. In addition, the tax treatment is likely to be impacted by the proposed amendment to the EU Parent Subsidiary Directive in relation to hybrid instruments.

TAX CREDIT

A foreign tax credit (**FTC**) is, in principle, available in respect of non-Belgian withholding tax (**WHT**) on foreign-source interest. The FTC is subject to anti-channelling rules and anti-stripping rules. In addition, the Belgian creditor must comply with complex debt-financing ratio requirements aimed at restricting the FTC to the Belgian tax on foreign interest income. Furthermore, the FTC is calculated by reference to the effective WHT, but capped at 15%. This means that a full credit is not available if the effective WHT exceeds 15%. Note, however, that the relevant double tax treaties may provide more beneficial rules (eg “tax sparing” clause).

CONTROLLED FOREIGN COMPANY LEGISLATION

Strictly speaking, Belgium has no controlled foreign company (**CFC**) legislation. However, the Belgian tax authorities may disregard a transfer of assets (including cash and interest-generating assets) to a low-taxed non-Belgian entity, unless the company can demonstrate: (i) that it has received, in exchange for the transfer, consideration which generates income attracting the normal tax burden in Belgium (as compared to the tax burden if no transfer had occurred); or (ii) that the transfer reflects legitimate business needs.

TRANSFER PRICING

As a general rule, Belgian and international intra-group transactions must be on arm’s length terms and conditions to avoid adverse tax consequences (eg non-deductibility, taxation of “abnormal or benevolent advantages” granted or received).

TAX RESIDENCE

For the purposes of corporate income tax, entities are resident in Belgium if they are incorporated in Belgium. Non-Belgian incorporated entities may be resident in Belgium if their seat of effective management is in Belgium. (NB – The terms of an applicable double taxation agreement may determine residence for treaty purposes in the case of dual-resident companies.)

Other

This section describes other opportunities and threats that should be taken into account when structuring tax-efficient mergers and acquisitions.

TAX CERTIFICATES IN THE CONTEXT OF AN ASSET DEAL

To ensure that a tax collector can recover the taxes due from a seller after it sells off a relevant part of its assets (transfer of a set of goods, consisting of one or more items allowing the purchaser to retain a client base), Belgian tax law provides that a purchaser may be held liable for the outstanding tax debts of the seller for an amount up to the purchase price paid before the end of the month following that during which a copy of the purchase agreement is formally notified to the local tax collector. Furthermore, the asset transfer is not enforceable against the Belgian tax authorities until the expiry of this period. However, the seller may request from the relevant tax collectors a certificate confirming that it has no outstanding tax debts or pending tax audits at the date of the certificate's issue. The certificate must be granted or refused within 30 days after the filing of the request and is valid for 30 days. If the purchase agreement is notified to the relevant tax collector together with the certificate within the 30-day period, the purchaser will avoid the risk of secondary liability.

TRANSFER OF SHARES IN "CASH-BOX" COMPANIES

The Belgian income tax code provides for a specific anti-avoidance clause targeting the sale of privately held "cash-box" companies.

The tax avoidance scheme consists of the sale of shares in a Belgian company holding only cash proceeds from a transfer of its assets, following which the purchaser of the shares illegitimately extracts the cash from the company and then disappears without paying the capital gains tax on the sale of the assets.

To ensure payment of the taxes in such a case, any corporate or individual shareholder selling at least 3/4 of a minimum participation of 33% within a one-year period, is jointly liable for the tax debts of the target related to the taxable period of the share transfer and in the three previous taxable periods. This joint liability regime also applies to the capital gains tax payable in respect of the sale of assets prior to a share deal, if the target has opted for rollover tax relief but the reinvestment is not made in due time after the share deal (in which case the entire capital gain becomes taxable).

Note that this anti-avoidance provision has a much wider scope than the avoidance scheme at which it was targeted. The joint liability regime applies if the assets of the target consist of at least 75% receivables, fixed financial assets, financial investments and/or cash. Consequently, the sale of a wide range of holding companies is affected.

TAXATION OF EMPLOYEES' AND DIRECTORS' EQUITY INCENTIVES

There are specific rules for the taxation of equity incentives received by employees and directors.

TIMING OF TAX RELIEF FOR INTEREST COSTS

In principle, the tax regime “follows” the accounting treatment. From an accounting perspective, “certain and liquid” liabilities relating to the financial year (or to previous financial years) must be recorded in the accounts, regardless of their actual payment.

INTEREST TAX RELIEF UTILISATION

Taking into account that there is no group tax regime in Belgium, interest tax relief utilisation is not automatically achieved in M&A transactions. A technique often used in Belgium to achieve the matching of the financing expenses of the purchaser with the operating profits of the target is to push the acquisition debt down to the target. A debt push-down is generally achieved by a dividend payment or by a capital reduction by the target. This dividend or capital reduction is financed with debt, and the parent company subsequently uses the cash to reimburse part of its own debt. Alternatively, instead of making an actual cash payment to the parent company, the subsidiary may assume part of its parent's debt up to the amount of the dividend or the capital reduction. Another frequently used debt push-down technique consists in the intra-group purchase of certain assets (eg participation in subsidiaries), again financed with debt or in return for the assumption of debt or an intercompany loan.

HIVE-UP

It may be worth considering moving a taxable source of income up to a company in the group that has deductions accruing.

FINANCIAL ASSISTANCE

Although it is not a tax issue as such, attention must always be paid to the Belgian financial assistance rules which, broadly, make it unlawful for a Belgian company whose shares are being, or have been, acquired (or for any of that company's subsidiaries) to give financial assistance for the purpose of that acquisition, subject to certain exceptions.

TAXATION OF DISTRIBUTIONS RECEIVED FROM SUBSIDIARIES

Dividend relief is available for qualifying participations. In Belgium, this relief takes the form of a tax deduction equal to 95% of the amount of the dividend (including liquidation proceeds) received (the Dividends Received Deduction or **DRD**). The basic qualifying conditions for the DRD are that: (i) the parent company should have a minimum participation of 10% or have incurred a minimum acquisition cost of at least EUR2.5million; and (ii) the distributed profits must have been subject to tax at an earlier stage, which is typically the case for Belgian-sourced dividends.

Withholding taxes Belgium imposes a withholding tax on dividends of 25%. A 15% withholding tax applies to dividends distributed by residential REITs (ie those which hold at least 80% of their real estate investments in residential real estate located in the EEA). An exemption from the Belgian dividend withholding tax of 25% is generally available for intra-group dividend payments within the EU or to entities that are resident in a tax treaty state which provides for an exchange of information in respect of taxation, subject to a minimum participation of 10% held for an uninterrupted period of one year (note that the ECJ recently held that the Belgian rules are incompatible with EU law to the extent non-resident corporate portfolio investors incur dividend withholding tax on dividends distributed by a resident company if the non-resident corporate portfolio investors hold a participation of less than 10% in the capital of the resident company but incurred a purchase cost of at least EUR1.2m, whilst resident corporate portfolio investors are effectively able to obtain a withholding tax refund).

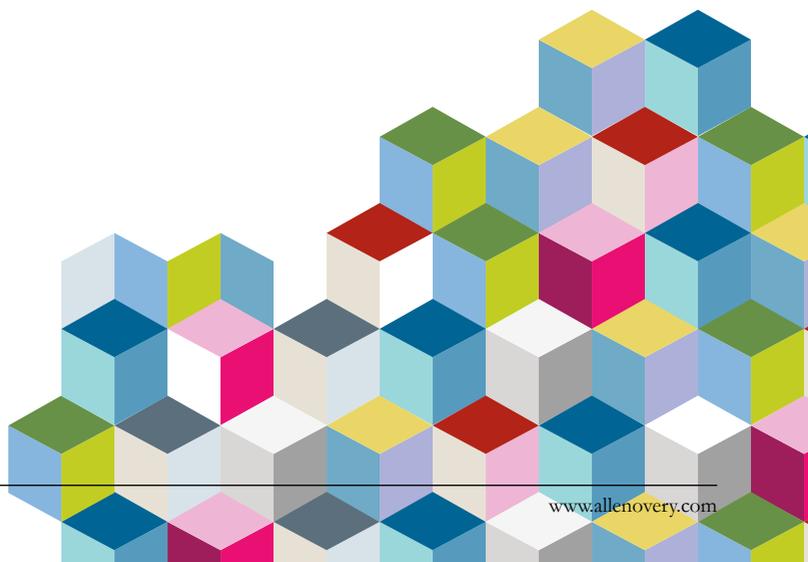
Interest payments by a Belgian company are in principle subject to a 25% interest withholding tax. However, exemptions are available based on: (i) domestic law; (ii) double tax treaties; and (iii) EU law. Pursuant to Belgian domestic law, exemptions are available for *inter alia*:

- most interest payments between Belgian corporate entities and to Belgian credit institutions (should withholding tax nevertheless be payable, it can generally be fully credited);
- interest on receivables paid to a licensed credit institution established in an EEA Member State or in a tax treaty jurisdiction;
- interest on receivables and (non-capitalisation) securities paid or attributed to non-resident lenders by “intra-group banks” and qualifying listed holding companies (including qualifying holding companies controlled by listed companies); and
- interest paid to non-resident investors on registered non-capitalisation bonds and on securities cleared through the X/N clearing system (managed by the National Bank of Belgium).

Although Belgium's new tax treaty policy is to provide for an exemption on interest payments between corporate entities, the majority of existing treaties do not yet reflect this. Important exceptions are the treaties with Luxembourg, the Netherlands, Germany, the United Kingdom and the United States, which all provide for broad withholding tax exemptions on interest payments between companies. Within a (cross-border) group, withholding tax relief is available for payments to EU-based "associated companies" under the Interest and Royalties Directive. Belgium has, however, opted for a broader definition of "associated companies" than set out in the Directive, as payments made between indirectly owned companies are also exempt.

The payment of **royalties** is generally subject to withholding tax (currently at a rate of 25%) when made to a person outside Belgium. An exemption may be available under a double tax treaty or under the Interest and Royalties Directive.

As from tax year 2014, a Belgian resident company will be subject to a "fairness tax" of 5.15% on the dividends it distributes, if (part or all of) its taxable profit has been offset against (current year) notional interest deduction and/or carried forward tax losses. The taxable basis is essentially equal to a percentage of the difference between the distributed dividends and the taxable result of the company (with a correction for "grandfathered reserves"). The fairness tax is a separate assessment borne by the company distributing the dividends and does not constitute a withholding tax on the dividends that are distributed. It cannot further be reduced by other deductions and is not deductible for corporate income tax purposes.



Contacts



Patrick Smet

Partner

Tel +32 2 780 2431
patrick.smet@allenoverly.com



Stéphanie Houx

Counsel

Tel +32 2 780 2487
stephanie.houx@allenoverly.com

Czech Republic

Transaction taxes

In this section we identify taxes that will be imposed on the vendor and the acquirer upon a transfer of assets or upon a transfer of shares, as well as other tax implications of a transfer of assets or shares.

STAMP DUTY ON THE TRANSFER OF SHARES

Nil.

CAPITAL DUTY PAID ON THE CONTRIBUTION OF CAPITAL

Nil. (except for real estate transfer tax (**RETT**))

Notary fees, registration fees and other similar expenses will generally be payable in the case of contributions to the registered capital of the company.

REAL ESTATE TRANSFER TAX

RETT is generally calculated as 4% of the purchase price or the comparative tax value (either 75% of the value established on the basis of the Czech Valuation Act or 75% of the average market value of comparable real estate as determined by the Tax Authorities, if available, at the discretion of the taxpayer), whichever is higher. However, a number of specific situations (eg a contribution into the equity of a company, an auction/execution, a financial lease or the sale of Real Estate (**RE**) as part of an enterprise) has different calculation of RETT base (eg the value established on the basis of the Czech Valuation Act, the purchase price or the fair value established by an expert). RETT will not be triggered on a share sale or upon merger/demerger.

CAPITAL GAINS TAX ON THE SALE OF ASSETS

Corporate vendor – Capital gains derived by a corporate vendor from an asset sale will be taxed as ordinary income of the corporate vendor subject to Czech corporate income tax at the rate of 19%.

Individual vendor – Capital gains realised by an individual vendor upon a sale of assets (assets forming part of his/her business property) will be taxed as ordinary income of the individual vendor subject to personal income tax at a flat rate of 15% (a solidarity surcharge of 7% may also apply under certain circumstances). An exemption from tax might be available in respect of certain assets that have been withdrawn from the business property of the individual vendor (after five years following the withdrawal).

CAPITAL GAINS TAX ON THE SALE OF SHARES

Corporate vendor – Unless exempt, capital gains realised by a corporate vendor upon a sale of shares will be taxed as ordinary income of the corporate vendor subject to Czech corporate income tax at the rate of 19%.

However, under the Czech participation exemption, capital gains derived by a Czech or EU/EEA parent company (with the exception of one in Liechtenstein) from a sale of shares of the Czech or EU subsidiary are tax exempt if the parent company holds at least 10% in the registered capital of the subsidiary for an uninterrupted period of at least one year. In order to qualify for the exemption, the companies concerned must: (i) have a legal form listed in the Annex to the EU Parent-Subsidiary Directive; (ii) be subject to corporate income tax; and (iii) be considered tax residents of the EU/EEA Member States based on local tax laws (EU in the case of a daughter company). The exemption does not apply where Czech tax resident subsidiary is liquidated. Same limitation applies if the shares in the subsidiary were acquired as part of the enterprise.

Capital gains derived by a Czech or EU/EEA (with the exception of one in Lichtenstein) parent company from a sale of shares in a third country (including EEA) subsidiary may, under certain conditions, be exempt as well.

Individual vendor – Unless an exemption from tax applies, capital gains realised by an individual vendor upon a sale of shares (shares forming part of his/her business property) will be taxed as ordinary income of the individual vendor at a flat rate of 15% (a solidarity surcharge of 7% may also apply under certain circumstances). An exemption is available if an individual vendor terminates his/her business activities (depending on the nature of the shares, this is after five or three years).

However, capital gains from a sale of shares in joint stock companies not forming part of the business property of the individual will generally be exempt from Czech personal income tax if such securities are held by the individual vendor for a period exceeding three years (applies with respect to shares acquired on or after 1 January 2014). Furthermore, capital gains from a sale of securities not forming part of the business property of the individual (including shares in joint stock companies or equity membership certificates in limited liability companies) will be exempt from Czech personal income tax if the annual (worldwide) income (on a gross basis) of the individual from the sale of such securities does not exceed the amount of CZK100,000. In other cases, capital gains will be exempt if the shares (such as participation in limited liability companies not forming part of the individual's business property) are held for more than five years.

AVOIDANCE OF CAPITAL GAINS TAX

In certain cases, capital gains are deferrable under the provisions of the EU Merger Directive as incorporated into Czech tax law provided that the reorganisations in question (ie mergers, de-mergers, transfers of business and share-for-share exchanges) meet the conditions set out by the law. In addition, capital gains may be exempt under the the Czech participation exemption – see “Capital gains tax on the sale of shares” for more details.

PRESERVATION OF TAX LOSS CARRY-FORWARD

In general, a tax loss can be carried forward for five consecutive years (taxable periods). If a *substantial change* in the structure of persons who directly participate in the capital or control of a company occurs, the set-off of tax losses carried forward against future profits is disallowed¹ unless the company passes a special revenue structure test. The test generally requires the company to prove that at least 80% of the company’s revenue in the year of substantial change and in the following years of intended use of tax loss, which was assessed for years prior to the substantial change, was derived from the same activities that were performed by the company in the period when the tax loss was assessed. The substantial change always means a change which relates in total to more than 25% of the registered capital or voting rights of the company or which results in a shareholder gaining dominant control over the company. In the case of companies having bearer shares it is deemed that the substantial change occurs unless proved otherwise.

On the merger or demerger of a company, a rollover of tax losses² carried forward by a dissolving company is possible under certain circumstances. Nevertheless, such tax loss carry-forwards can only be set against future profits of the acquiring company if certain restrictions are adhered to.³

NON-RESIDENT VENDORS

Share sale – Gains derived by a Czech tax non-resident vendor from: (i) a sale of shares in a company having its seat or the place of effective management in the Czech Republic; and (ii) a sale of shares in a company (representing tradable securities) having neither its seat nor the place of effective management in the Czech Republic to a Czech tax resident or a Czech permanent establishment of a Czech tax non-resident, will be considered a Czech source income and, as such, subject to Czech taxation. Nevertheless, Czech taxation is eliminated under a majority of the double taxation treaties concluded by the Czech Republic (approximately 80 treaties closely following the OECD model) or, to the extent that the Czech Republic preserves its taxing rights, under the Czech participation exemption (see “Capital gains tax on the sale of shares” for more details).

¹ The substantial change must have occurred in the year 2004 onwards.

² Tax losses incurred in the year 2004 onwards.

³ Decisive date of merger/demerger from 1 January 2004 onwards.

Asset sale – Gains derived from a sale of movable assets forming part of the business property of a Czech permanent establishment will be taxable in the Czech Republic provided that such assets are sold to a Czech tax resident (either an individual or a legal entity) or to a permanent establishment of a Czech tax non-resident in the Czech Republic. On the other hand, gains derived from the sale of real estate which is located in the Czech Republic shall be treated as Czech sourced income irrespective of the character of the buyer. The same treatment applies if such movable and immovable assets represent (part of) an enterprise which is located in the Czech Republic.

VALUE ADDED TAX

Share sale – No value added tax (**VAT**) is charged on a transfer of shares (the sale is either exempt from or falls outside the scope of VAT).

Asset sale (purchase of individual assets) – Czech VAT at the standard (exceptionally reduced) rate is generally charged on an asset sale involving the purchase/sale of individual assets/rights.

Transfer of (part of) an enterprise – In contrast to an asset sale, no supply is deemed to have taken place where transfer (part of) an enterprise is involved, ie such transfer is treated as outside the scope of Czech VAT. If the transferor is a person registered for Czech VAT, the transferee becomes a person registered for Czech VAT purposes *ex lege* as of the date of acquisition of the respective property.

Merger/demerger – Similar treatment as in the case of transfer of a (part of) an enterprise applies to Czech mergers/demergers.

VAT grouping – In principle, it is possible to establish a VAT group in the Czech Republic. A VAT group shall consist of related persons that have their seat in the Czech Republic or have a Czech fixed establishment (the foreign part of a taxable person whose Czech establishment forms part of a VAT Group is regarded as a separate taxable person from its Czech establishment)⁴. For VAT purposes, “related persons” comprise persons related through capital or otherwise related persons. Persons are related through capital where one person directly or indirectly holds at least 40% in the registered capital or voting rights of one or more persons. Other related persons are such persons where at least one identical person participates in their management.

⁴The approach is not consistent across EU. Nevertheless, this may change following the soon-to-come decision of the Court of Justice of the EU in the matter of Skandia America Corporation USA (C-7/13).

Opportunities and threats

In this section an overview is provided of opportunities to maximise relief for acquisition costs (such as financing costs), as well as other items which require attention when designing an efficient tax structure.

STEPPING-UP ASSET VALUES

Share sale – No step-up in basis can be achieved on a share sale. Neither the basis of the assets nor the rates at which the assets are depreciated are affected.

Asset sale (purchase of individual assets) – On a purchase of individual assets, a step-up in basis of the assets acquired is generally possible, allowing the acquirer to depreciate the assets from their acquisition cost.

Transfer of (part of) an enterprise – Depending on the particular circumstances of the transfer and the method of valuation of the acquired assets, either: (i) goodwill (meaning a difference between the value of a business as a whole and the aggregate of fair values of individual assets after their revaluation reduced by assumed liabilities); or (ii) valuation difference (meaning a difference between the value of a business as a whole and the aggregate of book values of individual assets reduced by assumed liabilities) can arise and be depreciated for tax purposes.

Merger/demerger – On a demerger, merger by formation of a new company and merger by acquisition (applies only to a company being acquired under certain conditions), the assets (and liabilities) can be revalued to a fair value for accounting purposes. Nevertheless, in contrast to the accounting basis of assets, no step-up in the tax basis of the assets is possible. Furthermore, neither goodwill nor valuation difference arising on merger/demerger can be depreciated for tax purposes.

TAX CONSOLIDATION RULES

There are no group taxation rules in Czech tax law. Consequently, no offset of profits and losses at a group level is possible and separate tax reporting must be made by each group company. Nevertheless, in practice, there are techniques that may enable tax consolidation to be achieved. However, it is important that any related structuring has a proper commercial underpinning to mitigate the risk of a challenge by the authorities.

THIN CAPITALISATION RULES

According to Czech thin capitalisation rules, the tax-deductibility of financing expenses (defined as interest expenses and related costs such as for example guarantee payments or fees for intermediation etc) on qualified debt instruments (such as loans, credits, promissory notes, etc) from related parties is limited by a debt to equity ratio of 4:1 (6:1 if the borrower is a bank or an insurance company).

The financial expenses incurred on related-party debt in excess of the statutory threshold are tax non-deductible. In addition, the interest in excess of the statutory threshold can be reclassified by the tax authorities as a hidden distribution of profits and taxed accordingly (unless distributed to a tax resident established in the EU/EEA (except for Lichtenstein) or Switzerland). The provision of a third party loan to a Czech borrower secured by a related-party guarantee is not subject to the Czech thin capitalisation rules. On the other hand, back-to-back loans fall under the Czech thin capitalisation rules.

Despite the above, qualified debt instruments, where the interest is capitalised into the acquisition price of assets as well as interest-free qualified debt instruments are not covered by thin capitalisation rules.

DEBT/EQUITY RULES

See “Thin capitalisation rules” and “Hybrid loans” for more details.

DISALLOWED AND DEFERRED INTEREST (OTHER THAN DEBT/EQUITY RULES)

The expenses of a parent company relating to the holding of an ownership interest (shareholding) in its subsidiary are regarded as tax non-deductible. The overhead (indirect) expenses relating to such holding are limited to 5% from dividends distributed by the subsidiary unless the taxpayer proves that the actual amount of these overhead (indirect) expenses is lower.

Unless the parent company proves otherwise, interest charged on any qualified debt instruments (such as loans, credits, promissory notes, etc) that were taken by the parent company within the period of six months prior to the acquisition of such ownership interest is regarded as an expense directly attributable to the holding of the ownership interest in the subsidiary for the entire period of such holding (including the period for which the ownership interest is held by a person who qualifies as a related party to the borrower). In practice, these adverse impacts can be mitigated by utilising certain planning opportunities. Any restructuring should nevertheless have proper commercial substance to mitigate the risk of a challenge.

Furthermore, expenses (including interest expenses) relating to revenues that are either tax

exempt, subject to final withholding tax (eg domestic dividend income) or included in a separate tax base (eg foreign dividend income) are treated as non-deductible. See also “Transfer pricing” and “Hybrid loans” for more details.

CONSEQUENCES OF GUARANTEES FROM A RELATED PARTY FOR THIRD PARTY DEBTS

See “Thin capitalisation” rules and “Financial assistance” for more details.

HYBRID LOANS

According to Czech tax law, financing expenses incurred in respect of qualified debt instruments (such as loans, credits, promissory notes, etc), where: (i) interest; or (ii) due date of the financing expense fully or mainly depends on the debtor’s profit, are tax non-deductible.

CONTROLLED FOREIGN COMPANY LEGISLATION

There is no controlled foreign company (**CFC**) legislation in the Czech Republic.

PASSIVE FOREIGN INVESTMENT COMPANY ANTI-DEFERRAL REGIME

There is no passive foreign investment company (**PFIC**) anti-deferral regime in the Czech Republic.

TRANSFER PRICING

Transactions between related parties must be performed on arm’s length terms. If the tax authorities ascertain that a transaction has been entered into on anything other than arm’s length terms, and the difference between the amount charged and the arm’s length amount is not properly substantiated, the tax authorities have the right to adjust the tax base of the parties involved in the transaction accordingly. The difference in excess of the arm’s length rate can be reclassified by the tax authorities as a hidden distribution of profits and taxed accordingly (unless the recipient is a tax resident established in the EU/EEA (except for Lichtenstein) or Switzerland).

Under Czech income tax law, persons are regarded as related if they qualify either as: (i) capital-related persons; or (ii) otherwise related persons.

Persons are regarded as capital-related if one person directly or indirectly participates in

another person's capital or voting rights, or one person directly or indirectly participates in the capital or voting rights of more persons. All persons involved in such a relationship are considered to be related. The participation in capital or voting rights is defined as the holding of at least a 25% share in the registered capital or voting rights of such persons.

Persons are considered as otherwise related if one of the following situations occurs:

- one person participates in the management or control of another person;
- identical persons or close persons (as defined under Czech civil law) participate in the management or control of other persons; such other persons are regarded as otherwise related;
- persons qualify as the controlling and controlled persons and/or persons happen to be controlled by the same controlling persons; and
- persons who have established a legal relationship predominantly for the purpose of reducing their tax base or for increasing their tax loss.

The Czech Ministry of Finance has issued a decree stating that the OECD Transfer Pricing Guidelines and EU Code of Conduct should be generally accepted in the Czech Republic. Although the decree is of a non-binding character, it is widely accepted in the Czech Republic. As such, documentation prepared in accordance with the EU Code of Conduct should be sufficient to substantiate the arm's length price.

In principle, preparation or filing of transfer pricing documentation is not mandatory in the Czech Republic. The taxpayer may nonetheless be requested at any time during a potential tax audit to substantiate that the terms of the respective related-party dealings are at arm's length.

Taxpayers are enabled to request an advance pricing agreement (**APA**) from the locally competent tax authority. The APA is valid for three years unless the circumstances under which the arm's length price was arrived at by the Czech tax authorities change.

A guidance issued by the Czech tax authorities concerning low value adding services provided between related parties/associated enterprises which follows the respective Joint Transfer Pricing Forum's guidelines is available from 2013. According to the guidelines, mark-ups of 3%–7% of the cost should be regarded as arm's length.

RESIDENCE

A taxpayer who is a legal entity is considered to be tax resident in the Czech Republic if it has either its seat or its place of effective management in the Czech Republic. A taxpayer who is not a legal entity (eg trust or mutual fund) is considered to be tax resident in the Czech Republic if it is founded or established under Czech law (the application of the place of effective management criterion with respect to this category of taxpayers is not clear).

An individual is treated as a Czech tax resident if he/she has a residential address (permanent residence) in the Czech Republic or if he/she stays in the Czech Republic for at least 183 days in the relevant calendar year, either continuously or intermittently.

ENTITY CLASSIFICATION (“CHECK-THE-BOX”) RULES

There are no entity classification rules similar to “Check-the-Box” in the Czech Republic.

TAXATION OF DISTRIBUTIONS RECEIVED FROM SUBSIDIARY BY A QUALIFYING PARENT COMPANY

Unless exempt, dividends received from subsidiaries by a Czech parent Company are generally subject to tax at 15%. The way the tax is collected depends on whether the dividends are payable by a Czech or a non-Czech subsidiary. Dividends from a non-Czech subsidiary enter a separate tax base of the parent company and are subject to self-assessment at the rate of 15% (on a gross basis). This treatment can be further modified by an applicable tax treaty. Dividends received from a Czech subsidiary are excluded from taxation at the parent company level as they are subject to withholding tax of 15% at source.

Unless exempt, dividends paid by Czech subsidiaries to Czech tax non-residents are subject to withholding tax (see “Withholding taxes” for more details).

Under the Czech participation exemption, dividends received by a Czech or EU/EEA (excluding Liechtenstein) parent company from a Czech or EU subsidiary are tax exempt if the parent company holds at least 10% in the registered capital of the subsidiary for an uninterrupted period of at least one year (the latter condition may be fulfilled subsequently, ie tax exempt distributions are possible even before the one-year threshold has been met). Besides the above principal criteria, in order to qualify for the exemption the companies concerned must further: (i) have a legal form listed in the Annex to the EU Parent-Subsidiary Directive; (ii) be subject to corporate income tax; and (iii) be considered tax residents of an EU/EEA Member State based on local tax laws (EU in the case of a daughter company). As concerns the parent company, it must be a beneficial owner of dividends. Similar exemption is available for a Swiss parent company holding a Czech subsidiary. The exemption does not apply where the subsidiary is liquidated (with the exception of an EU parent company receiving dividend from a Czech subsidiary).

Dividends received by a Czech or EU/EEA (excluding Liechtenstein) parent company from subsidiaries in third countries (including EEA countries) may also be exempt under certain conditions.

If exempt dividends are received, overhead costs corresponding to 5% of the dividend income are automatically deemed to be tax non-deductible costs relating to the shareholding in the subsidiary unless the parent company proves that the actual amount of such overhead (indirect) costs is lower.

WITHHOLDING TAXES

Dividend payments made by a Czech subsidiary are subject to a withholding tax of 15% or 35%. The 15% rate is applicable with respect to recipients, who are tax residents in either (i) an EU/EEA country or (ii) a country with which the Czech Republic has an effective double tax treaty or an effective double (or multilateral) treaty on the exchange of information. The 35% rate is applicable with respect to other recipients. The withholding tax may further be reduced or eliminated under the respective double taxation treaty or where exemption from tax is available. As regards conditions for the participation exemption, see “Taxation of distributions received from subsidiaries by a qualifying parent company” for more details.

Interest and royalty payments are generally subject to withholding tax of 15% or 35% (on a gross basis) (for details whether withholding tax of 15% or 35% applies please see above in relation to dividends). Nevertheless, tax relief at source (whether full or partial) might be available under the respective double taxation treaty or, insofar as the Czech Republic preserves its taxing rights, the payments may be exempt under the Czech implementation of the EU Interest and Royalty Directive. The latter exemption is available if the distribution is made to an associated company (as defined in the directive) established in an EU/EFTA country (except for Liechtenstein).

To the extent that interest or royalties remain taxable, the EU/EEA tax residents may opt to tax this income on a net (as opposed to a gross) basis by filing a Czech tax return. In this case, a standard corporate income tax rate (19%) applies. Any tax withheld is credited against a final tax liability stated in the tax return. Any overwithholding is generally refundable as a tax overpayment.

Other

This section describes other opportunities and threats that should be taken into account when structuring tax-efficient mergers and acquisitions.

ANTI-ABUSE REGULATIONS

There are essentially three main general anti-avoidance rules. Czech tax law addresses the “substance over form” principle and the jurisprudence of Czech tax courts further recognises a “circumvention of law” concept and the doctrine of “abuse of law”. The abuse-of-law doctrine is applied consistently with the twofold test – a subjective test and an objective test – as set out in the jurisprudence of the Court of Justice of the European Union.

In addition, Czech tax law contains a number of specific anti-abuse provisions (eg provisions relating to tax neutral reorganisations, a beneficial ownership concept, etc). Certain measures preventing tax loss trafficking were introduced in 2004 (see “Preservation of tax loss carry-forward” for further details).

TAXATION OF EMPLOYEES’ AND DIRECTORS’ EQUITY INCENTIVES

In the absence of any specific rules (including any approved schemes), taxation of equity incentives received by employees and directors (including share issues and share options granted to managers in private equity transactions) should be addressed on a case-by-case basis. Certain guidance in this respect can be derived from the jurisprudence of Czech courts (in particular, as concerns taxation of an employees’ stock options).

HIVE-UPS

In the absence of tax consolidation rules and having regard to further possible restrictions (such as the “acquisition cost disallowance” rule) it may be worth, upon debt-financed acquisition of a Czech target company, considering moving a taxable source of income up into the acquiring company in the structure which bears the relevant costs. Typically, an upstream merger could be used. Nevertheless, the impact of the merger on the post-merger combined equity of the acquiring company should always be considered, to avoid any possible thin capitalisation issues.

FINANCIAL ASSISTANCE

Although not a tax issue as such, Czech financial assistance rules should always be taken into consideration. Under Czech financial assistance rules, a limited liability, a joint stock company or a cooperative may provide financial assistance in respect of an acquisition of its own shares or, under certain circumstances, shares in its controlling company, only if statutory conditions are met and if certain procedures are followed (this is referred to as the whitewash procedure). Financial assistance is defined as the provision of an advance payment, loan or credit or provision of security by a company for the purposes of acquisition of shares in itself.

The conditions for providing financial assistance include, among other things, that the financial assistance is provided on fair (market) conditions and, in case of a joint stock company, that the company creates a special reserve fund in the amount of the financial assistance provided. These conditions are difficult to satisfy and the provision of financial assistance is therefore in practice avoided whenever possible. The risk is amplified by the fact that financial assistance provided in breach of applicable laws and regulations may in some cases be considered or declared invalid.

⁵ For example, the registration of mortgages with the land registry, and the registration of pledges over movable assets in the pledge register held by notaries etc.

Contacts



Michal Dušek

Senior Tax Adviser

Tel +420 222 107 159

michal.dusek@allenovery.com



Radek Novotný

Senior Tax Adviser

Tel +420 222 107 155

radek.novotny@allenovery.com

France

Transaction taxes

In this section we identify taxes that will be imposed on the vendor and the acquirer upon a transfer of assets or upon a transfer of shares, as well as other tax implications of a transfer of assets or shares.

STAMP DUTY ON THE TRANSFER OF SHARES

As from 1 August 2012, sales of shares (*actions*) in French corporations (*sociétés de capitaux*) other than companies whose assets mainly comprise real estate in France (**Real Estate Companies**) are subject to transfer taxes at the uncapped, flat rate of 0.1%, unless the market capitalisation of the company issuing the shares transferred exceeds EUR1 billion, in which case a financial transaction tax is applicable under certain conditions at the uncapped, flat rate of 0.2%.

Sales of participations in entities organised under the form of a partnership (*société de personnes*), other than Real Estate Companies, are subject to transfer taxes at a flat rate of 3%, without any cap but after application of a EUR23,000 allowance to be prorated, as the case may be, on the basis of the number of shares transferred.⁵

The following operations, however, are exempt from transfer tax:

- share buy-back programmes;
- transfers of shares or participations in an entity undergoing bankruptcy proceedings (*procédure de sauvegarde or redressement judiciaire*);
- transfers of shares or participations within the same French tax grouping (*groupe d'intégration fiscale*); and
- contributions of shares or participations constituting a full line of business within the meaning of the tax-deferral regime applicable to mergers and spin-offs.

Sales of shares in French-listed companies are subject to transfer taxes where a transfer deed has been executed (either in France or abroad; a tax credit being available in the latter case, to the maximum value of the transfer taxes due in France, in order to offset any transfer taxes paid abroad against the transfer taxes due in France).

Unless a transfer deed is executed in France, sales of shares or participations in a foreign entity which is not a Real Estate Company are not subject to any transfer taxes in France.

Sales of shares in a Real Estate Company are subject to a 5% transfer tax. The basis of such 5% transfer tax is equal to: (i) the fair market value of the real estate directly or indirectly held by the Real Estate Company; minus (ii) the debt liabilities pertaining to the acquisition of the relevant real estate (previously all debt liabilities used to be deductible for transfer tax purposes); plus (iii) the fair market value of all other assets.⁶

CAPITAL DUTY ON CONTRIBUTION OF CAPITAL

No capital duty upon incorporation of a company.

EUR375/EUR500 in the event of cash contributions during the life of the company:

- EUR375, if the share capital is less than EUR225,000 after such a contribution.
- EUR500, if the share capital is more than EUR225,000 after such a contribution.

REAL ESTATE TRANSFER TAX

5.09% (plus a 0.1% land registry fee) temporarily increased up to 5.81% in certain French *départements* (in respect of sales occurring between 1 March 2014 and 29 February 2016) of the transferred asset's value.

In addition, notary fees and other ancillary costs are payable at a rate of approximately 1% to 1.5%, depending on the size of the transaction.

A reduced rate of 0.715% (plus notary fees) may apply, particularly where the buyer makes the commitment to resell within a five-year period or with respect to sales of recently completed properties.

⁶ No administrative guidelines have been released yet. Numerous questions arise, eg, in the case of a double tier structure (sale of Holdco owning Propco) in terms of avoiding certain items being included twice in the tax basis (eg the value of Propco shares should be eliminated).

CAPITAL GAINS TAX ON THE SALE OF ASSETS

33.33% (increased, after surcharge, to 34.43% for companies with a turnover exceeding EUR7.6m, and to 38% for companies with a turnover exceeding EUR250m), corresponding to the standard corporate tax rate; or 15% (increased, after surcharge, to 15.5% for companies with a turnover exceeding EUR7.6m, and to 17.10% for companies with a turnover exceeding EUR250m) for patents and assimilated intellectual property rights, subject to the seller and the purchaser not being affiliated and to specific anti-avoidance measures.

CAPITAL GAINS TAX ON THE SALE OF SHARES

Corporate vendor

Capital gains tax on the sale of shares in a non-Real Estate Company:

- Capital gains arising from the transfer of a significant interest (*titres de participation*) are 88% exempted under the French participation-exemption regime (ie, 12% of the gain is taxable; it being noted that capital losses may not be offset) provided the interest was effectively booked as such and was held by the vendor for at least two years prior to the sale.
- Capital gains arising from the transfer of a venture capital interest (*titres de capital risque*, namely shares in *Fonds Communs de Placement à Risques* or *Sociétés de Capital Risque*) are exempt in proportion to the assets qualifying as significant interest (*titres de participation*) and subject to a 15% tax for the surplus (plus surcharge, if applicable) provided such interest was held by the vendor for at least five years prior to the sale.
- Capital gains arising from the transfer of other types of shares are subject to corporate income tax at the standard rate (plus surcharge, if applicable).

Capital gains tax on the sale of shares in a Real Estate Company:

- Capital gains arising from the transfer of shares in a listed Real Estate Company, such as a SIIC (*Société d'Investissements Immobiliers Cotée*, the REIT-like French structure) regime are subject to a 19% tax (plus surcharge, if applicable) provided such shares qualify as a significant interest and were held by the vendor for at least two years prior to the sale.
- Capital gains arising from the transfer of shares in a non-listed Real Estate Company are subject to corporate income tax at the standard rate (plus surcharge, if applicable), notwithstanding their holding period.

Individual vendor

Capital gains realised by individual vendors are subject to personal income tax in accordance with the standard progressive scale (ie, up to a marginal 45% rate, to which a 3% additional contribution may be added on any income and gains above EUR250,000 (EUR500,000 for taxpayers filing joint returns), increased to 4% for any income and gains above EUR500,000 (EUR1m for taxpayers filing joint returns)) and to social levies at the current rate of 15.5% for the amount corresponding to the difference between the net proceeds of the share disposal and their acquisition (or subscription) price (it being noted that a set fraction of the gains should not be taxable for personal income tax purposes only if a certain holding period is satisfied (50% for a two-year holding period, 65% for an eight-year holding period)).

An enhanced allowance applies to: (i) sales of shares in small- and medium-sized enterprises created less than ten years before the disposal; (ii) sales of shares to a family member; and (iii) sales of shares by a retiring manager (to whom an additional EUR500,000 fixed allowance would apply). The enhanced allowance adds up to 50% for a holding period comprised between one and four years, 65% for a holding period comprised between four and eight years and 85% for an eight-year holding period.

Capital gains arising from the transfer of shares in certain types of Real Estate Company are further subject to specific tax regimes.

AVOIDANCE OF CAPITAL GAINS TAX

Capital gains realised by a company upon merger, demerger, partial business transfer, contributions and exchange offers (*offres publiques d'échange*) may benefit from a tax deferral by rolling over the taxable gain provided, in certain circumstances, an undertaking to retain the shares issued in consideration for a three-year period.

In addition, a rollover may also be possible (subject to certain conditions) for an intra-group transfer of assets (ie, the transfer of assets between two companies that are members of the same tax group).

PRESERVATION OF TAX LOSS CARRY-FORWARD

The disposal of the entire share capital of a company does not entail the cancellation of such company's losses. These losses remain available for carrying forward to the extent that the activities of the company do not materially change following the disposal.

Applicable to fiscal years closed as from 4 July 2012, several tests have been defined in order to limit the possibility to preserve tax losses:

- There is a deemed liquidation in the case of a closing down (*disparition*) of such production means as are necessary for the going concern for a period of over 12 months (except in a case of *force majeure*) or when the closing down is followed by the transfer of a majority of the shares of the company.
- The change of activity would be characterised, for a given company, upon:
 - the addition of an activity that would lead, with respect to either the financial year of its incidence or the following financial year, to an increase (in comparison with the financial year preceding such addition) of more than 50% of either the company's turnover or both: (i) the average workforce of the company; and (ii) the gross amount of the company's fixed assets; or
 - the closing down or transfer (even partially) of an activity that would lead, with respect to either the financial year of its incidence or the following financial year, to a decrease (in comparison with the financial year preceding such closing down or transfer) of more than 50% of either the company's turnover or both: (i) the average workforce of the company; and (ii) the gross amount of the company's fixed assets.
- It is possible to avoid the deemed liquidation/change of activity by obtaining a ruling from the tax authorities, which would be conditional upon economic or business motivations or considerations linked to preservation of the activity (that generated the tax losses) and employment.

With respect to mergers, demergers and partial business transfers realised under a tax-deferral regime, the losses of the company that is merged or whose business is contributed may be transferred to the absorbing/beneficiary company subject to obtaining a ruling from the French tax authorities. The tax authorities must grant the ruling when certain conditions are met.

Corporate taxpayers may carry back their tax losses for only one year and carry forward the same without limit provided however that for any given financial year, the portion of the imputable carry-forward loss may not represent more than 50% of the taxable profits in excess of EUR1m of such financial year (ie, at least 50% of such profits are taxable), the non-imputable loss being carried forward to the following years.

NON-RESIDENT VENDORS

Corporate vendor

Capital gains tax on the sale of shares in a Real Estate Company:

Subject to a tax treaty providing otherwise, capital gains arising from the transfer of such shares are taxed at the standard corporate income tax rate of 33.33% (plus surcharge, if applicable). This rate is brought to 75% if the vendor is domiciled, established or incorporated in a non-cooperative State or territory.

Capital gains arising from the transfer of shares in a listed Real Estate Company regime (such as SIIcs) are, however, subject to a 19% tax (plus surcharge, if applicable) provided such shares: (i) qualify as a significant interest; (ii) have been held by the vendor for at least two years prior to the sale; and (iii) are transferred by an entity resident in an EU Member State.

Capital gains tax on the sale of shares in a non-Real Estate Company:

Subject to a tax treaty providing otherwise, these capital gains are subject to tax at the rate of 45% where the shareholder holds or has held, directly or indirectly, at any time during the preceding five-year period, 25% or more of the share capital of the company the shares of which are transferred. This rate is brought to 75% if the vendor is domiciled, established or incorporated in a non-cooperative State or territory. No tax should be levied on capital gains if this ownership test is not met.

Individual vendor

Capital gains tax on the sale of shares in a Real Estate Company:

Subject to a tax treaty providing otherwise, capital gains arising from the transfer of such shares are taxed at the standard 33.33% rate (plus social levies at a rate of 15.5%), or 19% (plus social levies at a rate of 15.5%) where the taxpayer is an EU resident or a resident of Iceland, Liechtenstein or Norway. The income tax rate is brought to 75% if the vendor is domiciled, established or incorporated in a non-cooperative State or territory (plus social levies).

In addition, again subject to tax treaty provisions, with respect to real estate assets other than building plots, capital gains in excess of EUR50,000 suffer another specific surtax, the rate of which can reach 6% (when the capital gain exceeds EUR260,000).

Capital gains tax on the sale of shares in a non-Real Estate Company:

Subject to a tax treaty providing otherwise, such capital gains are taxed at the rate of 45% where the shareholder (together with his/her family) holds or has held, directly or indirectly, at any time during the preceding five-year period, 25% or more of the share capital of the

company the shares of which are transferred. This rate is brought to 75% if the vendor is domiciled, established or incorporated in a non-cooperative State or territory. No tax should be levied on capital gains if this ownership test is not met.

SPIN-OFFS (DEMERGER RELATED TO 50% CHANGE IN CONTROL TRANSACTION)

The transfer of the control of a company does not trigger the termination of the business activity and therefore does not trigger consequences other than those mentioned above.

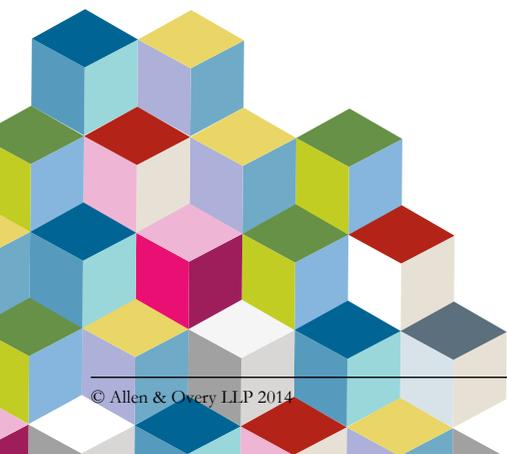
Subject to detailed rules, a spin-off (demerger) may be tax-free to the distributing corporation and the recipient shareholders.

VALUE ADDED TAX

Transfers of assets may be subject to value added tax (**VAT**).

The transfer of a branch in the context of mergers and contributions, to the extent that such branch constitutes a universality of assets, is VAT-exempt.

Certain transfers of real estate assets may be subject to VAT (eg, for constructions completed less than five years prior to their sale).



Opportunities and threats

In this section an overview is provided of opportunities to maximise relief for acquisition costs (such as financing costs), as well as other items which require attention when designing an efficient tax structure.

STEPPING-UP ASSET VALUES

The allocated portion of the purchase price of assets can be treated as the basis for depreciation and capital gains tax.

No amortisation of goodwill is possible (except in very limited circumstances); conversely, amortisation of certain intangible assets (eg patents) may be obtained if it can be evidenced that the benefit the intangible asset has for the company will cease at a certain date.

Acquisitions through share deals typically do not allow step-up of the tax basis of the assets of the target company, except with respect to partnerships (tax flow-through entities) for which, under certain circumstances, a tax-free step-up might be achieved.

TAX CONSOLIDATION RULES

Formation of a tax grouping for corporate tax purposes is possible for 95%-owned French subsidiaries, French branches of 95%-owned foreign subsidiaries and 95%-owned French subsidiaries of 95%-owned EU subsidiaries (provided certain other requirements are met).

Such tax grouping is conditional upon an election by the relevant companies and triggers the application of a specific tax regime, the philosophy of which is to deem and treat the entities belonging to the tax group as one for tax purposes.

DEBT/EQUITY RULES

As a general principle, interest paid to a direct shareholder is not fully deductible where:

- the borrowing company's share capital has not been fully paid up;
- the interest rate exceeds the average commercial lending rate offered by banks for two-year loans (eg, 2.79% for 2013);
- the lender, if affiliated with the French borrower, is subject to an income tax equal to at least 25% of the income tax determined under standard French tax rules upon the interest received from such borrower;
- more generally, the financing has not been concluded in the interest of the borrowing company (the *acte anormal de gestion* theory).

Thin capitalisation rules, as implemented since 1 January 2007 and as amended in 2010, further apply to the extent that the lender and the borrower are affiliated within the meaning of French tax code article 39.12 (ie: (i) one owns, directly or through an intermediary person, the majority of the share capital of the other (or controls, *de facto*, the decision-making process within the latter); or (ii) they are both under the control (as defined in (i)) of a third entity).

Under these rules, the deductibility of interest paid to affiliated lenders is limited if all three of the following thresholds are exceeded:

- the aggregate borrowings of the borrower *vis-à-vis* affiliated entities exceed 1.5 times the amount of the borrower's equity (or share capital subject to certain conditions), either as at the beginning or as at the end of the financial year, at the company's election;
- the aggregate interest paid by the borrower to affiliated entities exceeds 25% of its current adjusted income (increased, *inter alia*, by certain items such as interest paid to affiliated entities and depreciation);
- the amount of interest paid by the borrower to affiliated entities exceeds the amount of interest received from affiliated entities.

If all three of these thresholds are exceeded, the fraction exceeding the most favourable threshold is not tax-deductible (unless it amounts to less than EUR150,000). Such fraction may, however, be deducted from the taxable income of the following years, with a discount of 5% per year, subject to the limitation mentioned in the second threshold above. Also, the above limitations would not apply if the borrower could show that the debt/equity ratio of the group to which it belongs is equal to or higher than its stand-alone debt/equity ratio. Applicable to financial years ended as of 31 December 2010, the thin capitalisation rules also cover interest payments made in respect of loans provided by non-affiliated entities, to the extent that such loans are guaranteed by an affiliated entity. Such extension, however, does not apply to: (i) public offerings of bonds; (ii) loans guaranteed exclusively (besides the securities granted by the borrower itself) by a pledge of a borrower's shares or claims, or the shares of the entity owning, directly or indirectly, the borrower if both the borrower and such entity belong to the same French tax group; (iii) loans put in place as a result of the repayment of a prior financing which itself is the mandatory consequence of the change of control of the borrower;

(iv) financings contracted before 1 January 2011 as part of leverage buy-out transactions (or their refinancings); or (v) refinancings which have been made mandatory as a result of the opening of safeguard or bankruptcy proceedings.

The thin capitalisation rules are also applicable within a French tax grouping, at the level of each member of the tax grouping (except for the carry-forward of the non-deductible portion, which is to be deducted at the level of the head of the tax grouping). However, if the aggregate amount of the non-deductible interest, computed at the level of each member, is higher than the difference between the aggregate interest paid by the tax grouping members to affiliated entities (which do not belong to the tax grouping) and 25% of the tax-consolidated group's current taxable income (increased, *inter alia*, by such interest and decreased by dividends received from a tax grouping member), then such difference is deductible at the level of the head of the tax grouping; the portion which is non-deductible is then carried forward at the tax grouping level, with a discount of 5% per year and subject to a limit of 25% of the tax grouping taxable income.

A general limitation of interest expenses deduction must also be applied once the above-mentioned limitations have been taken into account: the amount of financing expenses (as defined below) incurred by a company that is not a member of a French tax group must be added back to its taxable result by an amount of 25% of the financing expenses. This applies to the extent the company's financing expenses exceed EUR3m in the relevant fiscal year. Financing expenses are defined as financing costs net of financial income. The limitations apply only to the portion of the financing expenses that have not been already disallowed under other interest deductibility limitations. For companies that are members of a French tax group, the EUR3m threshold is calculated at the level of the tax group, and the financing expenses subject to the limitations thus are the aggregate of each company's financing expenses that are: (i) due on loans that were granted by companies outside the tax group; and (ii) not already disallowed in respect of another interest deductibility limitation.

OTHER DISALLOWED AND DEFERRED INTEREST

The general interest rate limitation mentioned above (ie, the average commercial lending rate offered by banks for two-year loans) applies to any loans, whether granted by affiliated entities or not. However, with respect to financings provided by affiliated entities within the meaning of FTC article 39.12, the maximum deductible rate is the one that the borrower could have obtained from an independent financial institution under similar circumstances, if higher.

In the event of a French tax grouping being set up, an anti-avoidance provision referred to as *Amendement Charasse* may also apply. This provision denies the deduction of (part of) the interest charge⁷ borne by a tax grouping with respect to the acquisition, by a member of the tax grouping, of shares in another member of the tax grouping that were previously held by an entity (or an individual) which ultimately controls the tax grouping.

⁷ The head of the tax grouping will be required to add to the tax grouping's taxable profits a portion of the interest that is deemed to correspond to the financing cost of the shares acquired (such portion amounting to the ratio between the acquisition cost of the shares and the average indebtedness of the tax grouping).

Applicable since 2012, the deduction of the interest charge borne by a corporate taxpayer with respect to the acquisition of a participation that is eligible for the French participation-exemption regime (ie 88% exemption of the capital gains – please see “Capital gains tax on the sale of shares” on page 46), may further be restricted if such corporate taxpayer is not able to provide evidence that: (i) the decisions related to such participation are effectively taken by such corporate taxpayer (or by another French entity that is either: (a) controlled by; or (b) placed under the control of the same third entity); and (ii) when a control or an influence is exercised within the entity in which the participation is purchased, such control or influence is exercised either by the corporate taxpayer that purchased the participation (or another French entity it is either: (a) controlled by; or (b) placed under the control of the same third entity).

If such evidence is not provided, no deduction would take place in respect of the financial year(s) during which the evidence was required to be provided and in respect of the financial years closed during the following eight years. However, such restriction should not apply when: (i) the aggregate value of the participations held by the relevant corporate taxpayer is less than EUR1m; (ii) the acquisition was not financed by borrowings borne either by the relevant corporate taxpayer or by another entity of the group to which it belongs; or (iii) the debt-to-equity ratio of the group the relevant corporate taxpayer belongs to is higher than such corporate taxpayer's debt-to-equity ratio.

CONSEQUENCES OF GUARANTEES FROM A RELATED PARTY FOR THIRD PARTY DEBTS

Thin capitalisation rules also cover interest payments made in respect of loans provided by non-affiliated entities, to the extent that such loans are guaranteed by an affiliated entity.

Such extension, however, does not apply to: (i) public offerings of bonds; (ii) loans guaranteed exclusively (besides the securities granted by the borrower itself) by a pledge of a borrower's shares or claims, or the shares of the entity owning, directly or indirectly, the borrower if both the borrower and such entity belong to the same French tax grouping; (iii) loans put in place as a result of the repayment of a prior financing which, itself, is the mandatory consequence of the change of control of the borrower; (iv) financings contracted before 1 January 2011 as part of leveraged buy-out transactions (or their refinancings); or (v) refinancings which have been made mandatory as a result of the opening of safeguard or bankruptcy proceedings.

Up until such extension, guarantees by affiliated entities for third party debts have no consequences.

ANTI-HYBRID LOANS PROVISION

As from fiscal years ending on or after 25 September 2013, the deductibility of interest paid to an affiliated lender by a French borrower is subject to a minimal taxation requirement at the Lender's level.

The interest deduction will be possible only to the extent that the French borrower demonstrates, upon request from the French tax authorities, that the lender is subject to an income tax equal to at least 25% of the income tax determined under standard French tax rules upon the interest received from such borrower. For lenders which are resident or established outside of France, the minimal taxation requirement is assessed by the determination of the income tax liability that the lender would incur on the interest income in France if it were a resident of, or established in, France.

Where the lender is a French pass-through partnership or a French collective investment scheme referred to in articles L.214-1 to L.214-191 of the French monetary and financial code (including, among other things, UCITs, AIFs as well as other collective investment schemes such as SICAVs and SPPICAVs with a single shareholder) or an equivalent vehicle located in the European Union or in a State that has entered into an exchange of information or administrative assistance treaty with France other than non-cooperative jurisdiction, the deductibility limitation only applies to the extent such vehicle is directly or indirectly controlled by a share/unit holder or by a group of share/unit holders. In that case, the "subject to tax" condition is determined at the level of such share/unit holder or group of holders.

TAX CREDIT OR EXEMPTION TO AVOID DOUBLE TAXATION

Corporate investor

The participation exemption relief provides that only 5% of the amount of dividends received is taxable provided certain conditions are met, such as:

- the parent company owns at least 5% of the voting and financial rights of the company; and
- the parent company holds the shares for at least a two-year period (should the shares be sold during this period, the parent would have to pay back to the French tax authorities the exempted tax, plus interest for late payment).

Individual investor

Residents of France for tax purposes are subject to income tax at the standard progressive rate (ie, up to a marginal 45% rate, to which may be added a 3% additional contribution on any income and gains above EUR250,000 (EUR500,000 for taxpayers filing joint returns), increased to 4% for any income and gains above EUR500,000 (EUR1m for taxpayers filing joint returns)) on dividends received, the taxable amount of which being calculated as follows:

- reduction, subject to certain conditions, to 60% of the dividend paid by a distributing company which has its registered address in France, in an EU Member State or in a country with which France has signed a double taxation treaty (including any tax credit attached thereto); and
- deduction of any fees charged for the acquisition and custody of this income.

Subject to certain conditions, a 21% withholding tax is further applicable on the gross amount of the dividends distributed where the beneficiary is a resident of France for tax purposes (it being noted that such withholding tax may subsequently be offset against the amount of income tax eventually due, or reimbursed to the extent it would exceed the amount of income tax eventually due). Where the entity paying out the dividends is not situated in France, the burden of such withholding tax (the payment of which having to take place within the first 15 days of the month following the month of the payment of the dividends) is on the beneficiary (unless the paying entity is appointed to do so on his behalf). Foreign tax credits, if any, may not be offset against the 21% withholding; but they should be offsettable in accordance with generally applicable rules upon determination of the final French personal income tax to be paid.

In addition, residents of France for tax purposes are subject to social levies at the rate of 15.5%.

CONTROLLED FOREIGN COMPANY LEGISLATION

The Finance Bill for 2005 introduced controlled foreign company (**CFC**) rules that apply as of 1 January 2006, in response to French case law holding the former CFC rules to be incompatible with various tax treaties signed by France and with article 43 of the EU Treaty.

Scope of the CFC rules

If a French company that is subject to corporate tax in France and directly or indirectly has a permanent establishment or holds a participation of more than 50% in a subsidiary (whatever its form) in a low-tax jurisdiction, taxable profits would be attributed to, and assessed on, the company in France in respect of the profits of the permanent establishment or pro rata to the company's participation in the subsidiary. The 50% threshold retained for the shareholding will be reduced to 5% if more than 50% of the shares of such subsidiary are held by: (i) companies established in France; or (ii) related entities of the French company. These taxable profits are either imposed as a profit (when deriving from a branch) or as distributed income (when deriving from the subsidiary).

A low-tax jurisdiction is defined as a jurisdiction which subjects profits to tax at 50% or less compared with the French tax that would have been assessed on the profits.

The profits subject to the CFC rules only include passive investment income (eg dividends, interest and royalties) and income from intra-group service activities (eg in respect of holding and financial activities).

Double taxation relief and safe harbour

The foreign tax due on the profits falling within the CFC rules is credited against the corresponding French tax. As a safe harbour, the new CFC rules would not apply if the French company could prove that the localisation of the permanent establishment or subsidiary was not motivated by tax reasons. Within the European Union, only artificial structures would be penalised under French CFC rules.

PASSIVE FOREIGN INVESTMENT COMPANY ANTI-DEFERRAL REGIME

If an individual domiciled in France has a direct or indirect participation of at least 10% (whatever its form) in a foreign financial entity (companies, funds, trusts, or other similar entities) established in a low-tax jurisdiction (same definition as in the “Scope of the CFC rules” above), taxable profits of such entity are attributed for 125% of their amount to the individual’s taxable income, pro rata to its participation in the entity.

The assets of such foreign financial entity must be mainly composed of securities, receivables, deposits and currency accounts for such foreign financial entity to fall within the scope of the French passive foreign investment company (PFIC)-equivalent rules.

The foreign tax due on the profits falling within the French PFIC-equivalent rules is deductible from the corresponding taxable income in France.

TRANSFER PRICING

Transactions between French companies and foreign affiliates or companies located in low-tax jurisdictions or, as from fiscal years ending on or after 10 August 2014, companies located in a non-cooperative State or territory must be done on an arm’s length basis. If not, all profits indirectly transferred outside France may be added back to the French company’s taxable profits. The French tax authorities generally bear the burden of proof in demonstrating that profits have been indirectly transferred abroad. Once this proof is shown, the burden of proof is shifted to the taxpayer, who must show that the transaction was made on an arm’s length basis.

Specific transfer pricing documentation requirements are imposed on French companies whose turnover or total gross assets exceed EUR400m (directly or indirectly).

RESIDENCE

French tax law does not give any definition of the concept of residence for companies; only double tax treaties signed by France refer to the concept of residency. France applies the

territoriality principle to assess corporate tax, which means that companies are subject to corporate tax only on the profits derived from French sources.

ENTITY CLASSIFICATION (“CHECK-THE-BOX”) RULES

Not applicable.

TAXATION OF DISTRIBUTIONS RECEIVED FROM SUBSIDIARIES

Dividends and assimilated distributions received by a French company will be exempt from corporate income tax for 95% of their amount (a 5% fraction being in any case taxable) provided they qualify under the French participation-exemption regime (*régime des sociétés mères*), which, in particular, requires the holding of at least a 5% stake for a minimum of two years.

WITHHOLDING TAXES

Interest payments made by a French entity are not subject to any withholding taxes, unless: (i) they are made outside France in a non-cooperative State or territory (*Etat ou territoire non coopératif*, eight jurisdictions currently qualifying as such⁸); and (ii) the debtor cannot prove that the principal purpose and effect of the indebtedness was not that of allowing the payments of interest to be made in a non-cooperative State or territory. In such case, a 75% withholding tax may be imposed.

A 30% withholding tax (increased to 75% when made in a non-cooperative State or territory) is applicable to dividends and assimilated distributions, subject to: (i) the more favourable provisions of an applicable double tax treaty; and (ii) the general exemption dividends distributed to companies located within the EU (provided, *inter alia*, the holding of at least a 5% stake for at least a two-year period).

Applicable to distributions made from 17 August 2012; French or foreign entities that are subject to corporate income tax in France are subject to an additional tax amounting to 3% of the dividends (and deemed distributions) they distribute to their shareholders. Several types of entities are, however, not within the scope of such 3% tax (*inter alia* French flow-through partnerships for tax purposes, small-and medium-sized enterprises and certain collective investment schemes). Moreover: (i) dividends distributed by a company forming part of a French tax-consolidated group to another company forming part of the same French tax-consolidated group; (ii) dividends paid in the form of shares under certain conditions; (iii) dividends distributed by a company that has elected for the SIIC regime to companies that: (a) have also elected for the SIIC regime; and (b) hold the distributing company in accordance with certain conditions specific to the SIIC regime; and (iv) dividends distributed by listed companies having elected for the SIIC regime in order to satisfy their compulsory distribution requirements

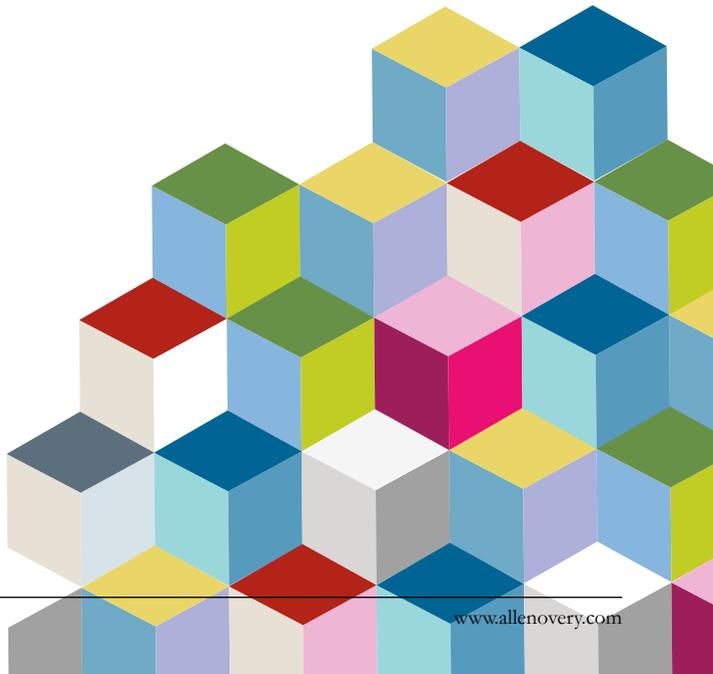
⁸ The list of non-cooperative jurisdictions for 2014 is as follows: Botswana, the British Virgin Islands, Brunei, Guatemala, the Marshall Islands, Montserrat, Nauru and Niue.

are also outside the scope of the 3% tax.

It should be noted that the 3% tax does not constitute a withholding tax but rather an additional corporate tax the distributing entity is liable for.

Likewise, the 30% French branch tax, imposed by way of a withholding tax on the profits the French branch of a foreign company is deemed to distribute: (i) may be reduced by the more favourable provisions of an applicable double tax treaty; and (ii) does not apply to French branches of companies located within the EU.

Payments of royalties (and some other fees) are generally subject to a 33.33% withholding tax (increased to 75% when made in a non-cooperative State or territory), save in cases where an exemption or a reduction is available under a double tax treaty or under the provisions implementing the EU Interest/Royalties Directive (a condition of which being that the payment is made between 25%-affiliated companies).



Other

This section describes other opportunities and threats that should be taken into account when structuring tax-efficient mergers and acquisitions.

ANTI-ABUSE REGULATIONS

The *abus de droit* theory is comparable to the “substance over form” analysis that exists in other jurisdictions. It enables the French tax authorities to disregard or re-characterise a transaction that is either: (i) fictitious; or (ii) by seeking the benefit of a literal application of texts or decisions against the initial objectives pursued by their authors, inspired by no other reason than to avoid or reduce the tax burden which would have been borne otherwise by the taxpayers had such transaction not been entered into.

Where the French tax authorities are successful in evidencing that an *abus de droit* has been committed, it can reassess the tax that has been avoided and claim interest for late payment and also a 40% penalty (increased to 80% should the tax authorities be able to provide evidence that the taxpayer either was the main initiator of the transaction which is subject to the recharacterisation or was its main beneficiary).

ATTRIBUTION OF CHARGEABLE GAINS OF COMPANIES

Not applicable.

TAXATION OF EMPLOYEES' AND DIRECTORS' EQUITY INCENTIVES

In the context of stock options granted to employees and directors domiciled in France, the favourable tax regime (it being noted that, applicable to incentives granted as from 28 September 2012, such favourable regime is essentially limited to: (i) lower rates for social security contributions; and (ii) a tax deferral for certain gains) may remain applicable despite certain operations (exchange offers (*offre publique d'échange*), mergers, demergers). In other words, the period during which the shares (obtained after the option is exercised) must be held in order to benefit from the favourable tax regime is not considered as interrupted by the event affecting the granting company.

In the context of allocation of free shares granted to employees and directors domiciled in France, such tacking of the holding period does not currently exist for the purposes of the application of the favourable tax regime.

TEMPORARY TAX ON HIGH REMUNERATIONS

Companies and other entities which carry on a business in France are subject to an exceptional tax on high remunerations awarded in 2013 and 2014. This tax is based on the portion of individual remunerations (ie the sum of the gross amounts of, *inter alia*, wages, salaries, assimilated revenues, cash benefits, benefits in kind, attendance fees, pensions, pension supplements, compensation, allowances or benefits relating to retirement, sums relating to profit-sharing schemes, stock options and free shares) which exceeds EUR1m.

The tax rate is 50% but the amount of the tax is capped at 5% of the company's turnover realised in the year in which the tax is due.

Contrary to the computation of the corporation tax, the solidarity tax is not deductible from the taxable result for the calculation of the exceptional contribution on corporation tax.

This tax will be payable in 2014 for remunerations awarded in 2013 and in 2015 for remunerations awarded in 2014.

TIMING OF TAX RELIEF FOR INTEREST COSTS

Deductibility of interest when accrued.

INTEREST TAX RELIEF UTILISATION

Not applicable.

HIVE-UPS

If tax grouping is not possible, it may be worth considering moving a taxable source of income up into a company in the structure which bears the relevant costs, typically by way of an upstream merger. However, this may raise certain financial assistance issues and, from a tax perspective, upstream mergers are scrutinised by the French tax authorities.

ACQUISITION STRUCTURE

Typically, structuring a French acquisition for non-French residents will involve setting up a French holding company and implementing a French tax group. However, other structures, such as the use of a non-resident acquisition vehicle, might prove more efficient in certain scenarios, in particular for real estate investments.

FINANCIAL ASSISTANCE

Under the French Company Act, a French SA, SCA or SAS cannot advance funds, grant loans or grant security in respect of the subscription or purchase of its own shares by a third party. There must also be a genuine and tangible consideration (corporate benefit) for a French company to grant a security interest over its assets, to secure its own debt or to guarantee or secure the obligations of a related company.



Contacts



Jean-Yves Charriau

Partner

Tel +33 1 40 06 53 60
jean-yves.charriau@allenoverly.com



Mathieu Vignon

Partner

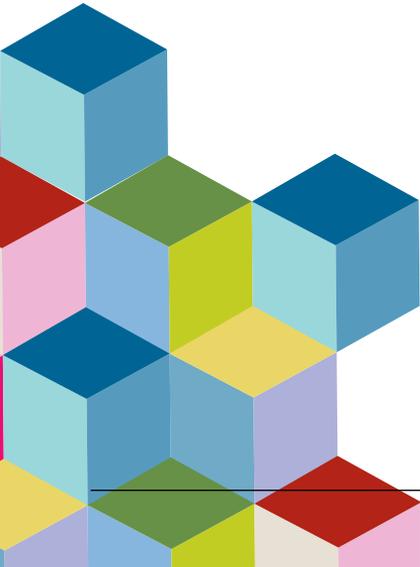
Tel +33 1 40 06 53 63
mathieu.vignon@allenoverly.com



Sophie Maurel

Counsel

Tel +33 1 40 06 53 72
sophie.maurel@allenoverly.com



Germany

Transaction taxes

In this section we identify taxes that will be imposed on the vendor and the acquirer upon a transfer of assets or upon a transfer of shares, as well as other tax implications of a transfer of assets or shares.

STAMP DUTY ON THE TRANSFER OF SHARES

None.

CAPITAL DUTY PAID ON THE CONTRIBUTION OF CAPITAL

None.

VALUE ADDED TAX

A transfer of assets is generally subject to value added tax (**VAT**) at a rate of 19%. Depending on the type of asset, the reduced rate of 7% or an exemption from VAT may apply. However, if the asset transfer qualifies as a transfer of a business as a going concern (*Geschäftsveräußerung im Ganzen*), it will not be subject to VAT. Transfers of shares in a corporation or interests in a partnership may either qualify as a transfer of a business as a going concern or as being exempt from VAT.

REAL ESTATE TRANSFER TAX

Real estate transfer tax (**RETT**) is imposed on the direct acquisition of German real estate, eg in an asset deal, but may also apply in a share deal where the target entity, or any of its subsidiaries, owns German real estate. If 95% or more of the shares in a company or interests in a partnership are transferred, directly or indirectly, to an acquirer or acquiring entities of the same group, this will generally be subject to RETT. RETT will also be imposed on a partnership

owning German real estate if, within five years, 95% or more of the partnership's interests are transferred to new partners.

The applicable RETT rate depends on the federal state where the transferred real estate is located. Currently, tax rates range from 3.5% to 6.5%. In an asset deal, the tax is computed from the portion of the overall purchase price allocable to the sold real estate. In a share deal, the standardised tax value of the real estate held by the target entity forms the tax base, which is generally a little lower than the fair market value.

Acquisition structures to avoid or mitigate RETT in a transaction are available but require careful structuring, in particular in light of reinforced legislation aiming to disallow certain of these structures. It is important to note that RETT generally already falls due on the signing of a sale and purchase agreement so that any structuring needs to take place before signing.

CAPITAL GAINS TAX ON THE SALE OF ASSETS (OTHER THAN SHARES)

Corporate vendor

A capital gain from an asset sale will be subject to corporate income tax at a rate of 15% (plus a solidarity surcharge of 5.5% thereon, giving a total of 15.825%). In addition, trade tax will apply to the gain at a rate of 7% to 17.5% depending on the municipality/municipalities in which the vendor conducts its business. Typically, the overall tax charge will be in the range of 29% to 32%. Generally, no German tax will apply to assets attributable to foreign branches in countries with which Germany has a double taxation treaty.

Individual vendor

A capital gain realised by an individual will be taxed at the personal income tax rate of the vendor. The rates are progressive and range from 14% to 45% (plus a solidarity surcharge of 5.5% thereon and, where applicable, church tax at a rate of 8% or 9% of the income tax). The capital gain will also be subject to trade tax, unless the transferred assets qualify as an entire business (*Betrieb*) or as a branch of activity (*Teilbetrieb*). Where trade tax applies, it will be charged at a rate of 7% to 17.5% depending on the municipality/municipalities in which the vendor conducts its business but will (at least to a large extent) be credited against the personal income tax of the vendor. An individual at the age of 55 years or more may invoke an alleviation to reduce income tax rates on the portion of the capital gain that is not in excess of EUR5 million to 56% of ordinary rates. The alleviation is granted only once in a lifetime.

CAPITAL GAINS TAX ON THE SALE OF SHARES

Corporate vendor

In general, 95% of the capital gain from the disposal of shares in a corporation is effectively exempt from corporate income tax and trade tax (the capital gains exemption). The remainder

is taxed at the rates indicated above for asset deals. Shares received in the course of not fully taxable business reorganisations are not eligible for the capital gains exemption until seven years after the reorganisations have elapsed (the **gain recognition rules**).

The gain from a disposal of interests in a partnership is fully taxable even though the capital gains exemption applies on a “look through” basis to the extent the partnership holds shares in corporations. Corporate income tax will apply at the level of the vendor and trade tax at the level of the partnership. The overall tax charge is similar to that of an asset deal.

Individual vendor

60% of capital gains from the disposal of shares in a **corporation** are subject to personal income tax (plus a solidarity surcharge and, where applicable, church tax) and to trade tax if the shares form part of the assets of a trade or business. The rates are the same as mentioned above for asset sales, and trade tax is (at least to a large extent) credited against the personal income tax of the vendor. Income tax at progressive rates of 14% to 45% (plus a solidarity surcharge and, where applicable, church tax) applies to 60% of the capital gain where the shares are not held as assets of a trade or business but the vendor or its predecessor held 1% or more of the shares in the corporation at any point in time during the five years preceding the disposal. In all other cases, generally the full gain will be subject to personal income tax at a flat rate of 25% (plus a 5.5% solidarity surcharge and, if applicable, church tax).

The gain from a sale of interests in a **partnership** is fully subject to personal income tax at the level of the vendor at the above rates even though the partial capital gains exemption applies on a “look through” basis to the extent the partnership holds shares in corporations. Trade tax will apply at the level of the partnership at the rates indicated above, unless the vendor as an individual has held the partnership interest directly. Where trade tax applies, it is largely creditable against personal income tax.

Special rules

Special rules apply to both individual and corporate vendors in the financial and insurance industries and to disposals by certain holding companies. In these cases, the gain may be fully subject to tax. The same may be true if the shares have been acquired in a reorganisation that has benefited from rollover relief.

FOREIGN VENDOR

Capital gains from an asset deal or from the disposal of a partnership interest derived by non-residents of Germany are subject to German income tax and, with some exceptions for individuals, trade tax at the rates indicated for residents above. Gains from the sale of shares in a German corporation are subject to German personal income tax if they are attributable to a German trade or business of the vendor (permanent establishment or permanent agent) or if the non-resident has held 1% or more of the shares at any point in time during the five years preceding the disposal. Only 5% of the gains will be subject to German corporate income tax

if a foreign corporation sells German shares. Trade tax only applies if the asset disposal is effectively connected with a trade or business conducted through a German permanent establishment. For individuals, similar rules as indicated for residents above apply. Under many of the German double taxation treaties, Germany does not tax gains from the disposal of shares in corporations if the non-resident vendor (corporation or individual) is a resident of the other treaty country. Special rules may apply in this regard for shares in real estate holding companies.

AVOIDANCE OF CAPITAL GAINS TAX

Rollover relief may be available to both shareholders and companies involved in statutory mergers, contributions in kind and certain other reorganisations covered by the Merger Tax Act. Tax optimisation for asset deals and disposals of partnership interests may be available in certain cases through a pre-sale restructuring.

PRESERVATION OF TAX LOSSES

If, within five years, an acquirer, related acquirers or unrelated acquirers acting in concert acquire, directly or indirectly, more than 50% of the shares in a corporation, the corporation's tax losses for corporate income tax and trade tax purposes will generally cease to exist. Accordingly, where more than 25% but no more than 50% of the shares are so acquired, the tax losses become unavailable on a proportionate basis. This will affect tax losses carried forward and current year tax losses up to the time of the transfer and applies to losses for corporate income and trade tax purposes.

An exception to this rule applies to the extent that the corporation whose shares are transferred has taxable built-in gains (*stille Reserven*). The losses will survive the share transfer up to the amount of such built-in gains. However, this may not represent a solution if the target is a holding company and the parent of a tax consolidated group. In this case, the losses will have accumulated at the parent level but the parent does not have any material built-in gains that are taxable given that the gain from a sale of the subsidiary shares would be 95% tax-exempt.

The tax losses will also become unavailable in an intra-group reorganisation, unless the transferor and the transferee of the shares are 100%, directly or indirectly, owned by the same person.

Trade tax losses of a partnership will not survive the transfer of a partnership interest but will cease to exist generally on a proportionate basis. Trade tax losses of a partnership will also be extinguished if the partnership materially changes its business activities.

Losses surviving the change in ownership can be carried forward indefinitely. However, the use of loss carry-forwards is limited. They will only be applied in full against the first EUR1m of taxable income. Only 60% of the income exceeding EUR1m can be offset by tax losses carried forward. The remaining 40% will be subject to income tax and trade tax at regular rates (minimum taxation).

Opportunities and threats

In this section an overview is provided of opportunities to maximise relief for acquisition costs (such as financing costs), as well as other items which require attention when designing an efficient tax structure.

STEPPING-UP ASSET VALUES

The purchase price in an **asset deal** will first be allocated to the tangible and intangible assets acquired up to the amount of their fair market value. Any portion of the purchase price exceeding the fair market value of the assets will be allocated to goodwill. The stepped-up values of the assets and the goodwill form the basis for depreciation and amortisation for tax purposes. The allowable deduction will depend on the remaining useful life of the assets according to tax depreciation schedules. Goodwill will be amortised over 15 years.

Similar rules apply to the acquisition of a **partnership interest**. The purchaser will be allowed to step up the tax basis of its pro rata share in the partnership's assets and goodwill, respectively, and to claim depreciation or amortisation deductions from the stepped-up basis.

The acquisition of shares in a **corporation** does not give rise to a step-up in the basis of the corporation's assets and goodwill.

TAX CONSOLIDATION RULES

To set off profits of the target corporation against expenses or losses of its parent, a tax-consolidated group needs to be established for corporate income tax and trade tax purposes.

Corporations having their corporate seat within the EU or the EEA and their principal place of business in Germany can be included as affiliates in a tax-consolidated group (*Organschaft*) of a common parent. Corporations not meeting this requirement and partnerships cannot be included.

The parent of a tax-consolidated group must be a corporation that is tax-resident in Germany or the German branch of a foreign corporation or a commercial partnership having its principal place of management and control in Germany. In each case, the shareholding in the affiliate must be attributable to a German permanent establishment of the parent.

To establish a tax-consolidated group, the parent must hold, directly or indirectly, the majority of the voting rights in the affiliate during the affiliate's entire fiscal year. In addition, the parent

and the affiliate must enter into a profit and loss pooling agreement (**PLPA**) with an initial term of at least five calendar years. The PLPA must provide for the parent compensating the affiliate for any losses incurred and must be registered in the commercial register prior to the end of the affiliate's fiscal year for which the PLPA shall apply for the first time.

Where a tax group has been established for corporate income and trade tax purposes:

- taxable income and losses of the parent and of all affiliates forming part of the tax-consolidated group will be pooled at the level of the parent;
- income will be reported at the affiliate level and then included in the parent's tax returns;
- in general, intra-group asset transfers are generally not disregarded but are taxable; however, certain double charges, eg trade tax on intra-group interest payments, may be avoided;
- intra-group distributions can be effected more tax-efficiently to the parent since the corporate income and trade tax on 5% of dividends received do not generally apply to profit allocations under a PLPA at the parent level; and
- tax losses of the affiliate incurred before it became a member of the tax group can be used neither at the parent level nor at the affiliate level while the tax group is in place.

DEBT/EQUITY RULES

Germany does not require a certain amount of minimum equity for tax purposes, although, in general, an equity amount of at least 10% of total assets is often recommended.

However, interest deductibility is limited under the interest ceiling rules (*Zinsschranke*). These limit the deduction of interest expenses for all businesses doing business in Germany that have an annual net interest expense (excess of interest expenses over interest income) of EUR3m or more.

The interest ceiling rules do not apply where an entity does not form part of a consolidated group and does not pay more than 10% of its net interest expenses to one or more shareholders holding more than 25% of its shares or parties related to such shareholders or to third parties having recourse against such shareholders or related parties.

Also, a business may escape the interest ceiling rules if it can show that its indebtedness (measured by equity over gross assets) does not exceed by more than 2% the indebtedness of the consolidated group of which it forms part. In computing the business's indebtedness certain adjustments will be made, eg the book value of shares in subsidiaries will be deducted from the business's equity. In principle, the consolidated group includes all entities that could be included in the consolidated accounts of the highest-tier parent entity under applicable accounting rules. This exception may, however, often be difficult to invoke since it is only available where the business further demonstrates that none of the group entities pays 10%

or more of its net interest expenses to shareholders outside the group holding more than 25% of the shares in the relevant group entity or to parties related to such shareholders or lenders with recourse against such a shareholder or related party.

In general, each company or partnership counts as a business for the purposes of the interest ceiling rules. However, a tax consolidated group is treated as a single business so that intra-group interest is eliminated for purposes of the interest ceiling rule and the EUR3m threshold is applied at the group level.

Where the interest ceiling applies, net interest expenses will be compared to the taxable EBITDA of the business. Taxable EBITDA is the taxable income plus the amount of interest expenses and any depreciation and amortisation deducted for tax purposes minus the amount of interest income. Tax-exempt income such as dividends received or income from foreign permanent establishments exempt under a double taxation treaty are not included. Net interest expenses in excess of 30% of the business's taxable EBITDA are not deductible but may be carried forward and used in later years where the net interest expense falls short of 30% of taxable EBITDA. A transfer of shares in an entity having an interest carry-forward may cause such carry-forward to cease to exist; similar rules as discussed under Tax Loss Preservation above apply. If 30% of the taxable EBITDA exceeds the net interest expense in a given year, the excess may be carried forward and may be applied against excess net interest expenses in any of the five subsequent years.

DISALLOWED AND DEFERRED INTEREST (OTHER THAN DEBT/EQUITY RULES)

From the deductible portion of the interest expenses after application of the interest ceiling rules, 25% is not deductible for trade tax purposes. This applies accordingly to other financing expenses such as losses from the sale of receivables, but also to lease rentals for movables, of which 5% is non-deductible, lease rentals for immovables (12.5% non-deductible) and royalties (6.25% non-deductible).

In addition, irrespective of the interest ceiling rules, interest payable to shareholders and to other related parties may be disallowed and may also be subject to withholding tax on dividends to the extent that it exceeds an arm's length amount. The same is true where the financing arrangements or the transfer prices applied have not been sufficiently documented.

CONSEQUENCES OF GUARANTEES FROM A RELATED PARTY FOR THIRD PARTY DEBTS

Guarantees from a related party may rule out exceptions from the interest ceiling rules as set forth above under "Debt/equity rules".

A German company would only be able to claim a deduction for guarantee fees paid to a related party if it can show that it also could have obtained the guarantee from an unrelated party on similar terms and conditions.

DIVIDEND DISTRIBUTIONS

Dividend distributions to non-resident shareholders are subject to German withholding tax at a rate of 26.375% which rate may be reduced to 15.825% where the shareholder is a foreign corporation. Withholding tax will be refunded and, under certain circumstances, an exemption may be available where the foreign shareholder is a corporation tax-resident in another EU Member State that holds 10% or more in the German payer of the dividend for more than one year. According to the European Court of Justice, similar benefits may be claimed even if the shareholding falls short of the 10% threshold but, due to a change in German law, this only applies to dividends paid prior to 1 March 2013. Otherwise, the shareholder may rely on one of the many double taxation treaties that Germany has entered into. In many cases, the withholding tax will be refunded save 15% (or 5% where the shareholder is a corporation in the other treaty country that holds a substantial portion of the shares in the target (typically 10% or 25%)). Stringent anti-benefit shopping rules apply that require the foreign recipient of the dividend to demonstrate valid business purposes for its involvement and physical substance (office space, telecommunication devices, staff) in the other Member State or treaty country to the extent it claims a reduction in withholding tax that would not be available to its shareholders, if they received the dividend directly.

HYBRID LOANS

Interest on hybrid loans and similar instruments (participating loans, silent participations, profit participating rights or bonds, convertible instruments) is generally deductible, unless the lender participates in the borrower's profits and liquidation proceeds. The latter will be assumed by the tax authorities if the instrument has a term of 30 years or more.

Interest payments under hybrid instruments are generally subject to German tax at a rate of 26.375% which rate may be reduced to 15.825% where the lender is a foreign corporation. Under many of the double taxation treaties that Germany has entered into, no further relief (reduction of withholding tax or refund) is available for interest paid on hybrid debt if it is deductible for the borrower.

TAX CREDIT OR EXEMPTION TO AVOID DOUBLE TAXATION

Under many of its double taxation treaties, Germany will exempt certain foreign-source income, such as income from permanent establishments in another treaty country. Otherwise, generally, a foreign tax credit is available that can be applied against the German tax to the extent allocable to income derived in the same year and from the same country from which the foreign tax originates.

95% of dividends (German and foreign-source) received by a German corporation are effectively exempt from German corporate income tax, provided the recipient of the dividend held at least 10% of the shares in the payer of the dividend at the beginning of the calendar year. For trade tax purposes, the minimum shareholding is generally 15% or more (10% if the

payer of the dividend is tax-resident in an EU Member State other than Germany) and is subject to certain further requirements (such as the dividend-paying entity maintaining a business which is active in nature).

CONTROLLED FOREIGN COMPANY LEGISLATION

Germany has controlled foreign company (**CFC**) legislation in place. Tax residents and certain expatriates need to include in their taxable income certain items of income derived by a foreign corporation in which they hold shares.

In order to fall within the scope of the CFC rules, the foreign company's income must be of the passive type (eg income from financing activities or income from intra-group activities) that has not incurred foreign tax of 25% or more. Certain exceptions apply to companies resident in the EU/EEA.

In general, income derived by a foreign company will only be subject to the German CFC rules if German tax-residents hold the majority of its shares. However, with regard to certain investment income of the passive type, potentially every German shareholder will have to include its share in such income regardless of the size of its shareholding.

Similar rules apply to foreign branches and to holdings in foreign partnerships.

TRANSFER PRICING

Transfer prices have to comply with the arm's length principle. In determining the arm's length transfer price, Germany applies the comparable uncontrolled price method, the resale price method, the transactional net margin method or the cost plus method, depending on the line of business and the functions carried out in Germany and abroad. Other methods may also be acceptable but, so far, Germany has been reluctant to apply profit-oriented methods of any nature.

In addition to setting arm's length transfer prices, German tax law imposes a number of stringent documentation requirements. First, all arrangements between related parties must be clear and made in advance. In practice, this requires that, before commencing business with a related party, a German company or partnership and its counterpart will have to enter into a written agreement setting forth in sufficient detail the relevant terms of the business relationship.

Second, the German entity must prepare transfer pricing documentation in compliance with German transfer pricing rules. The documentation must establish how the applied price was determined and why it is appropriate. Failure to prepare and present the documentation to the tax authority on time may give rise to significant adjustments on an estimated basis and also to a penalty of up to 10% of the income adjustment. Late submission of the transfer pricing documentation may trigger a penalty of up to EUR1m.

RESIDENCE

A corporation is tax-resident in Germany if it has its seat or its place of principal management and control in Germany.

A partnership as a fiscally transparent entity for income tax purposes does not have a tax residence. Its principal place of management and control will be located where its general partner(s) conduct(s) its business, ie typically at the place of management and control of its managing general partner. Irrespective of any such residence, the income derived from the disposal of a partnership's German permanent establishments is subject to trade tax at the partnership level and to income tax at the level of its resident and non-resident partners.

Other

This section describes other opportunities and threats that should be taken into account when structuring tax-efficient mergers and acquisitions.

STOCK AND OPTION INCENTIVE SCHEMES

Incentive schemes for directors and employees will generally give rise to taxable income. One has to distinguish between schemes granting a participation through shares of stock, on the one hand, and schemes granting an option or cash payments reflecting the performance of the stock (stock appreciation rights, phantom stock), on the other hand.

The granting of shares of stock is a benefit to the extent that the director or employee pays consideration less than their fair market value at the time that the shares are transferred to him or her. The benefit is treated as employment consideration and is subject to income tax at progressive rates, wage tax withholding and social security contributions. A gain from the later disposal of the shares (excess of sales proceeds over the fair market value of the shares at the time of acquisition) will be subject to income tax. Where the shareholding has been less than 1% at any point in time during the five years preceding the disposal, a flat tax of 25% plus the solidarity surcharge and, where applicable, church tax will apply. If the shareholding exceeded 1% at any point in time during the five years preceding the disposal, 60% of the gain will be subject to income tax at regular rates (14%-45%) plus the solidarity surcharge and, where applicable, church tax.

By contrast, where the employee is granted stock options or phantom stock, he or she will only realise a taxable benefit at the time that the option is exercised or the cash award is paid. In this case, the full benefit is treated as employment income and subject to income tax at progressive rates, wage tax withholding and social security contributions.

Careful structuring will be required to ensure that the German entity whose directors and employees benefit from the incentive scheme may claim a deduction for the associated costs.

TAX RELIEF ON INTEREST

In particular, where the target is a corporation, applying interest on acquisition debt efficiently may represent an issue. Without appropriate structuring, a German acquisition vehicle acquiring the shares in the target will not have sufficient income against which it can offset the interest expenses. This can be resolved by either the acquisition vehicle and the target forming a tax group so that the operating income of the target is attributed to the vehicle and may be

applied against the interest expenses (subject to the limitations discussed above) or the acquisition vehicle is merged into the target post-closing in order to combine income and expenses in one legal entity.

LIMITATIONS TO STRUCTURING

Anti-abuse provisions: under German tax law, a taxpayer is generally free to structure his/her transactions as he/she thinks fit. However, a number of special anti-abuse provisions need to be taken into account. Further, the general anti-abuse provision may be invoked by the tax authorities if structures are considered inappropriate in achieving the economic aim of a transaction or appear artificial or unusual.

Financial assistance: under German corporate law, a joint stock corporation (*Aktiengesellschaft*, AG) must not make available financing to its shareholders or acquirers of its shares and any agreement providing, directly or indirectly, for such funding will be null and void. The rules are less prohibitive for limited liability companies (*GmbH*). However, neither of these entities should fund or support their present or future shareholders using assets required to maintain their share capital. This means that any such funding or support would need to come from retained earnings or from contributions to capital other than share capital net of any losses carried forward.

EMPLOYEE CO-DETERMINATION

Entities established under German law will have a co-determined supervisory board (*Aufsichtsrat*) if they have more than 500 employees. The shareholders will elect two-thirds and the employees one-third of the supervisory board members. If a German entity has more than 2,000 employees (including employees of subsidiaries), the shareholders and employees each elect half of the supervisory board members.

Contacts



Eugen Bogenschütz

Partner

Tel +49 69 2648 5804
eugen.bogenschuetz@allenoverly.com



Dr Gottfried E. Breuninger

Partner

Tel +49 89 71043 3302
gottfried.breuninger@allenoverly.com



Dr Asmus Mihm

Partner

Tel +49 69 2648 5796
asmus.mihm@allenoverly.com



Dr Heike Weber

Partner

Tel +49 69 2648 5879
heike.weber@allenoverly.com



Klaus D. Hahne

Counsel

Tel +49 69 2648 5474
klaus.hahne@allenoverly.com

Hungary

Transaction taxes

In this section we identify taxes that will be imposed on the vendor and the acquirer upon a transfer of assets or shares, as well as other tax implications of a transfer of assets or shares.

STAMP DUTY ON THE TRANSFER OF SHARES

The direct or indirect acquisition of more than 75% of the shares of a company that owns Hungarian real estate is subject to stamp duty.

The stamp duty is calculated based on the general rates (see below) relating to the market value of the real property portfolio owned by the company. There are several exemptions which may mitigate or nullify this transfer tax (eg for intra-group restructuring etc).

CAPITAL DUTY PAID ON THE CONTRIBUTION OF CAPITAL

Not applicable.

Notary fees, registration fees and other similar expenses will generally be payable in the case of a contribution to the registered capital of the company.

REAL ESTATE TRANSFER TAX

The general stamp duty rate on real property transfers for consideration is 4% of the market value if the market value is below HUF1bn and 2% of the market value exceeding this threshold. The total amount of the property transfer tax may not exceed HUF200m per property.

CAPITAL GAINS TAX ON THE SALE OF ASSETS

Corporate vendor – Capital gains derived by a corporate vendor from an asset sale will be taxed as ordinary income of the corporate vendor, ie as a part of its annual profit, and it will be subject to Hungarian corporate income tax at the rate of 10% up to the first HUF500m of the positive tax base and 19% for the part of the tax base above this threshold.

Individual vendor – Capital gains realised by an individual vendor upon a sale of assets will be taxed as ordinary income of the individual vendor, ie it will be subject to the flat rate of personal income tax of 16%.

CAPITAL GAINS TAX ON THE SALE OF SHARES

Corporate vendor – Capital gains realised by a corporate vendor upon a sale of shares will be taxed as part of the annual profits of the corporate vendor and will be subject to Hungarian corporate income tax at the rate of 10% up to the first HUF500m of the positive tax base and 19% for the part of the tax base above this threshold.

Individual vendor – Unless an exemption from tax applies, capital gains realised by an individual vendor upon the sale of shares will be taxed as capital gains income of the individual vendor and will be subject to the flat rate of personal income tax of 16%. If the individual vendor realises the gains through a controlled capital market transaction, the tax base generated by profitable transactions can be decreased by the total loss realised on loss making transactions in the given tax year. In relation to long-term investments, the tax rate is 10% if a private individual invests at least HUF25,000 in a three-year term deposit, and 0% in case of a five-year term deposit.

As a general rule, private individuals are subject to a health care contribution at a rate of 6% for interest income and 14% for capital gains. Capital gains realised from controlled capital market transactions and income from long-term investments are exempt from the health care contribution, however, a 6% rate applies if the long-term investment contract is interrupted before the last day of the three-year term deposit.

AVOIDANCE OF CAPITAL GAINS TAX

In accordance with the Hungarian participation exemption rule, in the case of registration (within 75 days) of the acquisition of a participation by which a company becomes the owner of at least 10% of a Hungarian subsidiary, the capital gains arising in relation to the sale (or the in-kind contribution) of the registered participation are exempt from Hungarian corporate income tax (subject also to some further conditions).

A similar rule is applicable as of 2013 regarding the capital gains realised on the sale of intangible assets (intellectual property, valuable rights). The capital gains realised on such assets is exempt from corporate income tax if the acquisition of the intangible asset is registered with the National Tax and Customs Authority of Hungary within 60 days following the acquisition.

PRESERVATION OF TAX LOSS CARRY-FORWARD

In general, a tax loss can be carried forward indefinitely, but can be used up to a maximum of 50% of the tax base in each of the following tax years.

On a merger or demerger of a company, a rollover of tax losses carried forward is available to a successor company under certain circumstances and subject to certain restrictions.

NON-RESIDENT VENDORS

Share sale – Under Hungarian rules effective as of 1 January 2010, foreign entities are required to pay Hungarian corporate income tax on their capital gains realised through the alienation of their shareholdings in entities which own a Hungarian real property portfolio worth more than 75% of the total value of their total assets (real estate owning companies).

This tax must only be paid if Hungary does not have a double tax treaty with the state where the foreign entity is resident, or if the relevant treaty allows such taxation. Gains on shares traded on recognised stock exchanges are exempt.

Asset sale – If the non-resident vendor sells real estate in the territory of Hungary, the vendor establishes itself as a Hungarian tax establishment without any further activity or incorporation in Hungary.

VALUE ADDED TAX

Share sale – No value added tax (**VAT**) is charged on a transfer of shares.

Asset sale (purchase of individual assets) – Hungarian VAT at the standard rate of 27% may be charged on an asset sale involving a purchase/sale of individual assets/rights. However, from 2013, no VAT is charged on the transfer of a business line as a going concern, provided that the buyer intends to keep the business unit operational and the transfer complies with certain statutory conditions.

Merger/demerger – Company transformations are not subject to Hungarian VAT, however, certain restrictions apply.

Under Hungarian VAT grouping rules, the group members are exempt from VAT in a *vis-à-vis* arrangement, but they are jointly subject to VAT in external relations as they are recognised as a single taxable person for VAT purposes. VAT group members are jointly and severally liable for any tax debts prior to and during the term of the VAT grouping. To obtain membership of the VAT grouping, taxpayers are required to apply for permission from the Tax Authority.

Opportunities and threats

In this section an overview is provided of opportunities to maximise relief for acquisition costs (such as financing costs), as well as other items which require attention when designing an efficient tax structure.

STEPPING-UP ASSET VALUES

Share sale – As a general rule, revaluation of the assets of an entity is not triggered by the sale of the shares of that entity.

Asset sale (purchase of individual assets) – On a purchase of individual assets, assets are valued at their market value (especially in related party transactions).

Transfer of business – Under Hungarian law, the transfer of a whole business line is considered to be a preferential transfer of assets under the corporate tax rules. Subject to an agreement in writing made with the receiving company, such transfer enables the transferor to decrease its pre-tax profit by the portion of the income claimed in connection with the transfer of a strategic business unit that is in excess of the book value of the transferred assets, or to increase its pre-tax profit by the portion of the book value of the transferred assets that is in excess of the income claimed. Furthermore, since 2013, the transfer of a business line is outside the scope of Hungarian VAT.

Merger/demerger – On a (non-preferential) demerger, the merger of the assets (and liabilities) must be revalued to reflect their fair market value for accounting purposes.

TAX CONSOLIDATION RULES

There are no group taxation rules under Hungarian corporate income tax law. Consequently, no offset of profits and losses at a group level is possible and a separate tax return must be filed by each group company.

THIN CAPITALISATION RULES

Under the Hungarian thin capitalisation rules, the interest paid on liabilities exceeding a debt-to-equity ratio of 3:1 is non-deductible for tax purposes. The ratio must be calculated on the basis of the daily average amount of debt and equity.

It also applies to interest paid to non-related entities, but does not apply to interest paid to financial institutions.

DEBT/EQUITY RULES

See “Thin capitalisation rules” above.

DISALLOWED AND DEFERRED INTEREST (OTHER THAN DEBT/EQUITY RULES)

Not applicable.

CONSEQUENCES OF GUARANTEES FROM A RELATED PARTY FOR THIRD PARTY DEBTS

Not applicable.

HYBRID LOANS

Hungarian tax law does not contain any provisions that would define the characteristics of a hybrid loan for tax purposes, nor does it include any specific measures regarding the limitation of tax deductibility of interest accrued on such loans.

CONTROLLED FOREIGN COMPANY LEGISLATION

Under Hungarian law, controlled foreign company (**CFC**) means:

- foreign persons or non-resident entities, having their head office located outside of Hungary (the non-resident company), which have a beneficial owner considered to be resident (within the meaning of the Hungarian Act on personal income tax) for the majority of the relevant tax year of the non-resident company; and/or
- a non-resident company whose revenues for the relevant tax year originated mainly from Hungary,

in either case, if: (i) the quotient of the tax amount paid (payable) by the non-resident company for the tax year (less any tax refund) and the tax base in the case of a group taxation arrangement the amount of tax paid (payable) at group level (less any tax refund) and the tax

base is less than 10%; or (ii) the non-resident company has not paid any tax equivalent to corporate tax due to the fact that its tax base was zero or even negative, despite the fact that it has made a profit.

This provision does not apply if the non-resident company in question is established in or is a resident of a Member State of the European Union, a Member State of the OECD, or a state with which the Republic of Hungary has an agreement on double taxation provided that the non-resident company has a real economic presence in such a state.

PASSIVE FOREIGN INVESTMENT COMPANY ANTI-DEFERRAL REGIME

Not applicable.

TRANSFER PRICING

Transactions between related parties must be performed on arm's length terms, or the parties are required to adjust their tax bases accordingly.

Under Hungarian income tax law, persons are regarded as related if they qualify either as:

(i) capital-related persons; or (ii) otherwise related persons.

Legal entities are considered to be related parties if:

- one person has majority control of another person, directly or indirectly;
- a third party has majority control of two persons;
- a non-resident person has a Hungarian place of business or a Hungarian business establishment. It also applies to any person who acts as an intermediary in this relationship; or
- a person subject to Hungarian law who has a foreign branch. It also applies to any person who acts as an intermediary in this relationship.

For transfer pricing, the transactional net margin and the profit split methods have been added to the existing comparable uncontrolled price method, resale price method and cost plus method as being generally applicable if possible for transfer pricing purposes.

If none of the above methods can be applied, any other reasonable method can be used.

RESIDENCE

A legal entity is considered to be a tax resident of Hungary if it has either its seat or place of management in Hungary. If a foreign legal entity carries out a business activity or has an agent in Hungary, it is also subject to Hungarian corporate income tax under the provisions of the relevant treaty (if any).

As a general rule, an individual is treated as a Hungarian tax resident if he/she is a Hungarian citizen and has a residential address (permanent residence) in Hungary or if he/she stays in Hungary for at least 183 days in the relevant calendar year, either continuously or intermittently.

ENTITY CLASSIFICATION (“CHECK-THE-BOX”) RULES

Not applicable.

Other

This section describes other opportunities and threats that should be taken into account when structuring tax-efficient mergers and acquisitions.

ANTI-ABUSE REGULATIONS

The key anti-avoidance measure is the “substance over form” rule. This rule entitles the Hungarian tax authorities to re-characterise a transaction for tax purposes pursuant to its substance if the form of the transaction differs from it. Consequently, any sham transactions and steps in transactions are disregarded and the transaction is taxed in accordance with its substance, rather than its form. For the purposes of taxation, an invalid contract or any other transaction must be judged on the basis of the real economic results it produces.

Employees’ and directors’ equity incentives are taxed in general as ordinary incomes of the individual. The tax authority shall refuse to issue a tax number to any new entity if the representative/owner of that entity is or was also a representative/owner of another company whose tax number was deleted due to non-compliance with certain basic legal requirements within the last five years.

HIVE-UPS

Please see our comments regarding preferential transformations.

FINANCIAL ASSISTANCE

Under Hungarian financial assistance rules, a limited company limited by shares may provide financial assistance in respect of and in connection with an acquisition of its own shares only under market conditions, financed from the assets available for the payment of dividends, and subject to third-quarters majority general meeting approval.

TAXATION OF DIVIDENDS

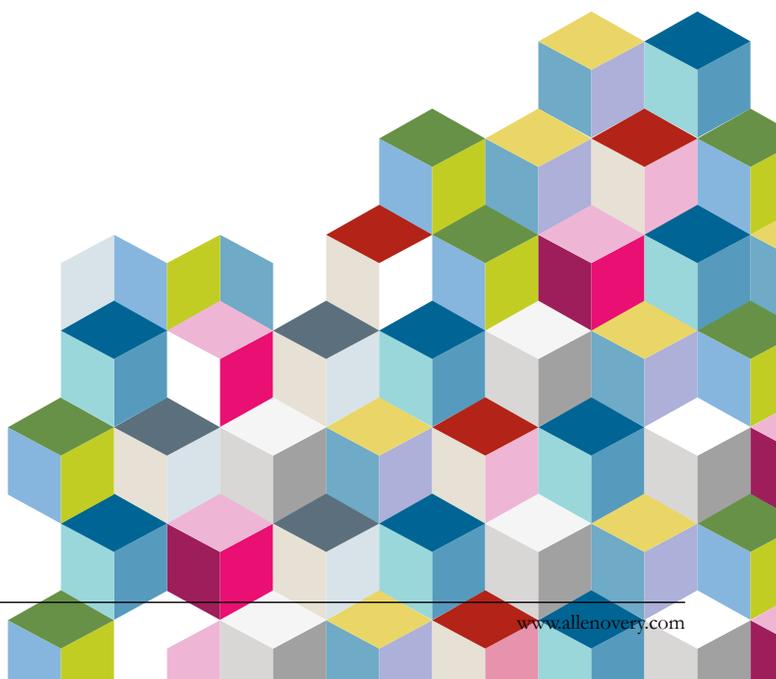
Under Hungarian law, dividends paid from taxed profits to beneficiaries other than private individuals are not subject to further tax as a general rule.

Dividends received by private individuals are subject to Hungarian personal income tax at the rate of 16%.

WITHHOLDING TAXES

No tax must be withheld from dividends paid to corporate beneficiaries.

The above personal income tax rate of 16% must be withheld by the payer of dividends if the beneficiary is a private individual.



Contacts



Gergely Szarka

Associate

Tel +36 1 429 6018

gergely.szarka@allenoverly.com

Italy

Transaction taxes

In this section we identify taxes that will be imposed on the vendor and the acquirer upon a transfer of assets or upon a transfer of shares, as well as other tax implications of a transfer of assets or shares.

STAMP DUTY ON THE TRANSFER OF SHARES

No stamp duty on a transfer of shares. Registration tax of EUR200 if the transfer is executed through a notarial deed or a notarised deed.

Stamp duty of up to EUR80 and registration tax of EUR200 are due on transfers of quotas of a limited liability company (*società a responsabilità limitata*).

FINANCIAL TRANSACTION TAX

As of 1 March 2013, a financial transaction tax applies at a rate of 0.2% upon a transfer of the ownership rights in: (i) shares and other participating securities issued by Italian resident companies pursuant to Article 2346(6) of the Italian Civil Code; and (ii) financial instruments representing these shares and/or participating securities, whether issued by Italian resident companies or not. Conversion of bonds into existing Italian shares should also trigger the financial transaction tax. The taxable base is the “transaction value” (ie generally the consideration agreed between the parties).

The tax rate is reduced to 0.1% if the transaction is executed on a regulated market or a multilateral trading system of an EU or EEA Member State exchanging information with the Italian tax authorities. Specific rules apply if, at the same date, a subject carries on a number of transactions involving the same instruments.

CAPITAL DUTY PAID ON THE CONTRIBUTION OF CAPITAL

Registration tax of EUR200.

Where there is a contribution of real estate, a registration tax of up to 12% may apply.

REAL ESTATE TRANSFER TAX

Value added tax (**VAT**) at the applicable rate (22% or lower 10% rate) and *cadastral* and mortgage taxes up to 4% apply. Alternatively, registration tax up to 12% (including *cadastral* and mortgage tax) for certain transactions may apply.

BUSINESS CONCERN TRANSFER TAX

Registration tax of up to 3% applies (and registration tax of up to 12% may apply in relation to the value of the business concern which relates to real estate).

CAPITAL GAINS TAX ON THE SALE OF ASSETS

Corporate Income Tax (**IRES**) generally at a rate of 27.5% is applicable, and an election can be made to pay the tax in five instalments over five tax periods if the assets sold were owned for more than three tax periods. Regional Tax on Productive Activity (**IRAP**) at a rate of up to 5.30% (plus regional surcharge, if any) may apply in certain circumstances.

CAPITAL GAINS TAX ON THE SALE OF SHARES

Resident corporate vendor⁹

Capital gains on a sale of shares is generally taxed at 27.5%; there is a partial exemption (ie 5% of the capital gain is taxed) where the participation exemption applies. If the participation exemption does not apply, an election can be made to pay the tax in five instalments over five tax periods provided that the participation was owned for at least three years.

According to Article 87 of the Italian Corporate Income Tax Act (**CIT**), capital gains realised by resident corporate entities on any kind of participation (in domestic or foreign entities, being corporate entities or other entities) will be partially¹⁰ tax-exempt, provided that:

- the participation is entered in the financial statements as a fixed financial asset, and has been held for more than 12 months;

⁹Including the Italian permanent establishment of foreign entities to which the participation is connected.

¹⁰95% tax-exempt.

- the company whose shares are disposed of has actually been carrying out a business activity at least from the beginning of the third tax period before the disposal; and
- the company whose shares are disposed of is not resident in a tax haven. This condition must have been satisfied at least from the beginning of the third tax period before the disposal.

Capital losses (either realised or simply accrued) on shareholdings which qualify for the exemption are not relevant for tax purposes (ie no deduction will be allowed). Moreover, recapture rules apply to tax-deductible write-offs carried out in 2002 and 2003 on shares subsequently transferred to take advantage of the new capital gain exemption regime.

IRAP at a rate of up to 5.30% (plus regional surcharge, if any) may apply in certain circumstances.

Resident individual vendor

If the requirements indicated above for the corporate vendor are met, an individual carrying out business activities is subject to a progressive rate on 49.72% of the capital gains realised through the sale of participations. In the case of an individual not carrying out business activities, the capital gains realised through the sale of participations is subject to a progressive rate on 49.72% of the capital gains provided that the company, whose shares are disposed of, is not resident in a tax haven; subject to certain conditions, the gains can be offset by losses.

The disposal of a non-qualifying shareholding (ie not higher than 20% of the voting rights or 25% of the company's capital; lower thresholds apply in the case of listed shares) by an individual (not carrying out business activities) is liable to a 20% capital gains tax (*imposta sostitutiva*).

Non-resident vendor¹¹

The disposal of a shareholding in an Italian company triggers an Italian tax at a rate of 27.5%¹² on 49.72% of the realised capital gains, unless a tax exemption is granted according to the applicable tax treaty.

However, the disposal of a non-qualifying shareholding is exempt in Italy provided that: (i) the vendor is resident in a so-called white-listed country; or (ii) the shareholding is negotiated in a regulated market. If neither of these conditions is met, a 26% (20% until 30 June 2014) capital gains tax is levied on the realised capital gains unless a tax exemption is granted according to the applicable tax treaty.

¹¹ Unless the participation is held through a permanent establishment in Italy.

¹² Capital gains realised by non-resident individuals are subject to a progressive rate.

AVOIDANCE OF CAPITAL GAINS TAX

Contributions to business concerns by resident companies (or individual entrepreneurs to resident companies or entities carrying out a business activity) are on a tax-free basis. The contributing companies must record the shares received at the tax value of the business concern as it was recorded in their books prior to the contribution. Moreover, the assets and liabilities contributed must be recorded by the receiving companies at the same tax value as at the time of the contribution. The assets and liabilities may also be recorded on the accounting books of the receiving companies at a different value, but in such case a statement must be attached to the tax return filed by the receiving company.

The receiving company is entitled to step-up the tax value of tangible and intangible assets received up to their accounting value by paying a substitutive tax at the rate of:

- 12% on the portion of the step-up in value up to EUR5m;
- 14% on the portion of the step-up in value from EUR5m up to EUR10m; and
- 16% on the portion of the step-up in value exceeding EUR10m.

The step-up of goodwill, trademarks and other intangible assets is alternatively allowed by paying a substitutive tax at the rate of 16% (in this latter case the depreciation period of these items would be reduced to ten years instead of the ordinary depreciation period of 18 years at least), while a step-up in value of receivables is allowed upon payment of a substitutive tax at a rate of 20%. Finally, a step-up of other assets received (eg participations) is generally allowed by paying taxes at ordinary rates.

Contributions of a qualifying shareholding (controlled or related company) between resident entities are on a tax-free basis insofar as the shares received by the contributing company are reported at the same tax value as the contributed shares, unless such shares are reported by the receiving company at a higher tax value.

A tax-neutrality regime also applies under certain conditions when both the contributing company and the receiving company are resident in an EU Member State, other than Italy, and the former has a permanent establishment in Italy. Finally, tax-neutrality may apply under certain conditions to contributions of a business concern or qualifying shareholding between Italian resident entities and non-resident entities (ie resident in an EU Member State).

PRESERVATION OF TAX LOSS CARRY-FORWARD

Losses may be carried forward without any time limit. However, the taxable income generated in each tax period can be set off against carried forward tax losses up to 80% of that taxable income (exceptions may apply for start-up losses).

Losses cannot be carried forward if: (i) the majority of participations in the company with losses are transferred to third parties; and (ii) the principal business activity of such company is modified within the two tax periods preceding and following the transfer. The limitation does not apply if the participations relate to companies which have been effectively operating during the two years before the transfer (on the basis of certain standards, such as a number of employees and amounts of revenues/expenses related to core business).

Opportunities and threats

In this section an overview is provided of opportunities to maximise relief for acquisition costs (such as financing costs), as well as other items which require attention when designing an efficient tax structure.

STEPPING-UP ASSET VALUES

As long as assets are directly purchased by an Italian company:

- the allocated portion of the purchase price of assets can be treated as the basis for depreciation and as the base cost for future capital gains tax;
- amortisation of goodwill (over 18 years at least) by equal instalments and intangible assets is possible;
- in the case of an acquisition of shares, depreciable step-up in an acquisition is not allowed.

In the case of a merger, a depreciable step-up of tangible and intangible assets is allowed up to their accounting value by paying a substitutive tax at the rate of:

- 12% on the portion of the step-up in value up to EUR5m;
- 14% on the portion of the step-up in value from EUR5m up to EUR10m; and
- 16% on the portion of step-up in value exceeding EUR10m.

A step-up in value of goodwill, trademarks and other intangible assets is alternatively allowed by paying a substitutive tax at a rate of 16% (in this latter case the depreciation period of these items would be reduced to ten years instead of the ordinary depreciation period of 18 years at least), while a step-up in value of receivables is allowed upon payment of a substitutive tax at a 20% rate. Finally, a step-up in value of other assets received (including participations) is generally allowed by paying taxes at ordinary rates.

TAX CONSOLIDATION RULES

Formation of a fiscal unity for corporate income tax purposes is possible for more than 50%-owned subsidiaries (provided that other requirements are met) or alternatively through a tax-transparency election (so-called consortium relief) if participation in the transparent company is between 10% and 50%.

Groups may elect to be taxed as single taxpayers for IRES purposes. The area of tax consolidation may be limited to any resident group companies, or extended to non-resident group companies.

Domestic consolidation

In this case, consolidation applies only to the parent company and its subsidiaries (which must all be resident in Italy for tax purposes). The tax results that may be consolidated are only those of the parent company and those of the subsidiaries that are under the legal control of the parent company and in relation to which the parent company owns directly or indirectly more than 50% of the company capital and is directly or indirectly entitled to receive more than 50% of the profits.

The consolidated income is the aggregate of the net tax results (positive or negative) realised by the parent and its subsidiaries. The consolidation includes the total net results of the subsidiaries regardless of the percentage of the controlling shareholding.

Each subsidiary is free to opt for the consolidation regime. Should a company choose to consolidate, the option cannot be revoked for three fiscal years, except where one of the subsidiaries no longer qualifies as such due to the absence of legal or economic control.

The parent company files the consolidated tax return and pays the corporation tax, but the consolidated subsidiaries remain jointly liable together with the parent for the higher taxes levied in relation to their taxable income attributed to the consolidation.

Carry-forward of pre-fiscal unity losses to fiscal unit years or carry-back of fiscal unity losses to pre-fiscal unity years is not allowed.

International tax consolidation

This regime allows for the consolidation of non-resident subsidiaries of Italian parent companies, under the same general principles as are described above, provided that the Italian parent company: (i) has its shares listed on a regulated market; (ii) is directly controlled by a public entity; or (iii) is directly controlled by Italian resident individuals, who do not control other entities in Italy or abroad.

However, international tax consolidation is not allowed for Italian companies that are included in a domestic consolidation unless they are the parent company of the domestic consolidation.

As far as international tax consolidation is concerned, the following issues must be considered:

- the parent company and all its non-resident subsidiaries must opt for the consolidation (the “all-in, all-out” principle), and the option cannot be revoked for five fiscal years;
- the consolidated income is calculated by adding to the parent company’s income the percentage of the subsidiaries’ income proportional to the shareholding directly or indirectly held by the parent;
- the accounts of the parent and the non-resident subsidiaries must be audited by professional auditors; and
- the parent company must file, within the first financial year, a tax ruling request in order to receive confirmation from the Italian tax authorities about the validity of the option.

Consortium Relief (Fiscal Transparency Regime)

According to Article 115 of the CIT, companies whose shareholders are exclusively other companies resident in Italy (each with a participation not lower than 10% but not exceeding 50%) can opt for the transparent tax regime usually granted to Italian partnerships.

Non-resident shareholders can apply for the regime if they are eligible for a withholding tax exemption on dividends paid out of Italy (eg under the Parent-Subsidiary Directive regime).

The option for the transparency regime cannot be revoked for three fiscal years. Such an option cannot be exercised if the company participates in a group taxation regime.

DEBT/EQUITY RULES

Debt/equity rules no longer apply.

DISALLOWED AND DEFERRED INTEREST (OTHER THAN DEBT/EQUITY RULES)

Interest expenses, net of interest receivable, are deductible for corporate income tax purposes up to a maximum amount computed as 30% of “*reddito operativo lordo*” (**Ceiling**).

The Ceiling is computed based on the results of the profit and loss account of the same fiscal year to which interest relates as the difference between:

- proceeds shown in Section A (numbered from 1 to 5) of the scheme of profit and loss account provided for by Art. 2425-bis of the Italian Civil Code (**ICC**) for non-financial institutions; and
- costs shown in Section B (numbered from 6 to 14) of the scheme of profit and loss

account provided for by Art. 2425-bis of ICC, but excluding costs shown in Section B, number 10, letters a) and b) (ie depreciation allowances for tangible and intangible assets) and also excluding financial lease rentals shown in the profit and loss account.

Interest capitalised on the cost of the assets is excluded from the above computation.

Banking and financial institutions, insurance companies, holdings of banking or insurance groups and some specific project companies are excluded from the application of the above mentioned limitations to interest deductibility. In these cases specific rules apply as to the limitation of interest-deductibility.

Further, interest relating to loans secured by mortgages on real estate to be rented may not be subject to the above limitations to interest deductibility.

A carry-forward mechanism is laid down, aimed at allowing for the deduction of interest expenses not deducted in a certain tax period if and to the extent the Ceiling of the following tax periods is higher than the amount of interest expenses (net of interest proceeds) incurred in such periods.

A carry-forward of the residual part of the unused Ceiling is also available.

Specific rules apply in relation to companies joining a tax consolidation.

HYBRID LOANS

Loans with certain equity features can be classified as equity for tax purposes. A portion of the remuneration of these loans under certain conditions may be tax deductible (ie if the debt features of such hybrids are sufficient for the purposes of the rules on deduction of interest from business income).

ALLOWANCE APPLICABLE TO CORPORATE EQUITY (ACE)

Companies are entitled to deduct for IRES purposes a notional amount equal to a presumptive return applied to new cash contributions and retained earnings (**ACE**). ACE should also apply to Italian permanent establishments of foreign entities.

New cash contributions and retained earnings are those effected after 31 December 2010 (set rules apply if the financial period does not end on 31 December of each calendar year).

The presumptive return for the fiscal year ending the 31 December 2014 will be equal to 4% (4.5% for the fiscal year ending the 31 December 2015 and 4.75% for the fiscal year ending 31 December 2016) of the amount of the increase in capital of the company (afterwards, presumptive return may be varied by decree of the Ministry of Economy and Finance).

The notional amount exceeding the income tax base may be carried forward to subsequent fiscal years.

According to measures introduced by the Italian Government (published in the Italian Official Gazette on 24 June and effective as of 25 June 2014), companies which have not applied the tax deduction for IRES purposes can obtain a tax credit to be used during a five-year period for the purposes of the IRAP.

The Italian Government has also set out further incentives for companies listed in the EU or EAA regulated markets after 25 June 2014.

These measures must be confirmed by the Italian Parliament within 60 days from their publication (otherwise they expire with retroactive effect) and could be subject to amendments.

CONVERSION OF DEFERRED TAX ASSETS INTO TAX CREDITS

Under certain conditions, Italian companies are allowed to convert certain deferred tax assets shown in their financial statements into tax credits. These rules address: (i) deferred tax assets derived from depreciation of goodwill and/or intangible assets provided that the relevant financial statements show a loss; and (ii) deferred tax assets derived from tax losses which, in turn, are due to depreciation of goodwill and/or intangible assets. Further, if the company is a financial institution, deferred tax assets derived from the write-off of bad debt falls under the scope of these rules. These rules apply also to Italian permanent establishments of foreign companies. Specific rules apply as for the determination of the tax credits derived from conversion of deferred tax assets. These tax credits can be off-set, according to certain rules, against taxes and social security contributions due from the company and/or disposed of by them at nominal value.

TAX CREDIT OR EXEMPTION TO AVOID DOUBLE TAXATION

Article 89 of the CIT provides for a 95% participation exemption regime under which 95% of the dividend income (including liquidation profits) distributed by companies and business entities, both resident and non-resident, to Italian companies is exempt from Italian taxation. However, in the case of companies that adopt IAS/IFRS for accounting purposes, dividends relating to shares or financial instruments held for trading are fully subject to IRES in the tax year of payment.

Corporate taxation at the rate of 27.5% is, therefore, only levied on 5% of the total of the dividends. The exemption regime is not subject to any condition for election such as a minimum participation or a minimum holding period. The tax exemption does not apply to dividends derived from a company located in a tax haven.

CONTROLLED FOREIGN COMPANY LEGISLATION

The Italian controlled foreign company (**CFC**) legislation is, at present, applicable to foreign entities over which an Italian resident has the control if:

- the foreign entity is not resident in a state or territory included in the list of states or territories allowing an adequate exchange of information with Italy and not granting a privileged tax regime, which is issued by the Ministry of Finance (the **White-list**). As the White-list has not yet been issued, this rule currently applies with reference to entities resident in states or territories having a privileged tax regime, which are itemised in a list as set out by Ministerial Decree of 21 November 2001 (the **Black-list**); or
- the effective tax burden for the foreign entity is more than 50% lower than the tax burden it would have borne on the same earnings in Italy; and
- the foreign entity derives more than 50% of its income from transactions concerning securities or financial assets, from transactions involving intellectual property or from the supply of services to an associated person.

The CFC legislation is extended to “affiliated” foreign entities (residents in a tax-haven country, listed in the Black-list) in relation to which an Italian resident is entitled to receive at least 20% (10% in the case of listed companies) of the profits.

TRANSFER PRICING

The arm's length principle is codified in the CIT. The arm's length principle applies to related parties provided that one of the parties is not resident in Italy. It is not mandatory to give evidence of inter-company transactions with companies included in the tax consolidation. However, providing for set documentation regarding intercompany transactions and transfer pricing analysis may avoid the application of tax penalties in cases of tax assessment. This documentation includes, in particular, the master file and the country file, which must be prepared in accordance with the rules set out by the Italian tax administration.

RESIDENCE

Whether an entity is resident for tax purposes in Italy is determined by reference to the seat of management, the location of the registered office and the place of main business purpose.

Furthermore, a foreign company is deemed to be resident in Italy (unless proof to the contrary is provided) if it controls an Italian company (ie it exercises “dominant influence”) and:

- is directly or indirectly controlled (subject to dominant influence) by an Italian-resident person (company or individual); or

- is managed by a management board or other governing body comprised of a majority of Italian-resident persons (companies or individuals).

TAXATION OF DISTRIBUTIONS RECEIVED FROM SUBSIDIARIES

Dividends received by an Italian company will generally be 95%-exempt from taxes. The 95% exemption applies to cash dividends as well as to distributions of dividends in kind. However, in the case of companies that adopt IAS/IFRS for accounting purposes, dividends relating to shares or financial instruments held for trading are fully subject to IRES in the tax year of payment.

The exemption will not be available to: (i) dividends received from a foreign company where the proceeds are not treated as dividends for Italian tax purposes; and/or (ii) dividends derived from a company resident in a tax haven.

WITHHOLDING TAXES

Outbound dividends paid by an Italian company generally trigger a 26% (20% until 30 June 2014) withholding tax; a tax refund can, however, be claimed under domestic legislation if certain conditions are met. The withholding tax rate may be reduced according to the applicable tax treaty. Further, the withholding tax applies at a reduced rate of 1.375% if the beneficial owner of the dividends is a company resident and subject to corporate income tax in another State of the EEA that allows an adequate exchange of information with the Italian tax authorities. Finally, an exemption may be available under the Parent and Subsidiary Directive.

Interest is generally subject to a 26% (20% until 30 June 2014) withholding tax when paid to a person outside Italy. The tax rate may be reduced (even to zero) according to the applicable tax treaty. An exemption may be available on interest from bonds, similar securities and commercial papers issued by Italian companies under certain circumstances. An exemption may also be available under the Interest and Royalties Directive if the relevant conditions are satisfied.

Further, according to measures introduced by the Italian Government (published in the Italian Official Gazette on 24 June and effective as of 25 June 2014), an exemption is available on interest paid in favour of banks, mutual funds and insurance companies established in an EU or EEA member State under medium-and/or long-term loans. These measures must be confirmed by the Italian Parliament within 60 days from their publication (otherwise they expire with retroactive effect) and could be subject to amendments

The payment of royalties connected with intellectual property is generally subject to withholding tax (currently a 30% withholding tax, which under certain conditions is applied to 75% of the gross amount of the payment) when paid to a person outside Italy. The tax rate may be reduced (even to zero) according to the applicable tax treaty. An exemption may be available on interest from bonds, similar securities and commercial papers issued by Italian companies under certain circumstances. An exemption may be available under a double tax treaty or under the Interest and Royalties Directive.

Other

This section describes other opportunities and threats that should be taken into account when structuring tax-efficient mergers and acquisitions.

ADVANTAGES OF THE ITALIAN HOLDING TAX REGIME

Easy access

As a general rule, Italian companies enjoy a partial participation exemption on capital gains, on the condition that they meet the requirements of Article 87 CIT, and dividends are largely not taxable provided that the subsidiary is not resident in a tax haven. As there is no participation threshold for capital gains and dividends, it is quite easy to achieve a favourable tax regime for Italian corporations with respect to (Italian and non-Italian) operative companies not located in tax havens. This also applies (with respect to capital gains) to Italian holding companies owning a group of companies, including companies located in tax havens, on the condition that the net assets of the companies located in a tax haven do not prevail over the net assets of the other companies.

The participation exemption regime is not applicable to real estate companies.

LIMITATIONS TO LEVERAGED ACQUISITIONS

The Ceiling rule greatly affects the tax leverage of Italian acquisition vehicles. It is, however, possible to reduce the impact of this rule by consolidating the Italian Target with the NewCo and other subsidiaries.

MEASURES RELATING TO LIMITATIONS TO LEVERAGED ACQUISITIONS

If a domestic consolidation election is made (in this respect the NewCo must have achieved more than 50% of the voting rights and profit participation in the Target), deductible interest paid by the NewCo may generate losses for the NewCo which can be offset by profits of the Target.

Within the domestic consolidation, any non-deducted interest expenses can be deducted, at consolidated level, to the extent that other companies joining the consolidation have at least a Ceiling which has not been “used” for the purpose of deduction of their interest expenses. Under certain conditions, the Ceiling of foreign subsidiaries can be taken into consideration for the purposes of the determination of the Ceiling threshold.

If the NewCo acquires a minority interest in the Target so that a tax consolidation cannot be made, it is advisable to allocate debt to: (i) the Target after the merger with the NewCo is effected; and (ii) a non-Italian upper-tier acquisition vehicle to exploit the lower limitation on interest of the relevant jurisdiction, if available. In particular, although a consolidation election is not made, interest of the Target is tax-deductible in Italy under the restrictions of the Ceiling rule.

TAX STEP-UP OF TARGET'S ASSETS

Tax step-up of Target's assets (including goodwill) following a merger with NewCo is allowed; therefore the cost of acquisition, if it exceeds the net assets of Target, can be used tax-wise in Italy. As the step-up is conditional upon payment of substitutive tax by the Target, this will affect the pricing of the transaction.

SHARE DEAL VS ASSET DEAL

Capital gains arising from the sale of assets (business concern) are subject to 27.5% corporate tax (but an election can be made to pay the tax in five instalments over five tax periods). In turn, capital gains arising from the sale of participations (for example in the Italian company owning the business concern) are partially exempt (95%) if the requirements of the participation exemption are met. There is, therefore, an indirect arbitrage in favour of share deals versus asset deals.

In particular, the contribution of a business concern is tax-neutral because of the operation (at domestic as well as EU level) of rollover relief, and the subsequent transfer by the contributing company of the participations received in exchange for the contribution benefit of the participation exemption (if the requirements are met). In addition, the step-up of values is allowed for tax purposes upon payment of a substitutive tax. It is therefore advisable to convert assets into shares by adopting such a tax-effective transaction. The transaction structure must have sound economic (ie other than tax) reasons to avoid being challenged by the tax authorities under anti-abuse provisions (*inter alia* for registration tax purposes); this aspect should be carefully examined on a case-by-case basis.

FOREIGN HOLDING/NEWCO

The arbitrage in favour of share deals versus asset deals creates a conflict of interest between the purchaser and the seller: the seller prefers a tax-exempt share deal under the participation exemption, while the purchaser prefers an asset deal in which the tax value of the purchased assets (business concern) reflects the acquisition price and triggers favourable tax depreciations (see above).

ITALIAN HOLDING/NEWCO

If the purchaser cannot incorporate a Luxembourg or Dutch holding (or a holding in a similar participation exemption jurisdiction), then the use of an Italian holding is tax-advantageous only upon the condition that the Target is consolidated. If consolidation is not achieved, adverse tax effects (as indicated above) occur, such as:

- no deduction of interest by the NewCo because of the lack of taxable income; and
- potential limitations on deduction of interest by the NewCo because of the Ceiling rule.

TAX-OPTIMISED ACQUISITION STRUCTURE

Luxembourg or Dutch (or equivalent) holdings owning an Italian sub-holding (NewCo): this avoids a lock-in effect in Italy of exempt capital gains.

BUYER STRUCTURE

Italian sub-holding (NewCo) as an acquisition vehicle:

- tax benefits of both holding regimes are obtained; and
- benefit of Italian participation exemption is obtained.

TAX-OPTIMISED ACQUISITION STRUCTURE

Hive-down of assets by Italian seller.

SELLER STRUCTURE

Creation of a Target corporate vehicle by the seller and the transfer of certain assets and liabilities to the Target following a demerger or a procedure for the transfer against cash or contribution against shares of the business as a going concern which is going to be purchased. The transaction structure must have sound economic (ie other than tax) reasons to avoid being challenged by the tax authorities under anti-abuse provisions: this latter aspect should be carefully examined on a case-by-case basis.

TAX-OPTIMISED ACQUISITION STRUCTURE

The NewCo is financed by Italian banks (international syndication is possible), including Italian branches of foreign banks, or by group companies and acquires the shares of the Target. Consolidation or merger between Target and NewCo.

TRANSACTION

The NewCo consolidates the Target:

- profits of the Target and losses of the NewCo (possibly triggered by leverage of the NewCo) can be offset by the restrictions set out under the Ceiling rule.

TAX-OPTIMISED ACQUISITION STRUCTURE

Dividends paid by the Target to the NewCo are partially (95%) tax-exempt, while dividends paid by the NewCo to a Luxembourg or Dutch holding are exempt from Italian withholding tax if certain conditions are met.

POST-TRANSACTION

Interest paid by the NewCo to a Luxembourg or Dutch holding are exempt from withholding tax if certain conditions are met. Restrictions apply to the deductibility of interest at the level of the NewCo.

Sale by the Luxembourg or Dutch holding of participations in the NewCo (or sale by the NewCo of participations in the Target before any possible Italian lock-in effect) is tax-exempt.

Contacts



Francesco Bonichi

Partner

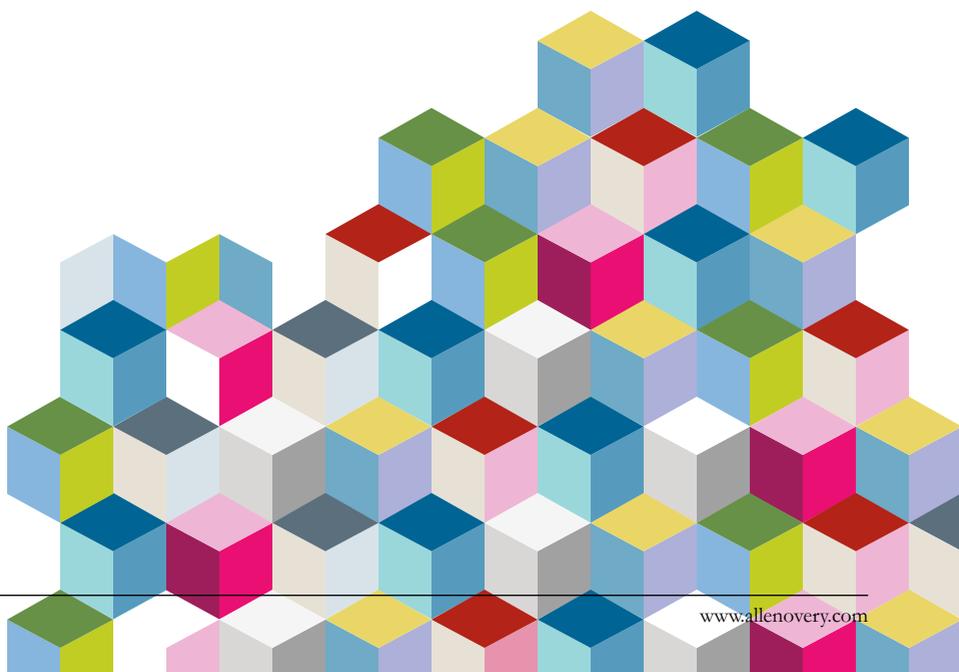
Tel +39 06 684 27566
francesco.bonichi@allenoverly.com



Francesco Guelfi

Partner

Tel +39 02 290 49659
francesco.guelfi@allenoverly.com



Luxembourg

Transaction taxes

In this section we identify taxes that will be imposed on the vendor and the acquirer upon a transfer of assets or upon a transfer of shares, as well as other tax implications of a transfer of assets or shares.

STAMP DUTY ON THE TRANSFER OF SHARES

Nil.

CAPITAL DUTY PAID ON THE CONTRIBUTION OF CAPITAL

A fixed registration duty of EUR75 is levied upon incorporation of a commercial company in Luxembourg and on each subsequent modification of its articles of association.

REAL ESTATE TRANSFER TAX

10% in Luxembourg city, 7% outside Luxembourg city.

CAPITAL GAINS TAX ON THE SALE OF ASSETS

29.22% (for corporates in Luxembourg city, for 2013).

Under certain conditions, a rollover of the gain may be available, provided that the proceeds of the sale are reinvested into replacement assets.

CAPITAL GAINS TAX ON THE SALE OF SHARES

Corporate resident vendor

29.22%, unless the conditions for the Luxembourg participation exemption are met (notably 10% of the share capital or a participation representing an historic acquisition cost of EUR6m has been, or will be, held for at least 12 months); currency exchange gains in relation to the participation should also benefit from the exemption.

Individual resident vendor

- Taxable if the vendor has held a substantial participation (at least 10% of the share capital).
- If the vendor has not held a substantial participation (at least 10% of the share capital), only taxable if the shares have been sold less than six months after the acquisition.

Non-resident corporate or individual vendor

- Taxable only if the vendor has held a substantial participation (at least 10% of the share capital) in a Luxembourg company and (i) the shares are sold within six months of the acquisition, or (ii) if the shares are sold more than six months after the acquisition, the non-resident used to be a Luxembourg tax resident for at least 15 years, and became non-resident less than five years before the disposal.
- Exempt if shares have been held in certain specific vehicles (and notably in undertakings for collective investment, with a corporate form).

AVOIDANCE OF CAPITAL GAINS TAX

If certain conditions are realised, latent capital gains will not be disclosed upon mergers and demergers, and share for share exchanges, both at the level of the shareholders and the companies.

PRESERVATION OF TAX LOSS CARRY-FORWARD

Loss carry-forward is, in principle, not limited in time. However, in the event of a merger, losses realised by a company which will cease to exist as a separate taxpayer as a consequence of the merger may no longer be carried forward.

Furthermore, the right to carry forward losses may be denied (within the frame of a share deal) if the transaction is considered as being abusive from a tax perspective.

Opportunities and threats

In this section an overview is provided of opportunities to maximise relief for acquisition costs (such as financing costs), as well as other items which require attention when designing an efficient tax structure.

STEPPING-UP ASSET VALUES

- Amortisation of goodwill and intangible assets is possible.
- There is no possibility of achieving a depreciable step-up in an acquisition of shares.

TAX CONSOLIDATION RULES

The tax consolidation regime is optional and available for corporate income tax and municipal business tax. No tax consolidation system exists for wealth tax.

Group companies can opt for tax consolidation, but each company remains an individual taxpayer. This regime allows one or more Luxembourg-resident subsidiaries (ie fully taxable Luxembourg-resident companies) of a Luxembourg parent company to be considered as fiscally integrated with the parent company.

The following conditions must be fulfilled:

- the parent company has to be a fully taxable Luxembourg company;
- the parent company must hold at least 95% of the share capital of each of the consolidated subsidiaries (the 95% shareholding condition has to be satisfied from the beginning of the first financial year for which the tax consolidation regime is requested without interruption), which have to be fully taxable Luxembourg companies;
- the application must be submitted to the Luxembourg tax administration before the end of the first financial year for which the tax consolidation regime has been applied; and
- the tax consolidation regime must operate for at least five years. Otherwise, the benefit of the tax consolidation regime will be withdrawn retroactively.

Under certain conditions, the benefit of the tax consolidation can be obtained even if the 95% participation threshold is not reached, in which case the parent has to hold a participation of at least 75%, and at least 75% of the minority shareholders has to approve the tax consolidation. Furthermore, if the 95% threshold is not reached, tax consolidation is also subject to the recommendation of the Minister of Finance. This is generally only available if, in the Minister of Finance's opinion, the participation is capable of promoting the development and the structural improvement of the national economy.

Even Luxembourg permanent establishments of non-resident companies which are fully subject to tax corresponding to Luxembourg income tax may qualify as parent companies for the purposes of the tax consolidation regime. Subsidiaries which are held indirectly by the parent company through a transparent company (eg a partnership) or through fully taxable companies may also be fiscally integrated.

DEBT/EQUITY RULES

Based on administrative practice, the debt-to-equity ratio is set at 85:15. It applies to loans granted by related parties for the financing of shareholdings. Interest paid on the excessive part of the debt will be subject to dividend withholding tax and will not be deductible for tax purposes.

CONSEQUENCES OF GUARANTEES FROM A RELATED PARTY FOR THIRD PARTY DEBTS

The debt-to-equity ratio also applies to loans granted by third party lenders if guaranteed by group members.

HYBRID LOANS

Non-interest bearing loans are considered as equity for the purposes of the debt-to-equity ratio. As a result, the capitalisation of a company corresponding to up to 1% of the total financing, 14% being financed by a non-interest bearing loan and 85% being financed by an interest bearing loan, will in principle be deemed acceptable by the Luxembourg tax administration.

Based on administrative practice, the tax classification of a hybrid loan shall be made based on the substance over form principle. Depending on their legal features, hybrid loans may thus qualify as equity or as debt from a Luxembourg tax perspective.

The participation exemption is in principle available only in relation to participations held in the share capital of a company. However, hybrid loans may qualify for the participation exemption regime under certain conditions (based on the substance over form principle).

TAX CREDIT OR EXEMPTION TO AVOID DOUBLE TAXATION

Dividends and capital gains derived from qualifying participations are exempt under the Luxembourg participation exemption.

Under most tax treaties entered into by Luxembourg, foreign-sourced income and capital gains are either exempt (eg real estate assets or permanent establishment) or entitle the Luxembourg recipient to a tax credit for the foreign withholding taxes (subject to certain limitations).

CONTROLLED FOREIGN COMPANY LEGISLATION

No controlled foreign company (**CFC**) legislation.

TRANSFER PRICING

If transfer prices are exclusively motivated by a particular relationship that a Luxembourg company has with a non-resident taxpayer, but are not based on sound business reasons, the tax administration may reassess the company's taxable profits.

The Luxembourg direct tax administration has issued a circular which relates to the tax treatment of intra-group financing transactions, and which endorses the OECD transfer pricing guidelines. In addition, the latter circular formalises the process for applying for an advance pricing agreement.

RESIDENCE

Under domestic tax law, a Luxembourg-resident company is a company incorporated under the laws of Luxembourg or which has its central administration in Luxembourg.

TAXATION OF DISTRIBUTIONS RECEIVED FROM SUBSIDIARIES

Dividends (including liquidation proceeds) received by a fully taxable resident company may be tax exempt based under the Luxembourg participation exemption regime if certain conditions are met (notably 10% of the share capital or representing an acquisition cost of at least EUR1.2m has been, or will be, held for at least 12 months).

Should the conditions of the participation exemption regime not be met, the fully taxable Luxembourg-resident company may, under certain conditions, still benefit from a 50% tax exemption on dividends received.

WITHHOLDING TAXES

Dividend distributions by a Luxembourg fully taxable company to its shareholders are, in principle, subject to a 15% withholding tax. However, the withholding tax may be reduced under the provisions of a double tax treaty. A full withholding tax exemption may also be obtained under certain conditions based on the domestic participation exemption regime (notably 10% of the share capital or a participation representing an historic acquisition cost of least EUR1.2m has been, or will be, held for at least 12 months by a qualifying shareholder). However, no withholding tax is due in Luxembourg on the payment of a liquidation surplus, regardless of the tax residence and tax status of the shareholder. Similarly, no withholding tax is in principle due on a partial liquidation, which could be the case upon complete and final exit of one of the shareholders.

Under Luxembourg tax law, no withholding tax is generally levied on interest payments made by a fully taxable Luxembourg company unless they pertain to certain profit-sharing bonds (or similar securities), they are paid to a silent partner (*baillieur de fonds*) receiving a profit-sharing return or they are recharacterised as a hidden profit distribution (eg if the payments are not in line with the arm's length principle).

Certain interest payments made by a Luxembourg paying agent to non-resident individuals or so-called residual entities established in the EU or certain dependent or associated EU territories may fall within the scope of the Luxembourg domestic legislation which has transposed the provisions of the EU Savings Directive. Where a withholding tax applies, the rate currently stands at 35%. No withholding tax is due if the beneficiary opts for the exchange of information as foreseen by the EU Savings Directive. It is expected that Luxembourg will abolish the withholding system in favour of automatic exchange of information under the EU Savings Directive as of 1 January 2015.

For Luxembourg-resident individuals, a 10% withholding tax applies to certain interest payments made by a Luxembourg paying agent. (This 10% withholding tax is in full discharge of income tax if the individual is acting within the framework of the management of his private wealth.)

Royalties paid in connection with intellectual property rights are, in principle, not subject to withholding tax.

Other

This section describes other opportunities and threats that should be taken into account when structuring tax-efficient mergers and acquisitions.

ANTI-ABUSE REGULATIONS

In Luxembourg, a structure chosen by a taxpayer may not be accepted by the tax administration if the administration considers the structure to be an abuse of law. A structure is deemed abusive by the administration when it allows the taxpayer to reduce taxes but is not justified by economic or other non-tax reasons or is inappropriate for the realisation of the purpose of the transaction.

Contacts



Jean Schaffner

Partner

Tel +352 44 44 5 5410
jean.schaffner@allenoverly.com



Patrick Mischo

Partner

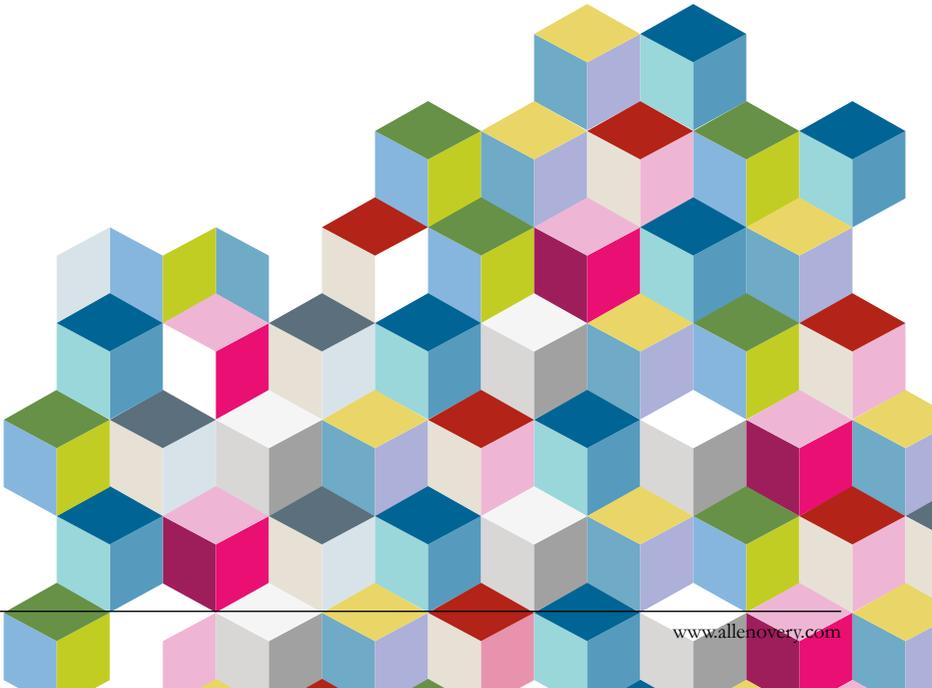
Tel +352 44 44 5 5429
patrick.mischo@allenoverly.com



Florent Trouiller

Counsel

Tel +352 44 44 5 5430
florent.trouiller@allenoverly.com



Netherlands

Transaction taxes

In this section we identify taxes that will be imposed on the vendor and the acquirer upon a transfer of assets or upon a transfer of shares, as well as other tax implications of a transfer of assets or shares.

STAMP DUTY ON THE TRANSFER OF SHARES

Nil, or 6% in a case where an interest of at least one-third in a real estate company is transferred (a reduced rate of 2% applies for private houses held by the real estate company).

CAPITAL DUTY PAID ON THE CONTRIBUTION OF CAPITAL

Not applicable.

REAL ESTATE TRANSFER TAX

6% or a reduced rate of 2% for private houses.

CAPITAL GAINS TAX ON THE SALE OF ASSETS

Capital gains on the sale of assets are taxed at the statutory corporate income tax rates of 20% on the first EUR200,000 taxable income and 25% on taxable income exceeding EUR200,000 (2013 rates).

CAPITAL GAINS TAX ON THE SALE OF SHARES

Corporate vendor

Capital gains realised upon the sale of a qualifying participation are exempt from corporate income tax under the participation exemption regime (more than 5% interest and where certain other requirements are met); otherwise gains are taxed at the statutory corporate income tax rate of 25% (20% on the first EUR200,000).

Individual vendor

Capital gains realised upon the sale of shares are taxed at 25% income tax if the shares form part of a substantial interest (more than 5%) in the company held by the seller or his/her family. If the shares do not qualify as a substantial interest, but the shares form part of a business enterprise of the individual, the capital gains are treated as ordinary business profits, taxable at progressive income tax rates (up to 52%). Otherwise nil.

AVOIDANCE OF CAPITAL GAINS TAX

If certain requirements are met, an asset merger, share-for-share merger, legal merger or demerger can be executed on a tax-free basis, by rolling over the taxable basis.

PRESERVATION OF TAX LOSS CARRY-FORWARD

Losses incurred in the current fiscal year may be carried back to the preceding year, and can be carried forward for nine years.

Certain restrictions apply for loss carry-forward. Carry-forward of losses is no longer possible if a substantial change of ownership has taken place (30% or more of the ultimate shareholders changed) in comparison to the year in which the company incurred the loss. Exceptions to this rule apply for certain bona fide cases (eg transfer to a party that already owned an ultimate interest of one-third or more; the change in the ultimate interest is not unusual and could not be known by the company (listed companies); active companies which did not and will not reduce their activities by more than 70% in a certain period prior to and after the change of shareholders). Losses incurred prior to a substantial change in ownership in a tax year cannot be utilised by way of loss carry-forward, nor by loss set-off against profits derived in the same tax year after the change in ownership took place.

If during (almost) the entire year, 90% or more of the company's activities consisted of the holding of participations or the direct or (in)direct financing of related parties, the loss incurred in that year may be offset only against profits of any subsequent year if during (almost) the entirety of such year: (i) the company was engaged in the same activities to the same degree; and (ii) the book value of its group receivables reduced by the book value of its group payables

does not exceed the net book value of such receivables and payables at the end of the year in which the loss was incurred. Exceptions to this second condition apply for certain bona fide cases, eg if the company can demonstrate that a change in this balance was not mainly intended to increase the ability to set off losses.

NON-RESIDENT VENDORS: CAPITAL GAINS TAX ON THE SALE OF SHARES

Corporate vendor

Taxable at a rate of 25% (20% on the first EUR200,000 taxable income) with respect to business income derived from an enterprise (including Dutch real estate) that is conducted through a permanent establishment or permanent representative in the Netherlands and with respect to income from a substantial interest in a company resident in the Netherlands, provided that: (i) this substantial interest is not attributable to the business of the non-resident shareholder; and (ii) the interest in the company resident in the Netherlands is held with the main goal, or one of the main goals, to avoid income tax or dividend withholding tax of another party.

Individual vendor

25% if the shares form part of a substantial interest (more than 5%) in the company held by the seller or his/her family and this substantial interest is not attributable to an enterprise and no tax treaty protection is available on the basis of which the capital gain is taxable only in the country of residence. Otherwise nil.

VALUE ADDED TAX

Value added tax (**VAT**) may be charged on supplies of goods and services made in the Netherlands. As a general rule, it is possible to obtain a refund for VAT charged by a supplier of goods or services if one is considered a VAT entrepreneur performing an economic activity and supplying VAT-taxable products and/or services. An acquisition vehicle or holding company, of which the sole purpose is to acquire and/or hold shares without any direct involvement in the management of the subsidiaries, is usually not regarded as performing an economic activity or supplying taxable services.

A transfer of a going concern (**TOGC**, *algemeenheid van goederen*) is not considered to be a transfer or service for VAT purposes.

Opportunities and threats

In this section an overview is provided of opportunities to maximise relief for acquisition costs (such as financing costs), as well as other items which require attention when designing an efficient tax structure.

STEPPING-UP ASSET VALUE

- Upon an asset purchase, the part of the purchase price allocable to each separate asset that is acquired forms the basis for depreciation for that asset and the base costs of such asset for future capital gains tax.
- Amortisation of acquired goodwill (at least over a period of ten years) and intangible assets is possible.
- There are no possibilities of achieving a depreciable step-up in an acquisition of shares.

TAX CONSOLIDATION RULES

Upon joint request, a Dutch-resident parent company and its, at least 95%-owned, Dutch-resident subsidiary or subsidiaries may form a fiscal unity for corporate income tax purposes if other requirements are met. On the basis of the Dutch fiscal unity rules:

- the tax is levied as if the subsidiary is absorbed by the parent company;
- a consolidated tax return is filed by the parent of the fiscal unity;
- profits of one company can be set off against losses of other companies forming part of the same fiscal unity;
- inter-company transactions between companies included in the same fiscal unity are disregarded; and
- splitting of profits is necessary for carrying forward pre-fiscal unity losses or carrying-back fiscal unity losses to pre-fiscal unity years.

There is no limit to the number of companies that may belong to a fiscal unity, nor need there be any relation between their business activities.

DISALLOWED INTEREST RELIEF (OTHER THAN THIN CAPITALISATION RULES)

There is a disallowance of interest relief for loans obtained from a related company that are used for certain categories of tainted transactions (circular transactions and certain group transactions), unless the company paying the interest can provide evidence that both the transaction as such and the loan are based mainly on sound business reasons, or that the interest is subject to at least 10% taxation in the hands of the recipient.

There is a disallowance of the interest relief on loans obtained from a related company that have no fixed maturity or a maturity of more than ten years that bears no interest, or an interest rate which is substantially lower than that which would have been agreed between unrelated parties.

GUARANTEE FROM A RELATED PARTY FOR THIRD PARTY DEBTS

A guarantee from a related party may taint third party debt, unless the sole purpose of the guarantee was to obtain a lower interest rate. Accordingly, the guaranteed debt may fall within the scope of rules that limit deductibility of interest expense. Where the guarantee is given to enhance the company's capacity to obtain third party finance, that portion of the debt that could not be borrowed without the guarantee will be tainted.

DISALLOWED INTEREST RELIEF OF ACQUISITION DEBT

The deduction of interest paid or accrued to related parties and third parties is restricted where it concerns acquisition debt on acquisitions made on or after 15 November 2011, whereby the company that is acquired with the acquisition debt is subsequently included in a fiscal unity for Dutch corporate income tax purposes with the borrower. If the acquisition vehicle has no taxable income itself, the interest exceeding a threshold of EUR1m per year is not deductible insofar as the acquisition debt at the end of the fiscal year exceeds 60% of the acquisition price. Over a period of seven years, this percentage is reduced by 5% each year to 25%. As of 1 January 2013 the deductibility of interest on loans related to participations is further limited. The tax deduction of so-called excessive interest related to participation will not be deductible to the extent the excessive part is higher than EUR750,000. The amount of non-deductible interest is calculated as follows: non-deductible interest = total annual interest * (average participation debt/average total debt). The starting point for determining the amount of participation debt is that all participations are deemed to have been financed with equity. A company will only have participation debt if the total amount of the fiscal cost price of the participations exceeds the equity of the company holding the participations. This excessive amount is the participation debt. Dutch taxpayers that are actively involved in group financing activities are allowed to disregard debts, as well as the interest and costs relating to these debts, insofar as these debts are connected to group loans receivable. In determining the participation debt, special provisions apply in respect of a participation acquired on or before 1 January 2006. Furthermore, the rules do not generally apply in respect of the expansion of the operational activities of the group where the subsidiary forms part of the group.

HYBRID DEBT

Debt with certain equity features is considered to function as equity for tax purposes. The remuneration of and changes in the value, including write-offs, of these loans are not deductible.

NON-BUSINESSLIKE LOANS

In a case where the credit risk on loans with certain non-businesslike features has been accepted by a shareholder in its capacity as shareholder and not as a creditor, write-offs of such loans are not tax deductible. A non-deductible write-off loss can, however, result in a deductible loss upon liquidation of the participation that is the debtor of a non-businesslike loan.

TAX CREDIT OR EXEMPTION TO AVOID DOUBLE TAXATION

Under the participation exemption regime, all capital gains (including currency exchange differences) and income derived from a qualifying participation are exempt from Dutch corporate income tax and dividend withholding tax. The participation exemption applies to equity interests of more than 5% and provided certain other requirements are met (eg the subsidiary does not qualify as a low-taxed portfolio investment).

If the participation exemption applies to income from a qualifying subsidiary, a taxpayer is not entitled to a tax credit for underlying tax levied at the level of the subsidiary. For low-taxed investment companies a credit system applies with respect to foreign tax.

CONTROLLED FOREIGN COMPANY LEGISLATION

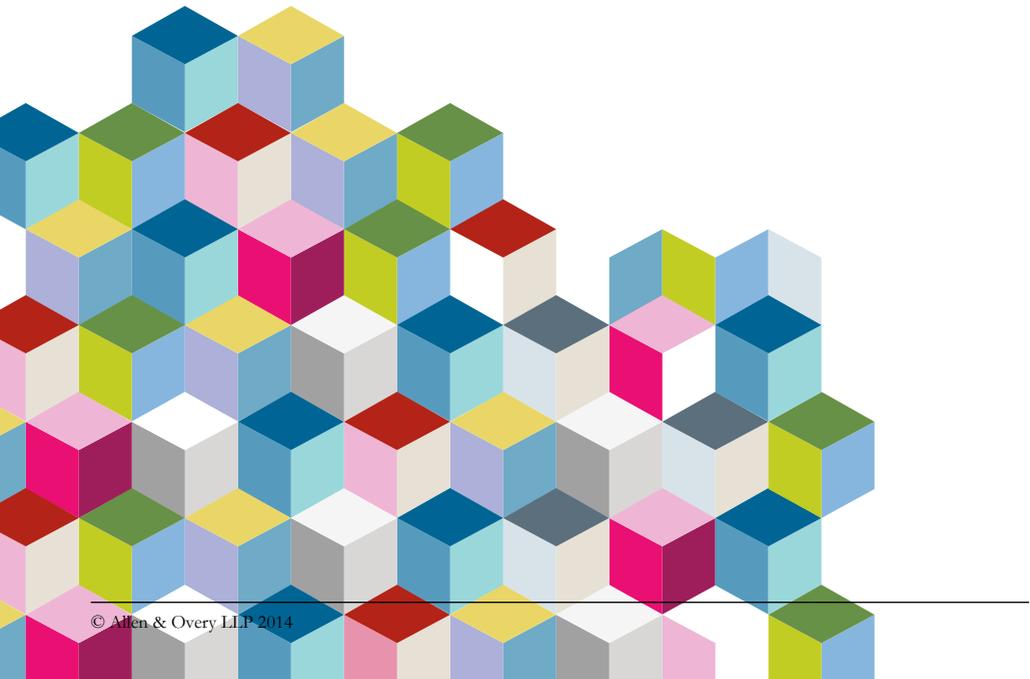
If a taxpayer participates in a company: (i) the assets of which consist of 90% or more of free portfolio investments; and (ii) the profits of which are not taxed at an effective tax rate of at least 10%, then such participation must be valued at fair market value in the books of the taxpayer provided that he (or together with a related entity) has an equity stake of at least 25% in such company.

TRANSFER PRICING

The Dutch Corporate Income Tax Act contains a general transfer pricing provision, stating that transactions between related parties and the pricing of such transactions should meet the arm's length test. The arm's length principle applies to a wide audience. It includes parties affiliated by a board relationship or a control relationship. It is mandatory to document inter-company transactions. If the tax authorities request information, the taxpayer must respond within four weeks. This period may be extended to three months for complex transactions.

RESIDENCE

Whether an entity is tax resident in the Netherlands is determined by reference to all relevant facts and circumstances, such as the seat of the board, the location of the head office and where the shareholders meet. Entities incorporated under Dutch law, such as BV and NV companies, are deemed to be resident in the Netherlands for the purposes of corporate income tax, except for the application of a limited number of articles in the Dutch corporate income tax act.



Other

This section describes other opportunities and threats that should be taken into account when structuring tax-efficient mergers and acquisitions.

CONDUIT COMPANIES

Special provisions apply to counter the use of companies that perform conduit financing or licensing activities within a group, unless they bear actual economic risk with respect to these activities. The interest or royalty income received or accrued by a non-qualifying conduit company is eliminated from taxable income. As a result, the company cannot credit any foreign withholding taxes. A non-qualifying conduit company is not considered the beneficial owner of the loan or licence; instead it is treated as an intermediary for the ultimate interest or royalty income recipient and has to report (at arm's length) remuneration for its intermediary services. A taxpayer is considered to bear actual economic risk on the finance activities, and can therefore credit foreign withholding taxes, if it has an amount of equity equal to at least the lower of 1% of the amount of the outstanding loans or EUR2m and this equity is actually exposed to risk in respect of the financing or licensing activities.

TAXATION OF EMPLOYEES' AND DIRECTORS' EQUITY INCENTIVES

Generally, assets and liabilities of an individual that are not treated as business income of that individual are subject to income tax under the regime for income from savings and investment. Under this regime, the individual is taxed upon the net fair market value of its assets and liabilities (including stocks and shares and including debt). The net value of assets and liabilities in this category is subject to income tax at 1.2% on the fair market value of such assets as at 1 January of a tax year.

In the event that individuals have acquired shares, receivables or other rights that have to be considered to be granted with the intention of forming a remuneration for services (to be) rendered by the individual or a related person, these qualify as a "lucrative interest". Income derived from such a lucrative interest will be taxed either: (i) as ordinary income at progressive rates up to 52%, if the lucrative interest is held directly by the individual; or (ii) as income from a substantial interest at a flat rate of 25%, if the lucrative interest is held through an entity in which the taxpayer holds more than 5%.

Shares constitute a lucrative interest if the shares qualify as:

- a subordinated class of shares that constitute less than 10% of the total share capital of the company; and
- preferential shares with entitlement to a preferential dividend of at least 15% per year.

The taxable income from lucrative interests also comprises a (partial) waiver of debts as compensation for work carried out by the individual or a related person.

Depending on the specific provisions in a tax treaty, foreign taxpayers will normally be protected against this domestic tax liability pursuant to tax treaties concluded by the Netherlands.



Contacts



Godfried Kinnegim

Partner

Tel +31 20 674 1120
godfried.kinnegim@allenoverly.com



John Brouwer

Partner

Tel +31 20 674 1541
john.brouwer@allenoverly.com



Jochem Kin

Counsel

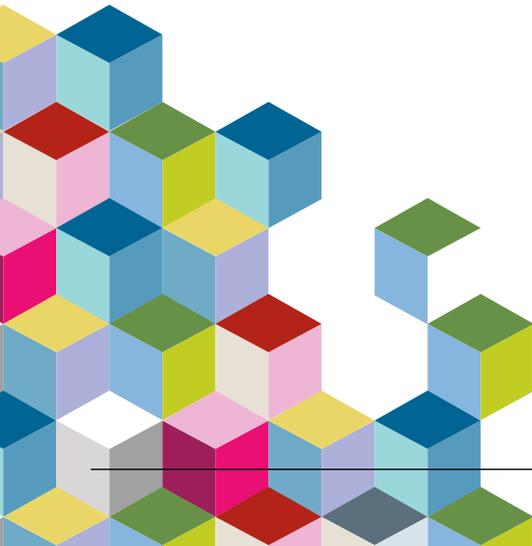
Tel +31 20 674 1173
jochem.kin@allenoverly.com



Rens Bondrager

Senior Associate

Tel +31 20 674 1314
rens.bondrager@allenoverly.com



Poland

Transaction taxes

In this section we identify taxes that will be imposed on the vendor and the acquirer upon a transfer of assets or upon a transfer of shares, as well as other tax implications of a transfer of assets or shares.

STAMP DUTY ON THE TRANSFER OF SHARES

There is a 1% transfer tax (*Podatek od Czynności Cywilnoprawnych* – **PCC**) charged on the market value of the shares, payable by the purchaser.

Exemption is available for the purchase of the shares of a joint-stock company (*Spółka Akcyjna* – SA) if: (i) the purchaser is an investment firm; or (ii) an investment firm acts as an intermediary in the sale; or (iii) the sale is on an organised market; or (iv) the sale is by an investment firm which purchased the securities on an organised market.

CAPITAL DUTY PAID ON THE CONTRIBUTION OF CAPITAL

PCC of 0.5% is charged on registered share capital only. There is no capital duty on share premiums. There are no regulations on the allowable proportion of share premium against registered share capital.

REAL ESTATE TRANSFER TAX

PCC of 2% is charged on the market value of the real estate sold (except where the real estate transfer is subject to value added tax (**VAT**) and not VAT exempt). If the sale of shares is of a real estate company, PCC is only charged on the sale of the shares (1% as a rule – please see above).

Any debts or liabilities associated with real estate do not diminish its tax base.

CAPITAL GAINS TAX ON THE SALE OF SHARES

In principle, there is a 19% flat rate tax for individuals; the revenue and associated tax deductible costs are amalgamated with other revenues earned (classified as capital gains), and costs incurred in the given tax period.

Capital gains are taxed at 19% for corporate income tax payers, and capital gains on the sale of shares are considered as for any other business revenues, so the revenue and associated tax-deductible costs are amalgamated with other revenues earned and costs incurred in the given tax period.

AVOIDANCE OF CAPITAL GAINS TAX

As a rule, holding companies in countries with participation exemption on capital gains are used (Luxembourg and Cyprus being foremost).

Polish corporations/individuals holding shares for sale sometimes transfer them to the above mentioned jurisdictions prior to the sale: corporations mainly utilise an exchange of shares; and individuals by an exchange of shares or a donation.

Another optimisation method involves using partnerships limited by shares or tax groups. Due to increased efforts to close tax loopholes by the Polish tax authorities, review of these structures at the end of 2014 will be necessary.

NON-RESIDENT VENDORS

Non-resident vendors are not usually taxed on a sale of shares in Poland because of tax treaties.

Any particular tax treaty should be verified. A sale of assets is taxable at the level of the seller.

SPIN-OFF (DEMERGER) RELATED TO 50% CHANGE IN CONTROL TRANSACTION

The transaction is tax-neutral if both parts of the business (the part remaining in the company and the other part separated out to another company) constitute organised parts of a business. Otherwise, the transaction is taxable as a sale of assets.

VALUE ADDED TAX

A sale of shares is considered as outside of, or exempt from, VAT. The sale of the business is also outside of VAT.

Opportunities and threats

In this section an overview is provided of opportunities to maximise relief for acquisition costs (such as financing costs), as well as other items which require attention when designing an efficient tax structure.

TAX CONSOLIDATION RULES

There is no VAT consolidation; consolidation is only available for corporate income tax. So far, this has not been a popular instrument. The requirements include that:

- only a Polish limited company (Sp. z o.o.) or joint stock company (S.A.) is allowed to form a group;
- there is a flat structure (one head company holding at least 95% of the shares of all the other companies, which are prohibited to hold shares in further companies and cannot be related – on the terms specified in the transfer pricing regulations – with companies not participating in the fiscal group);
- there is an average share capital of PLN1m (about EUR250,000); and
- there is a minimum 3% profitability.

There is an alternative consolidation of income tax upon the formation of an income tax transparent partnership (general or limited).

THIN CAPITALISATION RULES

Thin capitalisation is no obstacle in practice, as it only applies to loans of direct shareholders and loans from entities which have the same direct shareholder as the borrower (a 25% voting rights threshold in each case).

The allowable debt-to-equity ratio is 3:1. Equity is defined as the registered share capital less the contributions in the form of debt-to-equity swaps or non-depreciable intangibles.

Change of the rules is expected at the end of 2014.

DEBT/EQUITY RULES

There are no other rules other than the thin capitalisation rules.

DISALLOWED AND DEFERRED INTEREST (OTHER THAN DEBT/EQUITY RULES)

As a rule, interest is tax deductible if the debt is incurred for taxable revenue generating activity.

In general, interest is tax deductible on a cash basis, ie when paid and not when accrued.

Interest paid or accrued during an investment phase, until the day the investment is brought into use, shall be capitalised to the tax value of the investment and not expensed.

CONSEQUENCES OF GUARANTEES FROM A RELATED PARTY FOR THIRD PARTY DEBTS

Unless there is a corporate benefit, the guarantor should be remunerated at arm's length: otherwise the deemed taxable income could be recognised.

There are no provisions on disallowance of tax-deductibility of interest in such a case. However, back-to-back loans could potentially be challenged on the basis of tax abuse regulations and thin capitalisation regulations could apply (but this is a rather theoretical threat).

HYBRID LOANS

The concept of treating loans as equity is not developed in Poland. A Polish company can be at the "receiving" end but will rather not provide a debt treated as equity in Poland.

CONTROLLED FOREIGN COMPANY LEGALISATION

Controlled foreign company (CFC) legislation is expected to be introduced from January 2015.

PASSIVE FOREIGN INVESTMENT COMPANY ANTI-DEFERRAL REGIME

No passive foreign investment company (PFIC) regulations apply.

TRANSFER PRICING

The arm's length principle should be followed. The relationship is based on a 5% direct or indirect shareholding as well as on personal ties (family, the same board members).

If the transaction value exceeds certain thresholds, statutory transfer-pricing documentation must be provided within seven days of the request of the tax inspector. If the taxpayer fails, any additional income is taxable at a 50% penalty tax rate (compared to the normal 19%).

RESIDENCE

A company is considered to be a Polish tax-resident if it has a registered seat and/or place of management in Poland (there are no mechanisms of verification of the latter and we are not aware of any tax authorities' practice in verifying the place of management).

Entity classification ("Check-the-Box" rules) – no options.

TAXATION OF DISTRIBUTIONS RECEIVED FROM SUBSIDIARIES

There is an exemption under the implemented Parent Subsidiary Directive. However, dividends from non-EU or EEA companies or dividends from subsidiaries in which the Polish company does not hold at least 10% of the shares for an uninterrupted period of two years are subject to regular 19% tax.

WITHHOLDING TAXES

Domestic rates: 19% for dividends, 20% for interest, 20% for royalties.

For dividends, a withholding tax exemption is available for payments to qualifying EU or EEA companies under the implemented Parent Subsidiary Directive.

For interest and royalties, under the Interest and Royalties Directive, withholding tax exemption for payments between qualifying affiliated EU or EEA companies is available.

Further exemptions or rate reductions are available under double taxation treaties.

LEGAL AND BENEFICIAL OWNERSHIP NOT SEPARATED

In general, the Polish tax authorities would regard the legal owner as also being the beneficial owner. There are no regulations/rules/practices of separating the legal and beneficial owners.

However, in cashpooling transactions the tax authorities and the administrative courts consider the pool leader as not being a beneficial owner of received interest and deny it tax treaty protection (regardless of the cashpooling structure). Consequently, it can be expected that some concept of beneficial ownership will be developed over time.

FINANCIAL ASSISTANCE

In principle, and with some exceptions, financial assistance is prohibited in the case of a joint stock company (S.A.); however, it is not prohibited in the case of a limited liability company (Sp. z o.o.).

NO PROPER PARTICIPATION EXEMPTION REGULATIONS

A parent company is not entitled to deduct the corporate income tax payable by its Polish subsidiary. Moreover, a dividend distribution from the subsidiary to its parent is subject to 19% withholding tax, unless the parent company holds at least 10% of the subsidiary's shares for an uninterrupted period of at least two years. There is no participation exemption for capital gains.

NEW EXEMPTION FOR FOREIGN INVESTMENT FUNDS

Collective investment institutions having their registered office in an EU Member State other than Poland or in another EEA country and which jointly satisfy certain conditions (eg their scope of business consists solely of collective investing of funds gathered as a result of public or private offerings of interest in securities, money market instruments and other property rights and their business is regulated by the relevant authorities of their home country) are exempt from Polish income tax. This applies to income tax on any source of income, including dividends, interest, royalties and capital gains.

Other

This section describes other opportunities and threats that should be taken into account when structuring tax-efficient mergers and acquisitions.

BINDING RULINGS

A taxpayer can apply for a binding interpretation of a tax law applicable to its particular case. The procedure takes up to three months from the date the application is filed and does not involve any significant administrative costs. The ruling fully protects the applicant until a change in the approach is delivered to the taxpayer and a grace period lapses.

ANTI-ABUSE REGULATIONS

There is no real substance-over-form principle in tax law. However, the tax authorities can verify whether the given legal relationship exists or if it is as declared by the parties. In the case of a sham transaction hiding a real transaction, tax consequences shall be derived from the hidden transaction. However, if the same economic effect can be obtained in various ways, the taxpayer is allowed to choose whichever triggers the smallest tax burden. If the tax authorities challenge whether the given legal relationship exists between the parties, they should apply to a Civil Court for an assessment.

Under general civil law regulations, abusive transactions are ineffective.

INTEREST TAXABLE ON CASH BASIS

Interest is treated as a tax-deductible cost or taxable revenue upon payment (not accrual).

Contacts



Wojciech Pietrasiewicz

Senior Associate

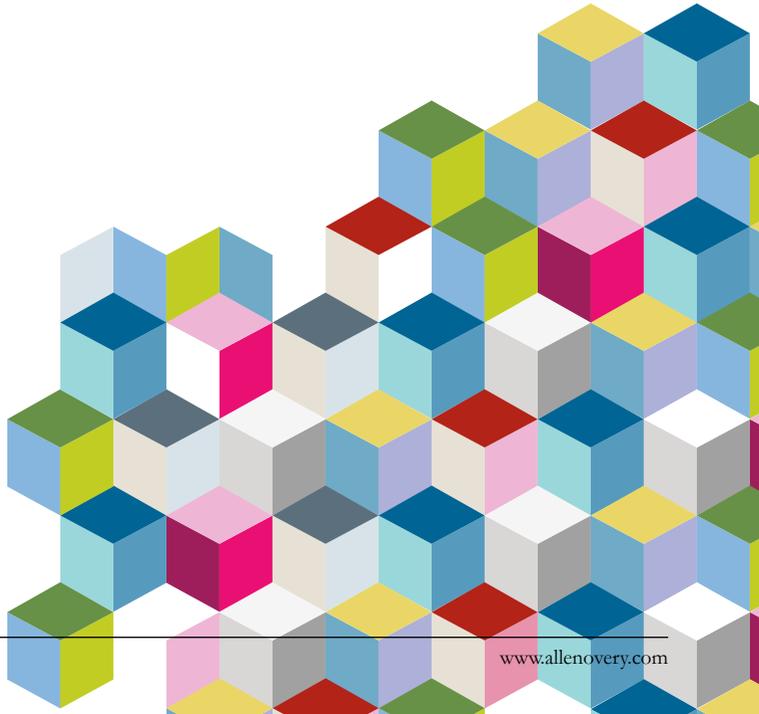
Tel +48 22 820 6225
wojciech.pietrasiewicz@allenoverly.com



Maciej Kulawik

Senior Associate

Tel +48 22 820 6135
maciej.kulawik@allenoverly.com



Spain

Transaction taxes¹³

In this section we identify taxes that will be imposed on the vendor and the acquirer upon a transfer of assets or upon a transfer of shares, as well as other tax implications of a transfer of assets or shares.

STAMP DUTY ON THE TRANSFER OF SHARES

Generally the transfer of shares is exempt from both value added tax (**VAT**) and real estate transfer tax (**RETT**).

However, a transfer in the secondary market of unquoted securities will be subject either to RETT or to VAT as a disguised transfer of real estate assets included in the assets of the company whose securities are transferred to the extent that such transfer of shares attempts to circumvent the payment of taxes applicable to the transfer of the underlying real estate assets.

Under certain circumstances, transfers of shares of real estate companies are deemed to involve such purpose unless there is evidence to the contrary.

General RETT rate is 7%. However, the applicable tax rate may vary, depending on the region where the assets are located.

CAPITAL DUTY ON THE CONTRIBUTION OF CAPITAL

The following transactions are exempt from capital duty: (i) incorporation of Spanish entities; (ii) capital increases; and (iii) contributions made by the shareholders which do not involve a capital increase. Restructuring transactions, such as mergers, spin-offs, share-for-share exchanges and contributions in kind are not subject to capital duty.

¹³ The Government of Spain is planning a material reform of the main taxes. According to the bill for a law ("*proyecto de ley*") which has been recently published (and is still subject to parliament discussions) the tax reform is expected to affect several points of the Spanish section which will be accordingly updated once the new rules are approved and become enforceable.

REAL ESTATE TRANSFER TAX

Generally 7%, although the tax rate applied may vary depending on the region where the assets are located. VAT (refundable) may be applicable, excluding the application of transfer tax.

CAPITAL GAINS TAX ON THE SALE OF ASSETS

Corporate vendor

30%; in the event that the proceeds of the sale are reinvested, a tax credit of 12% may apply, thus reducing the effective taxation to 18%.

Individual vendor

Short-term capital gains, which comprise capital gains and losses arising from a transfer of assets acquired within the one-year period prior to the transfer date, will be included in the general element of the taxable income subject to personal income tax (**PIT**).

The general part of the taxable base is subject to progressive rates, which currently range between 23.75% and 56%. Progressive rates vary depending on the Region where the individual vendor resides.

Long-term capital gains, which comprise capital gains and losses arising from the transfer of assets which are held for a period exceeding one year, will be included in the savings part of the taxable base.

Generally, any income included in the PIT savings element up to EUR6,000 will be taxed at a rate of 19% and the excess over such amount will be subject to a rate of 21%.

However, for the tax years 2013 and 2014, any income included in the PIT savings element will be taxed at the following three new tax rates: income up to EUR6,000 will be taxed at a rate of 21%; income from EUR6,000.01 to EUR24,000 will be taxed at a rate of 25%; and the excess over EUR24,000 will be subject to a tax rate of 27%.

Non-resident vendor

Generally, 19%; Tax Treaty reduced rates/exemption if applicable.

However, for the tax years 2013 and 2014, capital gains obtained by non-resident vendors will be taxed at the rate of 21%.

CAPITAL GAINS TAX ON THE SALE OF SHARES

Corporate vendor

Spanish shares: 30% (reinvestment tax credit may reduce effective taxation to 18%); tax credit available in relation to undistributed profits, provided that certain requirements are met.

Non-Spanish shares: in the event that the participation exemption applies, capital gains arising from non-Spanish shares shall be exempt from taxation (more than 5% participation; more than a one-year holding period; subject to analogous or identical taxation to Corporate Income Tax (CIT), among other requirements). Otherwise, 30% (a reinvestment tax credit may reduce the effective taxation to 18%). The participation exemption in respect of capital gains arising from non-Spanish shares may still apply on a proportional basis if some of the requirements are not met.

Individual vendor

Short-term capital gains will be included in the general part of the taxable base. The general part of the taxable base is subject to progressive rates, which currently range between 23.75% and 56%. Progressive rates vary depending on the region where the individual vendor resides.

Long-term capital gains will be included in the savings element of the taxable income subject to PIT.

Generally, any income included in the PIT savings element up to EUR6,000 will be taxed at a rate of 19% and the excess over such amount will be subject to a rate of 21%.

However, for the tax years 2013 and 2014, any income included in the PIT savings element will be taxed at the following three new tax rates: income up to EUR6,000 will be taxed at a rate of 21%; income from EUR6,000.01 to EUR24,000 will be taxed at a rate of 25%; and the excess over EUR24,000 will be subject to a rate of 27%.

Non-resident vendor

Generally, 19%; Tax Treaty reduced rates/exemption, if applicable.

However, for the tax years 2013 and 2014, capital gains obtained by non-resident vendors will be taxed at the rate of 21%.

AVOIDANCE OF CAPITAL GAINS TAX

The Spanish tax-neutral regime may apply to reorganisation transactions for mergers, spin-offs, share-for-share exchanges and contributions in kind, achieving deferral in the taxation of any capital gains realised.

PRESERVATION OF TAX LOSS CARRY-FORWARD

In a share deal, the amount of tax loss carry-forward in the target company will be reduced by an amount equal to the positive difference between the value of shareholders' contributions made on any basis, corresponding to the interest acquired in the target company, and its acquisition value, when the following requirements are met:

- (i) the majority of the share capital or the rights to participate in the entity's results have been acquired by a person or an entity, or by a group of related persons or entities, after the end of the tax period in which the relevant tax losses were suffered;
- (ii) the persons or entities to which paragraph (i) above refers had a participation of less than 25% at the end of the tax period in which the relevant tax losses were suffered; and
- (iii) the entity has not performed any economic transactions during the six months prior to the acquisition of the interest which confer a majority in the share capital.

In the case of corporate reorganisations, tax losses are also reduced under certain circumstances.

Tax losses are not transferred in an asset deal.

For tax periods commencing in 2013, 2014 and 2015, a temporary limitation on the offset of tax losses carried forward is included: companies with a turnover between EUR20m and EUR60m will be able to offset 50% of those pending tax losses, while companies whose turnover exceeds EUR60m will be able to offset 25%.

Generally, tax losses can be carried forward up to a maximum of 15 years after their generation. However, as a consequence of the limitation on the offset of tax losses carried forward, the term to offset pending tax losses has been extended, as from 1 January 2012, from 15 to 18 years.

NON-RESIDENT VENDORS

Generally, 19%; Tax Treaty reduced rates/exemption if applicable.

However, for the tax years 2013 and 2014, capital gains obtained by non-resident vendors will be taxed at the rate of 21%.

GROUP RESTRUCTURING

The Spanish tax neutral regime may apply to reorganisation transactions such as mergers, spin-offs, share-for-share exchanges and contributions in kind, achieving a deferral in the taxation of any capital gains realised, provided that certain requirements are met.

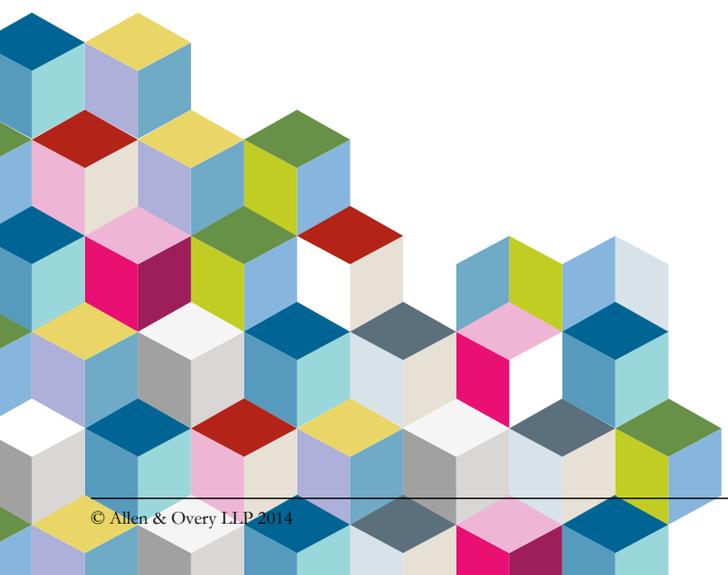
VALUE ADDED TAX

The transfer of shares is generally exempt from VAT. However, a transfer in the secondary market of unquoted securities will be subject either to RETT or to VAT as a disguised transfer of real estate assets included in the assets of the company whose securities are transferred to the extent that such transfer of shares attempts to circumvent the payment of taxes applicable to the transfer of the underlying real estate assets.

Under certain circumstances, transfers of shares of real estate companies are deemed to involve such purpose unless there is evidence to the contrary.

VAT rate is 21%.

A transfer of assets may be subject to (refundable) VAT, under certain circumstances, excluding the application of Transfer Tax as a result.



Opportunities and threats

In this section an overview is provided of opportunities to maximise relief for acquisition costs (such as financing costs), as well as other items which require attention when designing an efficient tax structure.

STEPPING-UP ASSET VALUES

Asset deal – The portion of the purchase price attributed to the assets is treated as the basis for depreciation and the base cost for future capital gains tax.

Amortisation of goodwill and intangible assets is possible. For the tax periods commencing in 2013, 2014 and 2015, the amortisation of goodwill arising from an asset deal is limited to 1% per annum.

Share deal – No step-up and no goodwill, unless a subsequent merger occurs.

Subject to certain requirements, there is the possibility of achieving a depreciable step-up and goodwill after a merger. For the tax periods commencing in 2013, 2014 and 2015, the amortisation of goodwill resulting from a merger is limited to 1% per annum.

Acquisition of foreign entities; financial goodwill amortisation – Following the EU Commission decisions published in the EU Official Gazette on 11 January 2011 and 21 May 2011, the amortisation of financial goodwill embedded in a share deal is no longer deductible for tax purposes as it is considered a state aid incompatible with the EU common market principles.

However, the tax deductions arising from acquisitions of EU foreign companies formalised before 21 December 2007 which met all the requirements to benefit from tax deduction shall continue to apply during the complete amortisation period. Similarly, tax deductions arising from acquisitions of non-EU companies formalised before 21 May 2011, provided that certain requirements are met, shall continue to apply during the complete amortisation period.

For the tax periods commencing in 2013, 2014 and 2015, the annual amortisation of financial goodwill, which is tax deductible, is reduced from 5% to 1%.

TAX CONSOLIDATION RULES¹⁴

The application of the Spanish tax consolidation regime, and consequently the formation of a tax group (or fiscal unity) for CIT purposes, is possible when two or more companies decide to form a tax group, provided all of them are resident in Spain and there is one dominant company upon which all the others are dependent. The dominant company has to fulfil the following requirements:

- it must be a legal entity subject to and not exempt from CIT;
- it must have a direct or indirect participation of at least 75% (70% in the event that the shares of the dependent companies are admitted to trading on a regulated market) in the share capital of the other companies on the first day of the tax period in which the tax consolidation regime is to be applied;
- its participation must be maintained uninterruptedly during the period of application of the tax consolidation regime (unless the company in which the participation is held is dissolved);
- it must not be dependent on any other Spanish-resident company that meets the requirements for being considered a dominant company; and
- it must not be subject to the special regime applicable to the European and Spanish Economic Interest Grouping and Joint Ventures.

Spanish permanent establishments of foreign companies can also be considered dominant companies of a Spanish tax consolidation group, provided that such foreign companies: (i) are not dependent on any other Spanish resident company that meets the requirements for being considered a dominant company; and (ii) are resident for tax purposes in a State that has entered into a double tax treaty with Spain containing an exchange of information clause.

In such cases, the dependent entities shall be those Spanish companies whose shares/participations are directly held by the permanent establishment.

In general terms, under the tax consolidation regime:

- the tax group's taxable base is calculated by adding together the taxable profits and losses of the group companies;
- inter-company transactions are disregarded;
- the tax group files a consolidated tax return;

¹⁴ Tax consolidation rules are currently under scrutiny by the EU authorities/courts.

- the profits of one company may be offset against the losses of another; and
- pre-consolidation tax losses pending compensation by a company at the time of its inclusion in a tax group may be offset against the group's positive taxable base up to the limit of said company's individual taxable base, provided that the group's consolidated taxable base is positive.

LIMITATION ON INTEREST RELIEF

Net financing expenses (arising from both third party loans and intra-group loans) incurred by Spanish tax-resident entities as from 1 January 2012 are tax deductible up to 30% of their EBITDA. "Net financing expenses" refer to the excess of financing expenses over income derived from the lending of own-capital to third parties. In any case, annual financial expenses up to EUR1m are tax deductible even if this exceeds the 30% threshold.

Any excess over the 30% threshold can be carried forward for an 18-year period. If net financing expenses accrued in the tax year do not reach the 30% threshold, the unused amount of financing expenses of that particular year can be added to the threshold to be computed in the following five years.

For entities belonging to a tax consolidation group, the 30% threshold will be referred to the tax consolidation group.

This new limitation imposed on the deductibility of financing expenses will not apply in respect of Spanish tax-resident entities in the year in which they are extinguished, with some exemptions. Credit entities and insurance entities are not affected by these new rules (except for non-credit entities belonging to the same tax consolidation group).

DISALLOWED INTEREST RELIEF OF INTRA-GROUP ACQUISITION DEBT

Interest arising from intra-group debt used either for the acquisition of equity stakes from group companies or for the contribution of equity to other group companies is no longer tax deductible, unless it can be evidenced that it is made for valid business reasons.

HYBRID LOANS

Profit-participating loans are treated as equity for corporate law purposes and as debt for tax purposes.

Profit-sharing arrangements/silent partnerships are treated as debt for tax purposes.

CONTROLLED FOREIGN COMPANY LEGISLATION

Controlled foreign company (**CFC**) provisions apply when the amount of CIT effectively paid by the non-resident entity in relation to “passive income” is lower than 75% of the amount that would have been due under Spanish CIT rules.

As of 1 January 2008, CFC rules are not applicable in respect of foreign entities which are EU resident for tax purposes, provided that: (i) their incorporation and operation derives from valid economic reasons; and (ii) they develop business activities.

HOLDING COMPANIES

Spain offers a favourable tax regime (the ETVE regime) for investments in foreign qualifying subsidiaries. Non-Spanish investors are generally tax exempt on dividends and capital gains arising from Spanish holding companies.

SPANISH REITs

Spain offers a favourable tax regime (the SOCIMI regime) for Spanish REITs engaged in either the acquisition of urban real estate for renting or the holding of participations in other Spanish or non-Spanish REITs as its main corporate purpose. Spanish REITs complying with certain requirements may benefit from a 0% Corporate Income Tax rate provided that their direct shareholders with an equity stake of at least 5% are taxed at least at a 10% rate on dividends received (if shareholders' taxation is lower than 10%, the Spanish REIT will be taxed at a rate of 19% on the gross amount of dividends distributed to those shareholders).

TRANSFER PRICING

According to Spanish transfer pricing rules, transactions carried out between related parties will have to be valued by the parties involved at market value. Additionally, the Spanish tax authorities are entitled to check whether such transactions have been effectively valued at market value by the parties involved, and are entitled to carry out the relevant corrections to the valuations, if necessary. The breach of the obligation to value at market value constitutes a tax infringement which triggers the corresponding tax penalty.

RESIDENCE

Entities which meet any of the following requirements will be considered to be resident in Spanish territory:

- entities incorporated in accordance with Spanish law;
- entities with their registered office in Spanish territory; or
- entities with their effective place of management in Spanish territory.

In this respect, an entity will be deemed to have its effective place of management in Spanish territory when the management and control of its overall activities are situated therein.

Finally, under certain circumstances, Spanish tax authorities may regard an entity established in a low-tax or tax-haven jurisdiction as tax resident in Spain when its main assets or business interests are directly or indirectly located in Spain.

ENTITY CLASSIFICATION (“CHECK-THE-BOX”) RULES

Spain does not have check-the-box rules.

In order to be eligible for U.S. check-the-box purposes, Spanish companies must be incorporated in the form of a *Sociedad Limitada (S.L.)*. *Sociedades Anónimas (S.A.)* are only eligible for U.S. check-the-box purposes if they are converted into an S.L.

TAXATION OF DISTRIBUTIONS RECEIVED FROM SUBSIDIARIES

Generally, dividend payments and other distributions received by a Spanish company from its subsidiaries will be subject to taxation at the level of the Spanish company.

However, dividends may benefit from certain tax credits or tax exemptions provided that certain requirements are met:

- (i) Domestic tax credit.
 - A 50% tax credit in respect of Spanish source dividends: the Spanish company would be

¹⁵ 30% is the current general Corporate Income Tax rate.

subject to an effective tax rate of 15% (50% of 30%¹⁵) in respect of Spanish dividends.

- A 100% tax credit when the dividends derive from Spanish entities in which an interest of at least 5% is held, provided that this interest has been held without interruption for the year prior to the dividend distribution date or, failing that, it is held, after such distribution date, for the necessary time to complete such one-year period.

In addition, the domestic tax credit would also apply in cases where the qualifying participation in the Spanish subsidiary has been reduced to at least 3%, without having transferred the remainder of the participation, but as a result of the Spanish subsidiary carrying out any of the transactions foreseen under the Spanish tax-neutral regime (mergers, spin-offs, share-for-share exchanges and contributions in kind) or a transaction within the public offering (OPA) regime. This new development would only apply within the three-year period following the execution of the relevant transaction.

Notwithstanding the above, under a specific anti-abuse provision no tax credit at all will be available for dividends on shares purchased within the two months prior to the dividend payment date if the shares, or similar shares, are sold within the two months following such date.

(ii) Tax exemption and international tax credit on dividends.

A Spanish company may benefit, in respect of foreign dividends, from a tax exemption when a number of requirements are met, namely: a minimum 5% holding, directly or indirectly held; a one-year holding period; and subject-to-tax test and performance of a business activity to be met by the foreign subsidiary.

This tax exemption will not be available when the equity investment in a foreign company has been made for the main purpose of benefiting from this tax exemption.

Should this tax exemption not apply, foreign taxes paid abroad (directly or indirectly) on dividends obtained will be deductible for Spanish tax purposes (up to the amount of tax that would have been paid in Spain if the relevant dividends had been paid in Spain), provided that the interest held is at least 5% and is held for at least one year.

WITHHOLDING TAXES

Dividends

Generally, dividends are subject to withholding tax at a rate of 19% on their gross amount. However, for the tax years 2013 and 2014, the withholding tax rate has been increased up to 21%. The withholding made constitutes an advance payment of the taxpayer's final income tax liability.

However, no withholding tax is imposed on dividends received by a Spanish company which is entitled to the 100% tax credit for the avoidance of domestic double taxation mentioned

above. This requires a one-year holding period prior to the distribution date.

Dividends distributed by a Spanish company to a non-Spanish resident company are, as a general rule, subject to taxation and to withholding tax in Spain at a rate of 19%. However, for the tax years 2013 and 2014, the withholding tax rate has been increased to 21%. Save for the exemption that may apply under the Parent-Subsidiary Directive, under the ETVE regime or a reduced tax rate under an applicable Tax Treaty, no reductions or tax credits apply.

It should be noted that the withholding tax exemption under the Parent-Subsidiary Directive would not apply in cases where the majority of the ultimate investors in the EU parent company are not resident for tax purposes in an EU Member State (apart from certain situations justifying the existence and role of the EU parent company).

Interest

Generally, interest payments by a Spanish borrower are subject to withholding tax at the current rate of 19%. However, for the tax years 2013 and 2014, the withholding tax rate has been increased to 21%. The borrower is responsible for making the withholding tax arrangement and for settling its obligation vis-à-vis the Spanish tax authorities through monthly or quarterly tax returns.

However, interest withholding tax does not apply in respect of:

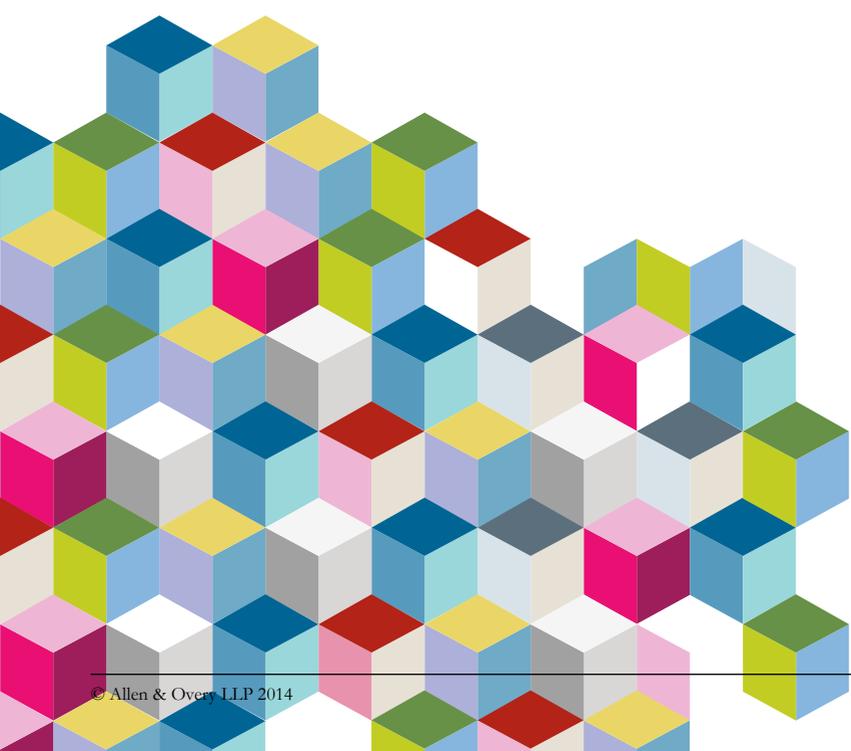
- a lender which is a Spanish bank or savings bank or a Spanish branch of a foreign bank; and
- a lender resident for tax purposes in an EU Member State (other than Spain), or a permanent establishment of an EU-resident situated in another EU Member State, not acting through a territory considered as a tax haven under Spanish law (as currently set out in Royal Decree 1080/1991, of 5 July) nor through a permanent establishment in Spain, and provides the Spanish borrower with, prior to any interest payment date, a tax residence certificate issued by the relevant tax authority (which is valid for one year from its date of issue).

Alternatively, a reduced withholding tax rate or tax exemption as set out in any applicable treaty for the avoidance of double taxation ratified between Spain and the relevant jurisdiction (a **Tax Treaty**) may apply, provided that the lender: (i) is effectively protected by the Treaty; (ii) does not carry on business through a permanent establishment in Spain (with which any principal and interest payable under the relevant financing agreement is effectively connected); and (iii) prior to any interest payment date, provides the Spanish borrower with a tax-residence certificate (or the equivalent document that may have been agreed in the applicable Tax Treaty) duly issued by the competent tax authority of its country of residence, stating that said recipient is tax-resident in the relevant jurisdiction within the meaning of the applicable Tax Treaty. This certificate (or equivalent document) is valid for one year from its date of issue.

Royalties

Generally, royalty payments made by a Spanish resident entity to a non-Spanish resident are subject to withholding tax at the general rate of 24%. However, for the tax years 2013 and 2014, the tax rate applicable to royalties has been increased to 24.75%.

Please note, however, that as from 1 July 2011, royalty payments made by a Spanish resident entity or permanent establishment located in Spain of another EU-resident entity to an entity resident in another EU Member State or a permanent establishment located in an EU member state of another EU resident are exempt from withholding tax and taxation in Spain, provided that certain requirements are met and that the payer and the recipient are related entities.



Other

This section describes other opportunities and threats that should be taken into account when structuring tax-efficient mergers and acquisitions.

ANTI-ABUSE REGULATIONS

The Spanish special tax-neutrality regime for reorganisations contains an anti-avoidance provision. This establishes that the Spanish tax authorities can reject the application of the special tax regime if the transaction has been carried out mainly for the purposes of tax fraud or evasion. In particular, Spanish CIT Law establishes that the special tax regime will not be applicable if the transaction has not been carried out for genuine business reasons, such as the restructuring or rationalisation of the activities of the companies involved, but rather for the purposes of achieving a tax advantage.

Therefore, unless sufficient economic and business reasons can be given for carrying out a reorganisation transaction, its implementation and the corresponding tax-neutrality achieved may be challenged by the Spanish tax authorities.

TAXATION OF EMPLOYEES' AND DIRECTORS' EQUITY INCENTIVES

Taxation of stock options given to employees free, or for a price lower than their market value, will depend on whether or not the stock options are transferable or tradable options.

Transferable or tradable options

The Spanish tax authorities would argue that the grant of options constitutes a taxable event for employees. This would be taxed as ordinary employment income (ie salary) subject to tax at progressive rates, which range from 23.75% to 56%, depending on the region where the employee is resident. Such ordinary employment income should be included by the employees in their PIT return corresponding to the year in which the options are granted.

Options neither transferable nor tradable

Employees will be taxed on exercising the options (not on the granting of the options). The taxable benefit is the market value of the shares on exercise (the quoted value in the case of listed shares) less the exercise price paid for the shares.

However, the taxable gains realised on the exercise of options may benefit from a special tax regime on employees' share option schemes if: (i) the offer made is within the company's general compensation policy; (ii) the beneficiaries are active employees; (iii) the employee, together with his/her close relatives, holds less than 5% of the company's shares; and (iv) the employee keeps the shares for a minimum period of three years. In such cases, taxable gains will be exempt up to EUR12,000 per year. The relevant income which cannot benefit from the exemption will have to be included in the PIT return of the year in which the options are exercised. This will constitute ordinary employment income (ie salary), subject to the above-mentioned progressive tax rates. Tax charges will be levied if the employee sells the shares within three years. A 40% reduction may be applicable to that part of the income which cannot benefit from the above exemption if the following requirements are met:

- the income qualifies as “long-term income”; that is the income must have a generation period of at least two years (ie two years must elapse between the granting and the exercise of the options); and
- the options are not granted annually.

The reduction base cannot be higher than EUR300,000 in any event.

The employer in Spain is responsible for making a payment on account (*ingreso a cuenta*) regarding the employee's income that cannot benefit from the above-mentioned exemption, at the time the options are exercised. This is also the case if the options were granted by the Spanish employer's foreign parent company.

The employee is also liable for PIT on gains obtained upon the transfer of shares, which will not be subject to withholding tax.

ACQUISITION STRUCTURE

Acquisitions in Spain are typically made through a leveraged local holding company which forms a Spanish tax group with the target company. Such fiscal unity allows the offsetting of financial cost against the target's operating income.

The ability effectively to deduct the financing costs against the target's operating income is subject to the 30% cap previously described.

FINANCIAL ASSISTANCE

Under section 150.1 of the Spanish Share Capital Companies Law, a joint stock company (*Sociedad Anónima* or **S.A.**) is prohibited from granting any kind of financial assistance for the purchase of its own shares or the shares of its holding company.

Article 143.2 of the Spanish Share Capital Companies Law provides an extended prohibition for limited liability companies (*Sociedad de Responsabilidad Limitada* or **S.L.**). This article also prohibits an S.L. from granting financial assistance for the acquisition of its own shares and of shares of any other company in its group of companies.

CONVERSION OF DEBT INTO SHARE CAPITAL

Generally, this transaction will not generate any taxable income for the debtor.

As a general rule, any premium a creditor obtains upon the conversion of any debt instrument is deemed taxable income (interest). Potential withholding tax will be levied on interest income.

Any previous write-off made by a creditor of such debt against its taxable income may be recaptured.

A debtor would obtain the tax-deductible costs on the conversion premium, if any.

Contacts

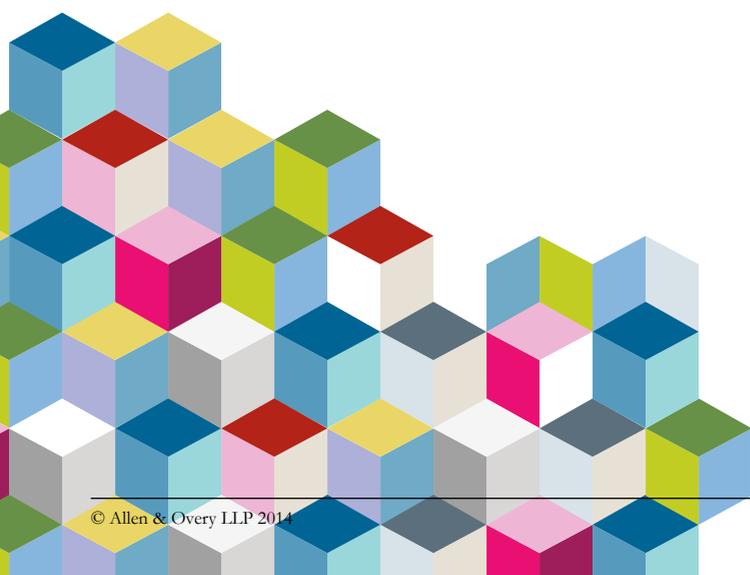


Carlos Albiñana

Partner

Tel +34 91 782 9962

carlos.albinana@allenoverly.com



United Kingdom

Transaction taxes

In this section we identify taxes that will be imposed on the vendor and the acquirer upon a transfer of assets or upon a transfer of shares, as well as other tax implications of a transfer of assets or shares.

STAMP DUTY ON THE TRANSFER OF SHARES

Stamp duty reserve tax at a rate of 0.5% on agreements to transfer shares in UK companies (unless stamp duty is paid on a transfer of shares within six years of the agreement, in which case no stamp duty reserve tax is payable).

Stamp duty at a rate of 0.5% on instruments transferring shares in UK companies. Reliefs such as group relief may be available.

CAPITAL DUTY PAID ON THE CONTRIBUTION OF CAPITAL

Nil.

REAL ESTATE TRANSFER TAX

Stamp duty land tax of up to 4% (7% in the case of high-value residential property generally, and up to 15% in the case of residential property where the purchaser is a “non-natural person”) charged on value of consideration. Reliefs, including disadvantaged areas relief and group relief, may be available.

CAPITAL GAINS TAX ON THE SALE OF ASSETS

Corporate vendor – Chargeable gains are generally subject to corporation tax (the main rate is 21% for financial year 2014, and is expected to fall to 20% in 2015). Indexation allowance may be available. Separate income regimes apply to certain types of assets, including financial instruments, derivatives and certain intangible assets.

Individual vendor – The amount chargeable to capital gains tax is charged at the rate of 18% or 28% depending on the amount of the individual's total income and gains. An annual allowance may also be available. Entrepreneur's relief, which provides for a 10% rate of tax (subject to a lifetime limit of GBP10m) may apply to disposals of a business or part of a business owned by the individual for at least one year.

CAPITAL GAINS TAX ON THE SALE OF SHARES

Corporate vendor – Exempt where the substantial shareholdings exemption (**SSE**) applies. The SSE applies where a trading company (or member of a trading group) sells shares in a company in which it has had a substantial shareholding (broadly, a holding of 10% or more) for 12 months out of the previous two years and that company is a trading company or the holding company of a trading group. Where the SSE applies, there is no charge to corporation tax on chargeable gains, but note that any loss is unallowable.

Individual vendor – As above for the sale of assets. Entrepreneur's relief may apply to the disposal of shares in trading companies (and holding companies of trading groups) in which the individual holds at least 5% of the shares and is an officer or employee.

MITIGATION OF CAPITAL GAINS TAX

If certain requirements are met, certain share-for-share or share-for-debenture exchanges may enable any gain to be "held-over" or "rolled-over". In addition to certain structural requirements, these include (except in the case of certain disposals of shareholdings of 5% or less) the exchange being effected for bona fide commercial reasons and the exchange not forming part of a scheme or arrangement of which the main purpose, or one of the main purposes, is the avoidance of liability to capital gains tax or corporation tax.

PRESERVATION OF TAX LOSS CARRY-FORWARD

Generally, income losses arising for a company can be carried forward indefinitely. There are certain restrictions on the profits against which they can be set – for example, trading losses can only be set against future profits of the same trade. However, if in the three years before or after a change in ownership of the company there is a major change in the nature of its trade (or in the case of an investment company there is a significant increase in its capital/debt level following the change in ownership), the carrying-forward and carrying-back of income losses may be disallowed.

Income losses may be transferred to other members of a UK tax group as group relief in the same accounting period only.

Capital losses can be carried forward indefinitely and set against capital gains. However, the use of losses may be restricted if the company with the losses joins a new tax group.

It is possible to reallocate a gain or loss to another member of the group.

NON-UK VENDOR

A non-UK resident seller (not subject to UK corporation tax) should not generally be subject to UK tax on any chargeable gains arising from the sale of UK assets or shares in a UK company. UK capital gains tax is chargeable on certain “non-natural persons” disposing of UK residential property, and there are proposals to extend the charge for capital gains tax to any non-residents disposing of UK residential property from 2015.

A non-UK resident seller trading through a permanent establishment in the UK may be subject to corporation tax on profits or gains from the sale of UK situs assets (including UK shares) used for the purposes of the trade.

VALUE ADDED TAX

Value added tax (**VAT**) may be charged on a supply of goods or services. However, there is no charge of VAT on the sale or purchase of shares. Asset sales and purchases may be subject to VAT unless transfer of going concern (**TOGC**) relief applies.

Opportunities and threats

In this section an overview is provided of opportunities to maximise relief for acquisition costs (such as financing costs), as well as other items which require attention when designing an efficient tax structure.

STEPPING-UP ASSET VALUES

On an asset purchase, the amount paid for the assets forms the basis for depreciation (to the extent that the asset is eligible for capital allowances) or the base cost in the assets.

Amortisation of acquired goodwill and intangible assets (acquired or created after 1 April 2002) is possible in accordance with the accounting treatment (or at a fixed rate of 4% per annum of expenditure that is capitalised for accounting purposes).

On the acquisition of shares there is generally no step-up in the cost of the assets of the target company, nor is there an increase in any depreciation on allowances available to the target company. However, it may be possible to achieve a step-up in asset values (capital assets only and not new intangibles) by undertaking a hive-down of the business into a NewCo and selling the shares in the NewCo. A number of detailed considerations will be relevant.

TAX CONSOLIDATION RULES

UK corporation tax is calculated broadly by reference to a company's solus accounts, and the relevance of consolidated accounts and equity accounting is very limited in UK tax law. However, there are some restricted areas where a group's consolidated accounts may be relevant, such as the worldwide debt cap (see below) and the UK bank levy.

While there is no concept of "fiscal unity" or general consolidation of a group for UK tax purposes, it may be possible to surrender losses between members of a tax group or to make elections (for example, as regards the allocation of chargeable gains and losses) among members of a tax group. A tax group is specifically defined and is not necessarily the same as the group for accounting purposes.

DEBT/EQUITY RULES

There are no set requirements as to debt-to-equity ratios. However, where loans are made between connected persons, interest may be disallowed if the rate of interest or the amount of the loan exceeds what would have been agreed between independent parties, which will need to be assessed on the facts of each case.

DISALLOWED AND DEFERRED INTEREST (OTHER THAN DEBT/EQUITY RULES)

Deductibility of interest may be limited by reason of the following:

- UK transfer pricing rules – these apply to non-arm’s length transactions (including a series of transactions) between companies (either in the UK or overseas) in which one company participates, either on its own or acting together with other persons, in the management, control or capital of the other company (or a third party participates in both) where a UK tax advantage is obtained. As well as incorporating the UK debt/equity rules mentioned above, these rules also apply where the lender and borrower are unconnected but the loan is influenced by an associated person (for example, a guarantee is given by the parent), whether that person is in the UK or overseas;
- results-dependent interest;
- interest exceeds a reasonable commercial return;
- deferred interest payable to a connected person resident in a “non-qualifying territory” (broadly, tax havens) – allowed as a deduction in the accounting period when paid, not when accrued;
- loan stapled to equity in the borrower;
- loan with certain equity features (convertible or carrying the right to receive shares);
- loan with an “unallowable purpose” (generally a tax avoidance purpose);
- hybrid entities or hybrid instruments are present in a transaction if there is an intention to obtain a UK tax advantage; and
- interest deductions may be disallowed where the UK worldwide debt cap rules apply (ie very broadly, where net UK financing deductions exceed aggregate worldwide group financing expenses as disclosed in the group accounts).

CONSEQUENCES OF GUARANTEES FROM A RELATED PARTY FOR THIRD PARTY DEBTS

The UK transfer pricing rules may apply to disapply any UK tax advantage (for example, restricting the deductibility of interest) where guarantees (and other arrangements) are provided by a related party, but generally only where the loan would not have been made at all to the borrower or exceeds the amount which would have been lent in the absence of the guarantee. A UK related party guarantor may have to impute arm's length guarantee fees for UK tax purposes.

HYBRID LOANS

Loans with certain equity features may be classified as equity for tax purposes, resulting, for example, in potential de-grouping. Equity-like characteristics may also affect the deductibility of interest paid – see above.

Hybrid loans that are treated as debt in the UK but equity in another jurisdiction may affect the deductibility of interest paid if there is an intention to obtain a UK tax advantage (for example, deductibility of interest) as a result of the use of the hybrid loan.

TAX CREDIT OR EXEMPTION TO AVOID DOUBLE TAXATION

The most common UK approach to relieving double taxation is the credit method, under which the foreign tax paid on an item of income is deducted from the UK tax payable on the same item of income (but there is no credit for overseas tax rates which are higher than the UK domestic rate, nor can excess credits be recovered in cash). Although there are provisions permitting the crediting of underlying tax paid by non-UK subsidiaries in certain circumstances, for corporation tax purposes, dividends and other distributions from UK or non-UK companies potentially qualify for various wide-ranging exemptions, with the result that the vast majority of such distributions should be exempt from UK corporation tax. In addition, legislation permitting companies to elect for exemption for their profits from non-UK permanent establishments has been introduced.

CONTROLLED FOREIGN COMPANY LEGISLATION

The UK-controlled foreign companies (**CFC**) rules can cause a proportion of the profits of non-UK resident companies, controlled by persons resident in the UK, to be imputed to and taxed upon UK companies which have a “relevant interest” in the non-UK resident company. The rules do not apply unless the company would have at least 25% of the non-UK resident company’s profits attributed to it on a “just and reasonable” basis. A reformed CFC regime is taking effect during 2013, and is aimed at making the rules more territorial and focused on “artificial diversion of UK profits”. The new regime provides, in particular, for exemption or a low effective tax rate for certain intra-group finance income of a CFC.

NB – see also “Attribution of chargeable gains of companies” below.

TRANSFER PRICING

The arm’s length principle is included in UK tax legislation and applies to transactions between affected persons (where one such person is directly or indirectly participating (either on its own or acting together with other persons) in the management, control or capital of the other, or the same person(s) directly or indirectly participate(s) in the management, control or capital of the affected persons). The rules apply to transactions between parties within the scope of UK taxation as well as to cross-border transactions, wherever there is a UK tax advantage.

There is a requirement to keep records. Where transfer pricing applies between two UK companies, a balancing payment may be made to neutralise the effect of the transfer pricing adjustment, or corresponding adjustments may be made to avoid double taxation.

RESIDENCE

For the purposes of corporation tax, entities are generally resident in the UK for tax purposes if they are incorporated in the UK. A UK-incorporated entity may nevertheless be treated as a non-UK resident if it is so treated under the provisions of an applicable double tax treaty. Non-UK incorporated entities may be resident in the UK for tax purposes if their “central management and control” is exercised in the UK.

TAXATION OF DISTRIBUTIONS RECEIVED FROM SUBSIDIARIES

Dividends and other distributions received by a UK company will in general be exempt from tax provided that they do not give rise to a tax deduction in a jurisdiction outside the UK. The exemption will not be available to “small” companies receiving distributions from a company resident in a tax haven.

WITHHOLDING TAXES

The UK does not impose any withholding tax on the payment of dividends.

The payment of “annual” interest is subject to withholding tax (currently at 20%) under domestic law. However, many treaties provide a full exemption from this withholding provided that the necessary direction is obtained by the payer. A similar exemption may be available under the Interest and Royalties Directive where the payment is made to an EU company with the necessary shareholding. There are also a number of exemptions available under domestic law, in particular an exemption for interest paid on a “quoted Eurobond” and for interest paid to a UK corporation tax payer.

The payment of royalties connected with intellectual property is generally subject to withholding tax (currently 20%) when paid to a person outside the UK. An exemption may be available under a double tax treaty or under the Interest and Royalties Directive.

Other

This section describes other opportunities and threats that should be taken into account when structuring tax-efficient mergers and acquisitions.

ANTI-ABUSE REGULATIONS

Promoters who devise and market certain tax schemes and arrangements, and taxpayers who use them, are under a reporting obligation. A general anti-abuse rule has been introduced to counteract tax advantages resulting from certain tax-motivated arrangements which “cannot reasonably be regarded as a reasonable course of action” in relation to the relevant tax rule.

ATTRIBUTION OF CHARGEABLE GAINS OF COMPANIES

Under certain circumstances, UK-resident shareholders in a non-UK resident company which would be a “close” company if resident in the UK could be liable to UK tax in respect of capital gains made by the company, even where those gains have not been distributed to shareholders.

ANNUAL RESIDENTIAL PROPERTY TAX

There is an annual charge on certain “non-natural persons” holding residential property, at a scaled rate depending on the value of the property concerned, up to c. GBP140,000 for properties with a value in excess of GBP20m.

TAXATION OF EMPLOYEES’ AND DIRECTORS’ EQUITY INCENTIVES

There are complex rules for the taxation of securities options and securities incentives (including share issues and share options to incentivise managers in private equity transactions) received by employees and directors.

PATENT BOX

From 1 April 2013, a new “patent box” regime is to be phased in, under which companies will be able to elect for certain profits derived from patented inventions, or certain other medical or botanical innovations, to be subject to corporation tax at a reduced rate. Once the new regime has been fully phased in (due in 2017), the applicable rate will be 10%.

TIMING OF TAX RELIEF FOR INTEREST COSTS

In certain circumstances (in particular where the creditor is a connected party situated in a tax haven) tax relief for interest is given only when the interest is actually paid, rather than as it accrues. There are various mechanisms through which the structuring of tax relief on an accruals basis can be achieved.

INTEREST TAX RELIEF UTILISATION

It will be important to consider how tax relief for interest costs will be utilised, in particular where the Target is a corporate(s) rather than a business(es). Tax grouping will need to be considered, as will the possibility of a hive-up of the Target's business.

HIVE-UP/HIVE-DOWN

It may be worth considering moving a taxable source of income up into a company in the structure which has deductions accruing but where group relief cannot be used. (It should be remembered that losses can only be transferred by way of group relief in any one particular accounting period and cannot be carried back or forward to earlier or later periods by the company to which they are transferred.)

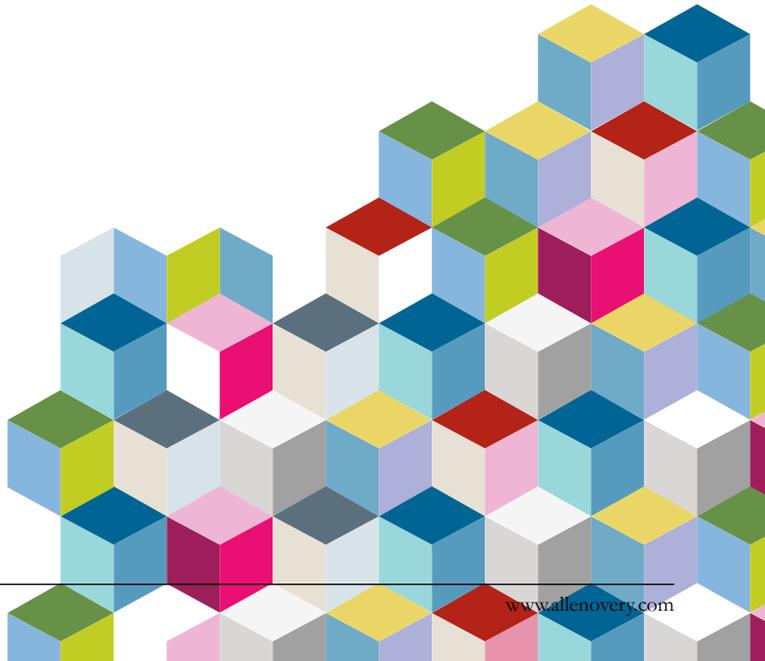
It may be advantageous to structure a business sale by way of a share sale of a subsidiary into which the business has been hived down. This may enable the purchaser to take the benefit of various tax attributes relating to the business, and to obtain a step-up of the assets' base costs to market value, and the seller may be able to take advantage of the substantial shareholdings exemption (see above) to exempt any gain.

ACQUISITION STRUCTURE

A structure involving one or more UK acquisition companies may be used (several companies may be used to facilitate the subordination of debt/equity). In such cases, tax reliefs for funding (whether interest, discount or premia) may be surrendered within the UK group, including to UK Target, as group relief. By contrast, if debt is provided to an overseas Topco acquiring a UK Target directly, interest deductions may well not be maximised in current accounting periods and may not arise in the UK.

FINANCIAL ASSISTANCE

Although not a tax issue as such, it may be necessary to consider the English financial assistance rules which, broadly, make it unlawful for an English public company whose shares are being, or have been, acquired (or a subsidiary of such a company) to give financial assistance for the purpose of that acquisition, or for an English public company to give such assistance in respect of an acquisition of shares in its private parent company (sections 678 and 679 of the Companies Act 2006) unless certain exceptions apply. These rules no longer apply to private companies.



Contacts



Vimal Tilakapala

Partner

Tel +44 20 3088 3611
vimal.tilakapala@allenoverly.com



Mark Middleditch

Partner

Tel +44 20 3088 3698
mark.middleditch@allenoverly.com



Christopher Harrison

Partner

Tel +44 20 3088 3638
christopher.harrison@allenoverly.com



Lydia Challen

Partner

Tel +44 20 3088 2753
lydia.challen@allenoverly.com



Charles Yorke

Partner

Tel +44 20 3088 4925
charles.yorke@allenoverly.com



Tim Harrop

Counsel

Tel +44 20 3088 3983
tim.harrop@allenoverly.com

United States

Transaction taxes

In this section we identify taxes that will be imposed on the vendor and the acquirer upon a transfer of assets or upon a transfer of shares, as well as other tax implications of a transfer of assets or shares.

STAMP DUTY ON THE TRANSFER OF SHARES

Not applicable at federal level. May apply at state level.

CAPITAL DUTY PAID ON THE CONTRIBUTION OF CAPITAL

Not applicable.

REAL ESTATE TRANSFER TAX

Not applicable at federal level. Most states impose a real estate transfer tax. Rates vary by state.

CAPITAL GAINS TAX ON THE SALE OF ASSETS

Resident corporate vendor

Up to 35% (top marginal rate).

Resident individual vendor

Generally, between 15% and 23.8% (if capital asset held for more than one year and not subject to depreciation recapture); up to 43.4% (top marginal rate) otherwise.

CAPITAL GAINS TAX ON THE SALE OF SHARES

Resident corporate vendor

Up to 35% (top marginal rate).

Resident individual vendor

Generally, between 15% and 23.8% (if capital asset held for more than one year); up to 43.4% (top marginal rate) otherwise.

NON-RESIDENT VENDORS

General

In general, non-resident vendors are not subject to U.S. tax on gains from the sale of assets or shares unless: (i) the gain is effectively connected with the non-resident vendor's conduct of a U.S. trade or business (**ECI**); (ii) in the case of gains realised by an individual non-resident vendor, the person is present in the U.S. for 183 days or more in the taxable year of the sale and certain other conditions are met; (iii) the non-resident vendor is subject to special rules applicable to certain expatriates; (iv) the gain is from the sale of certain intangibles sold for contingent payments; or (v) as discussed below, the gain is from the sale of a "U.S. real property interest" (**USRPI**).

FIRPTA

In general, under the Foreign Investment in Real Property Tax Act (**FIRPTA**), a non-resident's gain from the disposition of a USRPI is taxable in the U.S. as ECI, and the transferee of such an interest must withhold an amount of tax equal to 10% of the amount realised on the disposition. A USRPI includes an interest in real property located in the U.S. and any non-creditor interest in a U.S. corporation (but not a non-U.S. corporation) that is a U.S. real property holding corporation (**USRPHC**). A USRPHC is any corporation if the fair market value of its USRPIs equals or exceeds 50% of the fair market value of its: (i) USRPIs; (ii) foreign real property; and (iii) other trade or business property. A foreign person disposing of a non-creditor interest in a U.S. corporation generally is presumed to be disposing of a USRPI (and is therefore subject to a 10% purchase price withholding under FIRPTA) unless the foreign person obtains a statement from the corporation (or a determination from the U.S. Internal Revenue Service (**IRS**)) that the interest was not a USRPI as of the date of the disposition.

SPIN-OFF (DEMERGER) RELATED TO 50% CHANGE IN CONTROL TRANSACTION

Subject to complex and detailed rules, a spin-off (demerger) of the shares of a subsidiary can be tax-free to the distributing corporation and the recipient shareholders. An otherwise tax-free spin-off will, however, be taxable to the distributing corporation if, as part of a plan or series of related transactions, there is a direct or indirect 50% change in control of the distributing corporation or the spun-off subsidiary. A prohibited plan is presumed to exist if the change in control occurs within two years before or after the spin-off.

PRESERVATION OF TAX LOSS CARRY-FORWARD

General

Net operating losses (**NOLs**) generally can be carried back two years and forward 20 years. Subject to potential limitations, NOLs and other tax attributes remain available after taxable stock purchases, tax-free reorganisations, and parent-subsidiary liquidations, but are not available to the purchaser following taxable asset purchases.

Key Limitation on NOL Carry-forward

- If there is an “ownership change” of a “loss corporation” (ie a corporation with NOLs or “net unrealised built-in losses”), the amount of the loss corporation’s income in any post-change year that can be offset by pre-change losses cannot exceed the “Section 382 limitation” for such a year.¹⁶
- An “ownership change” generally occurs if, within a rolling three-year testing period, the percentage of stock of the loss corporation owned by one or more 5% shareholders has increased by more than 50 percentage points over the lowest percentage owned by such shareholder(s) at any time during the three-year testing period.
- The Section 382 limitation equals the value of the loss corporation’s stock immediately before the ownership change multiplied by a conservative discount rate (currently = 4.55%). The Section 382 limitation will be zero (ie no losses can be used) if the loss corporation’s business is not continued at all times for two years following the ownership change.

¹⁶All “Section” references herein are to the U.S Internal Revenue Code of 1986.

Opportunities and threats

In this section an overview is provided of opportunities to maximise relief for acquisition costs (such as financing costs), as well as other items which require attention when designing an efficient tax structure.

STEPPING-UP ASSET VALUES

Taxable Asset Acquisitions

The buyer gets a full fair market value basis step-up in acquired assets and therefore increased depreciation/amortisation and lower gain on the sale of property. It is possible to amortise goodwill and certain intangibles. The basis is allocated among seven classes of assets using the residual method with a specific system of priorities.

Taxable Stock Acquisitions (No Section 338 Election)

There is no basis step-up or amortisation of goodwill or intangibles owned by an acquired corporation.

Taxable Stock Acquisitions (With Section 338 Election)

A Section 338 election allows a “qualified stock purchase” to be treated as an asset purchase for U.S. federal income tax purposes. In general, a “qualified stock purchase” is a taxable purchase of at least 80% of a target’s stock during a 12-month acquisition period. There are two types of Section 338 election:

- Section 338(g) election. This is generally not used under current law because it triggers two levels of tax (ie taxable stock sale and taxable deemed asset sale by the target corporation); however, a Section 338(g) election may be beneficial if the target has ample NOLs or is a non-U.S. corporation (and not subject to U.S. tax on its deemed asset sale).
- Section 338(h)(10) election. In general, a Section 338(h)(10) election may be made when a U.S. target is purchased out of a U.S. affiliated group. Not available for non-U.S. targets. The election must be made jointly by buyer and seller. The seller bears the tax burden on the deemed asset sale; only one level of tax – stock sale is ignored for tax purposes.

TAX CONSOLIDATION RULES

- U.S. corporations connected by 80% stock ownership (vote and value) with a U.S. parent corporation generally may elect to file a consolidated federal income tax return.¹⁷
- The group is essentially treated as a single taxpayer. There is joint and several liability among members for group taxes; this is important when buying a member from a U.S. consolidated group, as it will retain liability for the taxes of other members of the group in periods prior to acquisition.
- A member's losses generally can offset the income of other group members, subject to certain limitations, such as those involving members entering and leaving the group.
- Inter-company dividends are excluded from income but stock basis must be reduced. It is possible to have negative stock basis, which may trigger a tax when an affected member leaves the group.
- Gains and losses from inter-company sales of property are deferred but may be triggered when the property or the buying or selling member leaves the group. Loss on the sale of member stock may be disallowed in certain cases.
- When a member enters or leaves the group, NOLs and other tax items must be allocated between the group and that member.
- In general, a U.S. corporation that is subject to the income tax of a foreign country may be prevented from using its NOLs to offset the income of another member of the corporation's U.S. group if such loss can also be used in a foreign jurisdiction to offset the income of another person. These rules may also affect a U.S. corporation's foreign partnership interests and branches in certain cases.

DEBT/EQUITY RULES

Whether an instrument is treated as debt or equity for U.S. tax purposes is a factual question that mainly depends on substance rather than form. Many factors are considered in making this generally all-or-nothing determination, including the issuer's debt-to-equity ratio. No single factor is controlling. A high debt-to-equity ratio is not necessarily fatal to debt treatment if such a ratio is normal for companies in the issuer's industry and the instrument otherwise has the indicia of debt.

¹⁷U.S. states often do not permit tax consolidation. Those that do may apply rules that are significantly different from the rules governing federal tax consolidation.

DISALLOWED AND DEFERRED INTEREST (OTHER THAN DEBT/EQUITY RULES)

Earnings Stripping Limitation

In general, if a corporation's debt-to-equity ratio exceeds 1.5:1, then no deduction is allowed currently for the lesser of: (i) "disqualified interest" paid or accrued by the corporation during a taxable year; or (ii) such corporation's "excess interest expense" (generally, the excess, if any, of a corporation's net interest expense over 50% of its "adjusted taxable income" for the year (roughly, EBITDA) plus any excess limitation carried forward). **Disqualified interest** is any interest paid or accrued by a corporation: (a) to a related person if no U.S. tax is imposed on the interest; or (b) to an unrelated person if: (A) a related foreign person (or U.S. tax exempt organisation) guarantees the debt; and (B) no U.S. gross-basis tax is imposed on the interest.

Limitation on Certain Acquisition Debt

In general, interest in excess of USD5m per year on certain acquisition debt is disallowed if a four-part test is met:

Purpose – The debt is issued by a corporation to provide consideration for the acquisition of stock (generally, at least 5%) or two-thirds of the business assets of another corporation;

Subordination – The debt is subordinated to claims of the issuer's trade creditors generally or is expressly subordinated to a substantial amount of the issuer's unsecured debt, whether outstanding or subsequently issued;

Equity participation – The debt is convertible into, or is sold as part of a unit with a warrant or option to acquire, stock in the issuer or in any member of its affiliated group; and

Financial ratios – The issuer's debt-to-equity ratio exceeds 2:1 or its average earnings for the past three years do not exceed three times the annual interest to be paid or incurred on the debt.

Deferral of Deduction Until Interest is paid to Foreign Lender

In general, no deduction is allowed for interest and original issue discount (**OID**) owed to a related foreign person and not effectively connected with a U.S. business of such foreign person until actual payment is made. This limitation also applies to interest and OID that is effectively connected with a foreign lender's U.S. business if the foreign lender claims an exemption or reduced rate of tax under a treaty.

Applicable High-Yield Discount Obligation (AHYDO)

An **AHYDO** is a debt instrument issued by a corporation with:

- a maturity of more than five years;
- a yield to maturity of at least five percentage points above the applicable federal rate (**AFR**); a rate of interest reflecting the borrowing rate of the U.S. federal government which is periodically revised; and
- significant OID.

In general, if a corporation issues debt that is classified as an AHYDO:

- deductions for OID are permanently disallowed to the extent, if any, attributable approximately to a yield in excess of six percentage points over the AFR; and
- to the extent not disallowed under the above, deductions with respect to OID are deferred until payment is made.

Interest Disallowance on Debt Payable in (or by Reference to) Equity

No interest deduction is allowed on debt issued by a corporation if a substantial amount of the principal or interest on the debt:

- is mandatorily paid in, or converted into, or determined by reference to the value of equity in the issuer or a related party;
- at the option of the issuer or a related party, can be so paid, converted or determined (regardless of the likelihood of the option being exercised);
- at the option of the holder or a related party, can be so paid, converted or determined (but only if there is a substantial certainty that the option will be exercised); or
- is part of an arrangement reasonably expected to result in such a payment, conversion or determination.

CONSEQUENCES OF GUARANTEES FROM A RELATED PARTY FOR THIRD PARTY DEBTS

See discussion of “earnings stripping” above. In addition, related-party guarantees raise the issue of whether the guarantor or the nominal obligor should be treated as the true obligor for tax purposes.

HYBRID LOANS

See response to “Debt/equity rules” above.

TAX CREDIT OR EXEMPTION TO AVOID DOUBLE TAXATION

The U.S. has a classical corporate tax system, which generally permits two levels of tax on corporate profits, one at the corporate level and one at the shareholder level. In addition to rules governing consolidated groups and foreign tax credits, the U.S. employs a “dividends-received deduction” (**DRD**) to help ensure that corporate profits are taxed no more than twice. The DRD generally permits a U.S. corporation to deduct a percentage of dividends received from another U.S. corporation (and from certain foreign corporations). The DRD is 100% in the case of 80-100% share ownership, 80% for 20-79.99% ownership, and 70% for ownership up to 20%.

CONTROLLED FOREIGN COMPANY ANTI-DEFERRAL REGIME

A “U.S. shareholder” of a “controlled foreign company (**CFC**)” must pay current U.S. tax on the CFC’s “Subpart F income”, regardless of whether the CFC makes actual distributions. A U.S. shareholder is a U.S. person that owns (directly, indirectly or constructively) at least 10% of the voting power of the foreign corporation. A CFC is a foreign corporation more than 50% of whose stock (by vote or value) is owned (directly, indirectly or constructively) by U.S. shareholders. In general, Subpart F income includes, among other types of income, certain passive investment income and certain income derived from dealings with related corporations where a foreign corporation is used to shift income away from related parties in high-tax jurisdictions. Subpart F income generally does not include active business income.

PASSIVE FOREIGN INVESTMENT COMPANY ANTI-DEFERRAL REGIME

In general, regardless of the level of U.S. ownership or control, a foreign corporation is a passive foreign investment company (**PFIC**) if:

- at least 75% of its gross income is passive; or
- at least 50% of its assets produce, or are held for the production of, passive income.

Any U.S. person that owns (directly, indirectly or constructively) any amount of stock in a PFIC is generally subject to the PFIC regime, which essentially denies U.S. persons the benefit of deferring U.S. tax on PFIC income. Under the PFIC regime, a U.S. person has two options:

- if certain requirements are met, it can elect to be taxed currently on its share of the PFIC's income or, in the case of certain "marketable" PFIC stock, to include any appreciation in the value of such stock in income on a mark-to-market basis; or
- it can avoid current tax but instead must pay tax and a significant interest charge when certain distributions are made and when PFIC stock is disposed of.

TRANSFER PRICING

Transactions between related parties (broadly interpreted) must be at arm's length and supported by contemporaneous documentation/transfer pricing studies. In the case of a transfer or licence of intangible property between related parties, the Section 482 "super-royalty" rule provides that the income with respect to such transfer or licence must be commensurate with the income attributable to the intangible property.

In general, under this super-royalty rule, the IRS has authority to make periodic adjustments to related-party royalty payments to take into account changes in the profitability of the transferred or licensed intangible, regardless of whether the consideration for the transfer or licence was at arm's length at the time the parties entered into the transfer or licence arrangement.

Other

This section describes other opportunities and threats that should be taken into account when structuring tax-efficient mergers and acquisitions.

RESIDENCE

Corporations (and other entities treated as corporations (eg publicly traded partnerships)) are “domestic” (and therefore taxable in the U.S. on their worldwide income) if they are created in or organised under the laws of the U.S. or any U.S. state. All other corporations are “foreign” and are subject to U.S. tax only on certain U.S.-source income and income connected with their U.S. businesses. Because partnerships are fiscally transparent, their situs often has limited importance in U.S. taxation, although partnership situs may be relevant for sourcing, withholding and reporting purposes. In general, a partnership is “domestic” if it is created in or organised under the laws of the U.S. or any U.S. state; otherwise, it is “foreign”.

ENTITY CLASSIFICATION (“CHECK-THE-BOX”) RULES

“Per Se” Corporations

In general, U.S.-incorporated business entities and non-U.S. business entities listed in U.S. tax regulations (including, for example, UK Plcs; Netherlands N.V.s; Belgium/France/Luxembourg/Spain S.A.s; Germany A.G.s; Italy S.p.A.s) are treated as “per se” corporations for U.S. tax purposes and cannot elect a different tax status.

Other Business Entities (ie “Eligible Entities”)

U.S. Eligible Entities. Unless an election is made to be treated as a corporation, a U.S. eligible entity (usually a limited liability company or LLC) is disregarded (ie treated as a branch) if it has a single owner, or is treated as a partnership if it has two or more owners.

Non-U.S. Eligible Entities. Unless an election is made to be treated otherwise, a non-U.S. eligible entity is:

- disregarded if it has only one owner and that owner has unlimited liability;

- treated as a partnership if there are two or more owners and at least one owner has unlimited liability; or
- treated as a corporation if all owners have (or the single owner has) limited liability.

Liability is limited for these purposes if under local law the owner has no personal liability for debts of or claims against the entity.

BRANCH PROFITS TAX

In general, a foreign corporation conducting a business in the U.S. through a branch is subject to U.S. corporate tax at 35% on the U.S. business income when earned. In addition, unless reduced or eliminated under a treaty, a 30% branch profits tax is imposed when the income is repatriated (or deemed repatriated) from the U.S. branch.

BRANCH INTEREST

There are two special rules governing interest paid by the U.S. business/branch of a foreign corporation. First, in general, interest paid by the U.S. branch is treated as if it were paid by a U.S. corporation; therefore, it is U.S.-source interest that may be subject to withholding tax unless exempt under treaty or domestic law. Second, in general, to the extent that the amount of interest allowable as a deduction in computing taxable income of the U.S. branch exceeds the interest actually paid by the branch, the excess is treated as interest paid by a U.S. corporation to the foreign parent corporation, which would be subject to 30% U.S. interest withholding unless reduced or eliminated under a treaty.

IRS ABILITY TO RECHARACTERISE TRANSACTIONS

In addition to numerous specific statutory and regulatory anti-abuse provisions, the IRS has general authority under statutory and case law to disregard sham transactions and steps in transactions in certain cases and to tax a transaction in accordance with its substance, rather than its form.

CONDUIT ENTITIES

There is judicial and regulatory authority to permit the IRS in certain cases to disregard intermediate entities for withholding tax purposes and to treat loan, licence and certain other transactions as taking place directly between the principal parties to the transaction if the intermediate entity is used as a mere conduit for tax avoidance purposes.

Contacts



Dave Lewis

Partner, U.S. Tax

Tel +1 212 756 1147

dave.lewis@allenoverly.com



Jack Heinberg

Partner, U.S. Tax

Tel +1 212 610 6383

jack.heinberg@allenoverly.com



Stephen Fiamma

Consultant, U.S. Tax

Tel +44 20 3088 3657

stephen.fiamma@allenoverly.com

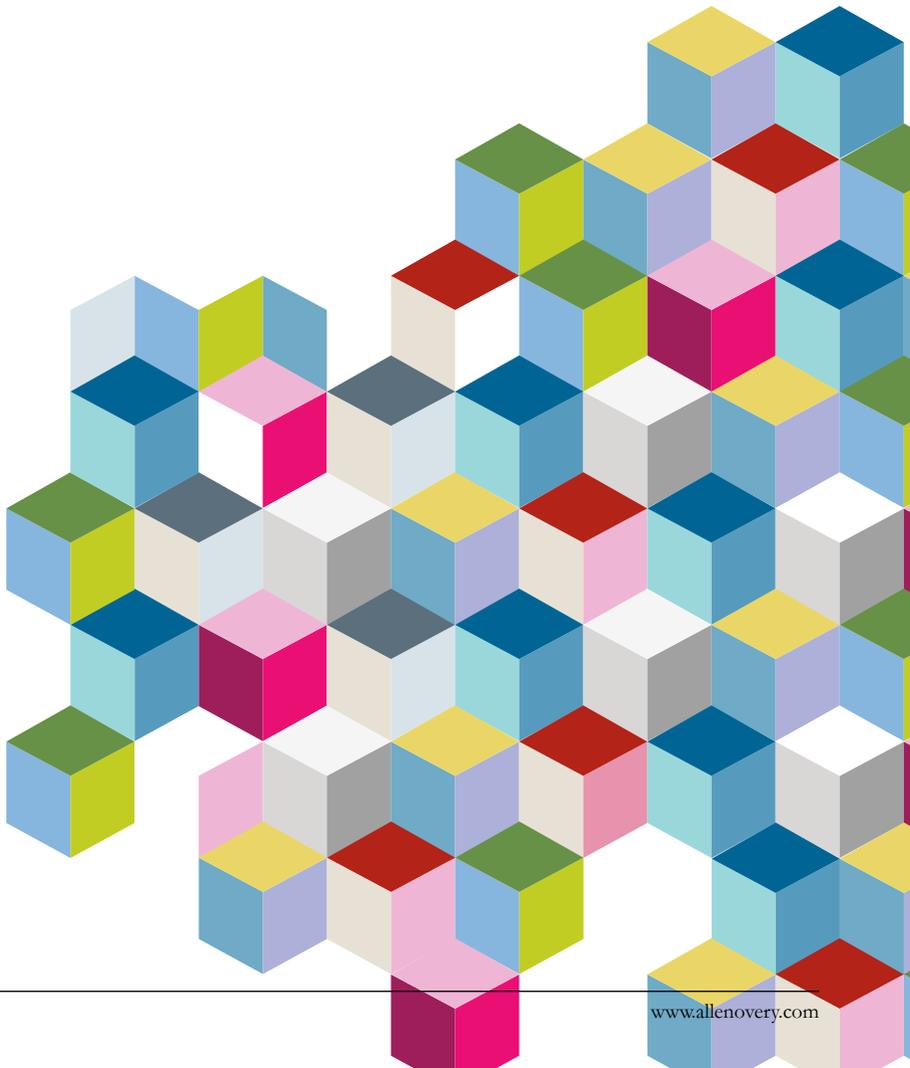


Craig Cohen

Senior Counsel, U.S. Tax

Tel +1 212 756 1162

craig.cohen@allenoverly.com



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