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FEE Position Paper on Take Over of Losses in the EU

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PART I

1. INTRODUCTION

The objective of this paper is to study the treatment of losses, both domestically and across-borders, in Europe. The analysis is based on a survey examining the rules on loss compensation in Member States' tax systems.

In particular, this study considers how the current differences in the tax treatment of domestic and foreign losses by Member States offends against the principle of freedom of establishment and, by so doing, delays the establishment of an effective Internal Market.

The paper first briefly introduces (chapter 2) the reader to the technical background of the topic of take over of losses, EU legislation proposals and the increasingly significant role of the European Court of Justice rulings.

Subsequently, the results of the survey (chapter 3) provide an analysis of the answers received to the questionnaire sent to EU Member States. Information has been gathered on their offset of losses system in three situations: in country, cross border inwards and cross border outwards. Short recommendations are supplied on each considered issue.

Consequently (chapter 4) conclusions on the analysis are drawn and consistent FEE recommendations are provided.

At the end of the paper (Part II, chapter 5) are listed the answers to the questionnaires.

2. BACKGROUND

2.1 Technical background

The ability to set off losses against profits ("***take-over of losses***" or "***transfer of losses***") for assessing the tax liability of a domestic group of companies is a basic feature of any company tax system.

However, as shown by FEE survey, the rules on loss compensation differ substantially at domestic and at international level: while in many cases offset of domestic losses is possible in all Member States (even though the details differ significantly amongst the countries), the taking into account of foreign losses is restricted or impossible. As a consequence, foreign investment is mostly treated less favourable than domestic investment.

In a worldwide taxation system, the clear distinction between foreign Permanent Establishments and foreign Subsidiaries plays an important role in relation to the treatment of foreign losses:

- Foreign ***Permanent Establishments*** (branches) are not separate legal entities and their results form an integral part of the total results of the enterprise;
- Foreign ***Subsidiaries*** are separate legal entities and their results are not part of the results of the domestic parent company or of the domestic group.

Loss compensation can be achieved mainly following four systems:

- ***Tax consolidation*****:** this system allows the consolidation of profit and losses of the parent company and subsidiaries included in the perimeter of tax consolidation; losses can be offset against profits in the calculation of the consolidated tax base, under conditions that varies from country to country;
- ***Group contribution or group relief*****:** this regime enables surrender of losses between two or more companies in the same group, under conditions that varies from country to country;
- ***Recognition of foreign losses***: this system allows losses incurred by Permanent Establishments to be deducted from the taxable income of the main office;
- ***Tax transparency***: this regime is typical of partnership taxation, according to which the profit or the loss of the partnership is allocated *pro-quota* to the partners; in case of losses, this means that the share of the loss attributable to the partner is deducted from his taxable income; in some countries this regime is allowed to companies as well, on an optional basis.

In order to prevent international double taxation, Member States apply two methods for taxing overseas profits[1]:

- *Credit method*;
- *Exemption method*.

[1] See for more details BEN J.M.TERRA, PETER J.WATTEL, *European Tax Law*, third edition, The Hague, 2001.

According to the ***credit method***, a taxpayer earning foreign-source income should be taxed in his home country on his worldwide income, and may credit, against the home-State tax attributable to the foreign income, the foreign tax already paid in the source State. The credit method is applied by countries adhering to the principle of *capital export neutrality*, according to which the State should tax foreign–source income of its residents so that they are neither encouraged to invest nor discouraged from investing abroad (home neutrality).

It should be noted, however, that profits of foreign legal entities are not subject to home country taxation on an arising basis (except when CFC regimes are applicable), and they only effectively fall into the home country tax regime when paid-out by way of dividends or similar distributions. The reverse of this, not surprisingly, is that losses of foreign legal entities are rarely deductible against profits of the home country group.

According to the ***exemption method***, the taxpayer is granted a reduction of domestic tax on his total worldwide income which is equal to the part of the domestic tax attributable to the foreign-source income. The exemption method is applied by countries adhering to the principle of *capital import neutrality*, according to which a State should exempt the foreign-source income of its residents, since that income has already borne tax in the source State: foreign and domestic taxpayers should be able to compete on the foreign market on equal conditions.

The difference of principle between the two systems is that they start from different neutrality ideas: while taxpayers resident in *credit* countries compete on foreign markets on *home*-State conditions, taxpayers resident in *exemption* countries compete on foreign markets on *source*-State conditions.

Although a worldwide system of taxation will generally grant relief in the home country for the losses of an overseas branch and, by the same token, levy tax on any profits arising from it, the granting of relief for the losses of an overseas branch conflicts with the fundamental logic of an exemption method. However, certain countries with an exemption method have introduced specific provisions to grant such a relief while providing for the automatic recapture of any deduction so allowed, after a defined period.

In both systems the issue of ***recapture*** of losses previously deducted is important. Where a foreign branch's loss has been deducted, in order to avoid double offset, subsequent branch's profits will have to be taxed.

Under a credit system, recapture occurs in effect automatically as the home State will only grant credit in respect of the subsequent branch profits and in fact no foreign tax will normally be paid on subsequent profits until all losses have been recaptured as the loss is offset against profits in the foreign State.

Under an exemption system recapture is not automatic and the result is that the home State tax exemption of the subsequent branch profit is only granted to the extent that subsequent profits exceeds the branch's losses previously deducted. Indeed, in the absence of a provision for the recapture of the deduction of the foreign loss, instead of representing a tax deferral, it would represent a permanent tax saving because future profits of the branch would not be taxed by virtue of the exemption.

If the losses of the branch could not be carried forward and, as a consequence, future profits of the branch were taxed in the host country, the provision in the home country for the recapture of the previous deduction would give rise to double taxation. However, also the *length* of the period allowed by the foreign country for the carry forward of the loss of the permanent establishment could produce relevant consequences, either affecting the sharing of the total tax burden of the enterprise between the

two jurisdictions (in the case of credit method) or causing an international double taxation (in the case of exemption method)[2].

2.2 Past European Commission proposals

In the early 1990s the Commission brought forward a proposal for a Directive on `The taking into account by enterprises of the losses of their permanent establishments and subsidiaries'. Even though the Ruding Committee, the Commission itself and the European Industry have been urging for approval since then, the proposal Directive has not been adopted by Council.

The starting point for the proposal is that there is no justification for discriminating against the form of enterprise, whether a branch or subsidiary. The choice between the two should be a purely commercial matter, unaffected by tax considerations.

The other underlying principle is that relief should be available in the `home' Member State for losses incurred in another Member State. Accordingly, this relief should be available regardless of whether the loss was incurred through a branch or subsidiary. For this reason the draft Directive provided that relief should be available in the home Member State for the losses of a subsidiary, based in another Member State. Accordingly, the losses of both branches and subsidiaries would have been eligible for relief. In the case of a subsidiary, this loss would be computed by reference the tax laws of the Member State in which the subsidiary was based.

The Commission in its proposal Directive provided that Member States which apply an exemption system should allow relief for the losses incurred by branches in other Member States, while at the same time providing for the automatic recapture of any deduction so granted, after six years. In order to overcome the potential problem of double taxation, the Commission emphasised that its proposal should be adopted in conjunction with a proposal for the carry-over of company losses, which was first put forward in 1984.

However, even this limited proposal made no progress because of the intransigence of the revenue authorities of the majority of Member States. Likewise the more fundamental proposal, introduced by the Commission in the 1990s, proved too radical for the revenue authorities of the various Member States and the Commission was forced to withdraw it. Although the Commission proposed introducing

[2] For example, consider a foreign P.E. having a loss of 100 in year 1, year 2 and year 3, zero result in year 4, year 5 and year 6, and a profit of 300 in year 7. At the end of the 7 years- period the total result of the P.E. is zero. Consider that the home office of the enterprise have an income of 100 in year 1, year 2 and year 3, zero result in year 4, year 5 and year 6, and a profit of 300 in year 7. At the end of the seven years period the total result of the main office of the enterprise is 600 and the global result is 600 as well. “Inter-nation equity” would suggest that the entire income tax (let’s consider a 30% rate on 600, i.e. 180) should be allocated to the jurisdiction of the main office of the enterprise, because the P.E. has not produced any income in fact over the seven years.
If the foreign country allows a three years period for the carry-forward of losses, than the profit of the P.E. in year 7 will be taxed in the foreign country (300 at 30% = 90). In the same year:
(i) If the home country follows the credit method, it will tax the total income of the enterprise, deducting the foreign tax (300 + 300 = 600 at 30% = 180 – 90 = 90), so that the tax will be shared between the foreign country and the domestic country, while the income is totally attributable to the domestic country;
(ii) If the home country follows the exemption method, but allows the deduction of the losses of a foreign P.E. with recapture provision, than it will tax 600 in the year 7 (600 at 30% = 180) and the company will have to pay and additional tax of 90 in the foreign country, because of a double taxation.
If the foreign country allows and indefinite period for the carry forward of losses of the P.E., in year 7 no tax would be levied in the foreign country and the home country will tax the same amount of 600, whatever is the method followed. In this case, neither an unfair sharing of taxes among jurisdictions nor an international double taxation will arise.

a new draft Directive, it has been overtaken by events before the courts, especially the European Court of Justice (see 2.3).

The issue of take over of losses and the problems caused by company tax law in Member States has been further analysed by the European Commission in a 2002 Study[3], which concludes on the subject that national company tax laws contain '…a bias in favour of domestic investment, thus indirectly hampering cross border economic activities. This is particularly true in the larger Member States, because the domestic market of such States may be large enough to accommodate one important enterprise, while an enterprise of the same size operating from a smaller Member State is immediately confronted with the lack of cross border loss compensation of some parts of its business operating in other Member States'. The effects culminate in a violation of the basic right of free establishment.

2.3 European Court of Justice and freedom of establishment

The European Court of Justice (ECJ) has been playing an increasingly significant role in the last few years. Its responsibility is to ensure that the law is observed in the interpretation and application of the Treaties establishing the EU. To enable to carry out that task, the Court has wide jurisdiction to hear various types of action. Inter alia, its competence is to rule on applications for annulment or actions for failure to act brought by Member States or institutions, actions against Member States to fulfil obligations, references for a preliminary rulings and appeals against decisions of the Court of First Instance.

Many ECJ cases have implications on cross border compensation of losses. Amongst them, the so called 'Marks and Spencer case'[4] requires particular attention. In such case, which the UK courts have referred on in 2003 to the ECJ, the taxpayer, Marks and Spencer, believes that the UK provisions on group relief are against the Treaties where, on the one hand, they prevent a parent company which is resident for tax purposes in UK from setting off losses incurred in other Member States by subsidiaries companies which are resident for tax purposes in those States, while on the other hand they allow losses offset at domestic level.

It is not easy to define the possible consequences if the taxpayer is successful in its case. Revenue authorities will be forced to respond to limit the risks to their tax bases in the future. At one extreme, Member States may possibly be forced to dismantle existing domestic loss consolidation provisions (so as not to discriminate against losses incurred in other Member States). At the other extreme, Member States which currently operate a system of worldwide taxation may possibly have to introduce Pan-European exemption systems.

[3] 'Company Taxation in the Internal Market' Commission Staff Working Paper, Bruxelles, 2002.
[4] Case C-446/03 published on Official Journal of the EU 13 December 2003.

3. RESULTS OF THE SURVEY

3.1 In-country take over of losses

QUESTION 1: Within one legal entity

Does the tax system recognise:
(a) Carry back of losses
(b) Carry forward of losses (if yes, state maximum of years).

Results of the Survey

Question 1 a) Carry back of losses

Only 5 out of 24 surveyed countries[5] allow carry back of losses at domestic level.

FEE Recommendations

FEE is in favour of carry back of losses for two reasons:

- It provides an incentive to businesses:

  The cash flow is not affected as business can have in the years they suffer from losses a refund of the tax paid in the previous years.

- It is according the principle of *tax equity* (fairness):

  When a company is allowed to carry back losses, it can be granted a tax refund of the tax paid in the previous years whenever it has a loss in the subsequent periods. In case the carry back is not allowed, this would be against the principle of tax equity, as the company would not have any refund for the tax previously paid even though it has a loss afterwards.

  On the other hand, when the carry forward of loss is allowed, the company would have had no tax to pay if it had had the loss the year before, and the profit afterwards.

A basic example might better illustrate the different consequences:
We consider 3 years of the business life of Company A:

Year 1
Profit 100
Tax (40)

Year 2
Loss 100
Tax 0

[5] The questionnaire has been sent to EU Member States and the candidate country of Romania. FEE received the answers from all Member States, except Greece and Poland, and from Romania. The 24 countries which answered are referred to as the 'surveyed countries' for simplification for the readers.

Year 3
Profit 0
Tax 0

Carry back of losses allowed:
End of Year 3
Cumulated Profit 0
Tax paid (40)
Tax refund 40
Consequence: being the cumulated profit equal to 0, the tax burden is 0, which is consistent with the equity principle of taxation. From a going concern perspective, the company is not forced to liquidate just because it has paid a tax on the taxable income of just one year that, in a three year perspective, is not existent.

Carry back of losses not allowed:
End of Year 3
Cumulated Profit 0
Tax paid (40)
Consequence: the pays taxes on a cumulated profit of 0, so that tax is levied – de facto – on capital, and this could produce going concern problems.

Of course, a reasonable time limit for a carry back of losses has to be established: from the taxpayer perspective there is the need to pay taxes provided that a cumulated profit arise; from the tax authorities perspective there is the need to preserve stability in the tax revenues and to be able to assess the results of the fiscal years in which taxes were paid. A good compromise could be to identify a period for carry back of losses that is consistent with the deadline for tax authorities to make assessment.

Hence, FEE recommends that carry back of losses is allowed, for the same time period the tax authorities have the right to examine and re-open tax assessment.

Question 1 b) Carry forward of losses

All the surveyed countries, except from Estonia, allow for a carry forward of losses at domestic level and mostly for an unlimited period of time or for 5 years.

FEE Recommendations

Carry forward of losses is a common principle in EU taxation. FEE is in favour of an unlimited or long period for allowing carry forward of losses, as this encourages a long-term perspective in investment, large scale projects, and the growth in employment, in line with the Lisbon objective for 2010 "to become the most competitive and dynamic knowledge based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion" [6].

[6] Lisbon European Council, 23 and 24 March 2000, Presidency conclusions, Point 5.

QUESTION 2: Between two or more legal entities

Does the tax system recognize take over of losses between two corporations?

If the tax system recognises take over of losses between two corporations, the method is:

- Transfer of losses
- Tax consolidation
- Group contribution.

Results of the Survey

The majority (17 out of 24 countries) of surveyed countries allow take over of losses at domestic level between two corporations, subject to required ownership and other conditions. The most common system is tax consolidation.

FEE Recommendations

FEE is in favour of allowing take over of losses between two corporations as this is in accordance with the principle of *tax neutrality* of the legal form of the enterprise. FEE believes that the tax treatment of groups should be identical regardless of their legal structure (subsidiaries, branches, etc), in order to avoid that taxation can influence the choice of the legal form of businesses.

The most common system to allow the take over of losses between two corporations is tax consolidation. A trend can be also observed in Europe towards tax consolidation, as some countries are in progress of adopting this method.

FEE does not have a specific preference for the method of tax consolidation compared to other methods of take over of losses; however, it can be said that tax consolidation encourages third parties investment and employee participation, facilitates growth through take-overs and fosters the growth of SMEs towards more structured business models.

QUESTION 3: Between corporations and partnership

Does the tax system allow for deduction of losses incurred in a trading partnership in which a company is a partner?

Results of the Survey

Half of the surveyed countries (12 out of the 24) allow for deduction of losses between corporations and a partnership at a domestic level.

In many countries partnerships are tax transparent, as partners are taxed on their share of profits and are given tax relief for their share of losses. In some countries, however, the relief of losses arising from a participation in a partnership is not available.

FEE Recommendations

FEE recommends that deduction of losses between corporations and a partnership be allowed in order to protect the economic unity of the business regardless of the legal structure (which might be divided into subsidiaries, etc. See question 2).

FEE is in favour of an optional *transparency* regime. The legal regime of partnerships allows take-overs also where consolidation is not possible: there is no need of a majority of shares to be able to get a relief for losses.

3.2. Inwards (cross border) take over of losses: country of reporter as home country of mother corporation

QUESTION 4: Within one legal entity

Does the tax system recognises foreign losses in the home-country:
(a) If foreign activity = Permanent Establishment (PE)?
(b) If foreign activity= NOT deemed to be Permanent Establishment?

If the reporter's country recognises foreign losses, how are foreign recognised losses being calculated? Is there a need to restate the loss of the foreign PE by applying the mother company country tax rules?

If the reporter's country recognises foreign losses, are there any recapture rules?

Results of the Survey

In the case the foreign activity is a Permanent Establishment, 14 out of 24 of the surveyed countries recognise foreign losses in the home-country.

In all of these 14 countries which recognise foreign losses in the home-country there is a requirement to restate the loss of the foreign Permanent Establishment by applying the mother State rules on calculation of the taxable income. Only 8 of these 14 countries have recapture rules where profits arise in the foreign Permanent Establishment.

In the countries in which losses are not deductible the main reason is that profits are exempt from tax, according to the exemption method of foreign income.

In the case the foreign activity is NOT deemed to be a Permanent Establishment, the majority (21 out of 24) of the surveyed countries recognise foreign losses in the home-country.

FEE Recommendations

From a purely domestic perspective, the two methods of tax credit and tax exemption both achieve the objective of avoiding international double taxation of the profit of the foreign Permanent Establishment.

At a European level, it has to be observed that most of the countries which apply the tax exemption method do not allow for deduction of the foreign Permanent Establishment losses against domestic profits.

This creates a barrier to the freedom of establishment in the countries where the Permanent Establishment is located and is against the principle of *capital export neutrality*. According to the latter principle, a State should tax foreign–source income of its residents so that they are neither encouraged to invest nor discouraged from investing abroad (home neutrality). A Taxpayer earning foreign-source income should be taxed in his home country on his worldwide income, and may credit, against the home-State tax attributable to the foreign income, the foreign tax already paid in the source State.

FEE therefore recommends that losses of foreign permanent establishments be deductible against home country (head office) profits. FEE recommends that the tax credit method be followed at international level. In cases where the tax exemption method applies, FEE recommends that the foreign Permanent Establishment losses be deducted using appropriate recapture rules.

QUESTION 5: Between two legal entities

Does the tax system of corporation in the country of reporter allow for deduction of foreign subsidiary's losses?
If the reporter's country allows for foreign losses offset, how are foreign losses being calculated: is there a need to restate the loss of the foreign company by applying the mother company country tax rules?
If the reporter's country recognises foreign losses, are there any recapture rules?
Would a write-down of the investment in the foreign subsidiary be tax deductible at the parent company level?
Would a loss upon sale/liquidation of the foreign subsidiary be tax deductible at the parent company level?

Results of the Survey

The overwhelming majority (21 out 24) of the surveyed countries do NOT allow for deduction of foreign corporation's losses.

Only three countries, namely Austria[7], Denmark and Italy, do allow a deduction of losses incurred by foreign subsidiaries according to the international tax consolidation method. In these two cases the losses need to be restated using domestic tax rules and recapture rules exist where the subsidiaries report a profit.

FEE Recommendations

It must be noted that the fact that the majority of countries do not allow for deduction of foreign subsidiaries' losses may be contrasted with the domestic legislation as most of the countries have domestic provisions allowing offset of losses at a domestic level (see question 2). Such difference in treatment may be inconsistent with treaty principles of *freedom of establishment* and *free movement of capital*. The argument that that profits of foreign subsidiaries are not taxed in the home country on an arising basis is not a justification for such treatment, because the same applies on a purely domestic situations as well.

In this respect the pending case Marks & Spencer needs to be considered (see chapter 2.3). The taxpayer Marks & Spencer believes that the denial (provided by UK domestic legislation) of the right

[7] Austria and Italy have both recently modernised their tax system.

to offset losses suffered overseas (in other Member States) against its domestic profits represents an infringement of the right to freedom of establishment under the Treaties. In the case the ECJ rules out that in this respect UK legislation (and similar legislations of other Member States) is inconsistent with the treaties, the consequence would be that UK (and other Member States') domestic provisions become automatically applicable at international level, thereby causing serious problems.

FEE therefore recognises the lack of provisions at European level on international group relief and fosters the idea that the European Commission launch a Recommendation providing coordination and guidelines on this subject.

In addition, FEE encourages the adoption of international tax consolidation model at EU level.

QUESTION 6: Between legal entity and partnership

Does the tax system of a corporation in your home country allow for a deduction of foreign partnership losses:
(a) If partnership = Permanent Establishment?
(b) If partnership = is NOT deemed to be Permanent Establishment?
If the reporter's country allows for foreign losses deduction, how are foreign recognised losses being calculated?
Is there a need to restate the loss of the foreign partnership by applying the mother company country tax rules?

Results of the Survey

In the case the foreign partnership is deemed to be a Permanent Establishment, 11 out of 24 of the surveyed countries allow for a deduction of foreign partnership losses. In 10 of these 11 countries there is a requirement to restate the loss of the foreign Permanent Establishment by applying the mother State rules. Only 9 of these 11 countries have recapture rules where profits arise in the foreign Permanent Establishment.

In the countries where losses are not deductible the main reason is that profits are exempt from tax, according to the exemption method of foreign income.

If the foreign partnership is not deemed to be a Permanent Establishment 14 out of the 24 surveyed countries allow for a deduction of foreign partnership losses, even if based on different principles.

The tax treatment of a foreign partnership depends on the legal status of the partnership under the domestic law of the country of registration. In the case where the participation of the foreign partnership is classed as a PE, foreign partnership loss offset is only allowed in half of the surveyed countries, while in all the other cases, the possibility of deduction of foreign partnership losses is greater.

FEE Recommendations

In order to avoid any barriers to international joint ventures FEE recommends that the tax treatment of foreign partnerships be the same as the tax treatment of domestic partnerships, i.e. partnerships should be tax transparent (see question 3).

3.3 Outwards (cross border) take over of losses: your country as home country of subsidiary, PE or partnership

NB: Questions 7, 8 and 9 are considered jointly.

QUESTION 7: Within one legal entity
Does the tax system allow for deduction of losses of a head office in the home-country of Permanent Establishment?

QUESTION 8: Between two legal entities
Does the tax system of the subsidiary allow deduction of losses of foreign group companies?

QUESTION 9: Between partnerships and corporations
Does the tax system of the partnership allows deduction of losses of foreign corporate partners if the partnership is deemed to be a Permanent Establishment?

Results of the Survey

In no circumstances (within one legal entity, between two legal entities, between a partnership and corporations) is an outward cross border relief of losses of a parent or related foreign corporation allowed in the home country of the subsidiary or PE in any of the 24 surveyed countries.

FEE Recommendations

It can be observed that while at domestic level subsidiaries are generally allowed to have relief for the losses of parent companies (by means of tax consolidation or of transfer of losses or optional transparency regimes), at international level such relief is denied in all cases.

However, the principle of *capital import neutrality* requires that from the perspective of the country where the subsidiary is located a relief be allowed for the losses of parent company in the country of the subsidiary. A difference of treatment between domestic and international levels represents a barrier to the freedom of establishment.

FEE recommends in the short term that the European Commission issue a Recommendation to provide rules consistent for both international and domestic treatments. The ECJ decision on the Marks & Spencer case will in any case provide guidance on the issue.

In the long term FEE is in favour of the creation of a European Common Consolidated Tax Base, excluding at the same time any harmonisation in tax rates which could create a distortion in the Internal Market.

3.4 The surveyed countries

The questionnaire has been sent to the 25 EU Member States and the candidate country of Romania. Answers have been received from Romania and all EU Member States except from Greece and Poland. The 24 countries which answered are referred to as the 'surveyed countries' for simplification for the readers.

The matrixes below summarise the answers by country.

Matrix 3.4.1 relates to the following countries: Austria, Belgium, Cyprus, Czech Republic, Germany, Denmark, Estonia, Spain, Finland, France, Greece, Hungary, Ireland.

Matrix 3.4.2 relates to the following countries: Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovenia, Republic Slovak, Sweden, United Kingdom.

3.4.1 Matrix of the key issues regarding the Study of the Take Over of losses in the EU

Countries: Austria to Ireland

	AU	BE	CY	CZ	DE	DK	EE	ES	FI	FR	HU	IR
A. In-country offset of losses												
1. Within one legal entity												
The tax system recognises:												
(a) Carry back of losses	No	No	No	No	Yes	No	No	No	No	Yes	No	Yes
(b) Carry forward of losses	Yes	Yes	Yes	Yes	Yes	Yes	No	Yes	Yes	Yes	Yes	Yes
If yes, maximum of years	Ultd /3	Ultd	Ultd	5	Ultd	Ultd		15	10	Ultd	Ultd	Ultd
2. Between two or more legal entities												
The tax system recognises take over of losses between two corporations	Yes	No	Yes	No	Yes	Yes	No	Yes	Yes	Yes	Yes	Yes
If yes, the method is:												
- Transfer of losses			X								X[8]	X
- Tax consolidation system	X					X		X		X		
- Group contribution					X				X			
3. Between corporations and partnership												
The tax system allows for deduction of losses between corporations and a partnership	Yes	Yes	No	No	Yes	Yes	No	No	No	Yes	No	Yes
4. Within one legal entity												
The tax system recognises foreign losses in the home-country:												
(a) If foreign activity = Permanent Establishment	Yes	Yes	No	No	No	Yes	No	Yes	Yes	No	No	Yes
(b) If foreign activity = NOT deemed to be Permanent Establishment	Yes	Yes	No	Yes	Yes	Yes	No	Yes	Yes	Yes	Yes	Yes
If the reporter's country recognises foreign losses, how are foreign losses being calculated:												

[8] Yes, in case of successor

	AU	BE	CY	CZ	DE	DK	EE	ES	FI	FR	HU	IR
Is there a need to restate the loss of the foreign P.E. by applying the mother company country tax rules?	Yes	Yes	N/A	N/A	N/A	Yes	N/A	Yes	Yes	N/A	N/A	Yes
If the reporter's country recognises foreign losses, are there any recapture rules?	Yes	Yes	N/A	N/A	N/A	Yes	N/A	Yes	No	N/A	N/A	Yes
5. Between two legal entities												
The tax system of Corp.1 allows for deduction of foreign corporation's losses	Yes	No	No	No	No	Yes	No	No	No	No	No	No
If the reporter's country allows for foreign losses offset, how are foreign losses being calculated:												
Is there a need to restate the loss of the foreign company by applying the mother company country tax rules?	Yes	N/A	N/A	N/A	N/A	Yes	N/A	N/A	N/A	N/A	N/A	N/A
If the reporter's country recognises foreign losses, are there any recapture rules?	Yes	N/A	N/A	N/A	N/A	Yes	N/A	N/A	N/A	N/A	N/A	N/A
Would a write-down of the investment in the foreign subsidiary be tax deductible at the parent company?	No	No	No	No	No	No	No	Yes	No	Yes	Yes	No
Would a loss upon sale/liquidation of the foreign subsidiary be tax deductible at the parent company?	Note [9]	Yes [10]	No	No	No	No [11]	No	Yes	No	Yes	Yes	Yes
6. Between legal entity and partnership												
The tax system of Corp.1 allows for a deduction of foreign partnership losses:												
(a) If partnership = Permanent Establishment	Yes	Yes	No	No	No	Yes	No	Yes	Yes	No	No	Yes
(b) If partnership = is NOT deemed to be Permanent Establishment	Yes	Yes	No	No	Yes	Yes	No	Yes	Yes	Yes	Yes	Yes
If the reporter's country allows for foreign losses deduction, how are foreign recognised losses being calculated:												
Is there a need to restate the loss of the foreign partnership by applying the mother company country tax rules?	Yes	Yes	N/A	N/A	N/A	Yes	N/A	Yes	Yes	N/A	N/A	Yes
If the reporter's country recognises foreign losses, are there any recapture rules?	Yes	Yes	N/A	N/A	N/A	Yes	N/A	Yes	No	N/A	N/A	Yes

[9] Sale: No; Liquidation: Yes

[10] Deduction allowed only in case of liquidation or bankruptcy

[11] If the period of ownership is less than three years a loss can be carried forward and offset against future gains on shares owned less than three years.

C. Outwards (cross border) take over of losses: your country as home country of overseas subsidiary.												
7. Within one legal entity												
The tax system allows for deduction of losses of Corp. 1 in the home-country of the 'activities' in case activities = Permanent Establishment	No	No	No	No	No	No	No	No	No	No	No	No
8. Between two legal entities												
The tax system of Corp.2 allows deduction of losses of foreign Corp. 1?	No	No	No	No	No	No	No	No	No	No	No	No
9. Between partnership and corporation												
The tax system of the partnership allows deduction of losses of Corp. 1 or Corp.2 if partnership = Permanent Establishment	No	No	No	No	No	No	No	No	No	No	No	No

Legend:

- **AU**: Austria; **BE**: Belgium; **CY**: Cyprus; **CZ**: Czech Republic; **DE**: Germany; **DK**: Denmark; **EE**: Estonia; **ES**: Spain; **FI**: Finland; **FR**: France; **HU**: Hungary; **IR**: Ireland
- **Ultd**: unlimited

3.4.2 Matrix of the key issues regarding the Study of the Take Over of losses in the EU

Countries: Italy to UK

	IT	LU	LT	LV	MA	NE	PT	RO	SI	SK	SW	UK
A. In-country offset of losses												
1. Within one legal entity												
The tax system recognises:												
(a) Carry back of losses	No	No	No	No	No	Yes	No	No	No	No	No	Yes
(b) Carry forward of losses	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
If yes, maximum of years	Uld /5	Uld	5	5	Uld	Uld	6	5	5	5	Uld	Uld
2. Between two or more legal entities												
The tax system recognises take over of losses between two corporations	Yes	Yes	No	No	Yes	Yes	Yes	No	Yes	No	Yes	Yes
If yes, the method is:												
- Tax consolidation system	X	X				X			X			
- Group contribution or group relief					X[12]		X				X	X
3. Between corporations and partnership												
The tax system allows for deduction of losses between corporations and a partnership	Yes	Yes	No	No	No	Yes	No	Yes	No	No	Yes	Yes
4. Within one legal entity												
The tax system recognises foreign losses in the home-country:												
(a) If foreign activity = Permanent Establishment	Yes	No	No	Yes	Yes	Yes	Yes	No[13]	Yes	No	Yes	Yes
(b) If foreign activity = NOT deemed to be Permanent Establishment	Yes	Yes	No	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
If the reporter's country recognises foreign losses, how are foreign losses being calculated:												
Is there a need to restate the loss of the foreign P.E. by applying the mother company country tax rules?	Yes	N/A	N/A	Yes	Yes	Yes	Yes	N/A	Yes	N/A	Yes	Yes
If the reporter's country recognises foreign losses, are there any recapture rules?	No	N/A	N/A	No	N/A	Yes	No	N/A	Yes	N/A	No	Yes
5. Between two legal entities												
The tax system of Corp.1 allows for deduction of foreign corporation's losses	Yes	No	No	No	No	No	No	No	No	No	No	No
If the reporter's country allows for foreign losses offet, how are foreign losses being calculated:												

[12] Limited to groups of companies having coinciding financial years

[13] Carry forward of losses of the Permanent Establishment (PE) is allowed only against the future profits of the P.E.

	IT	LU	LT	LV	MA	NE	PT	RO	SI	SK	SW	UK
Is there a need to restate the loss of the foreign company by applying the mother company country tax rules?	Yes	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
If the reporter's country recognises foreign losses, are there any recapture rules?	Yes	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Would a write-down of the investment in the foreign subsidiary be tax deductible at the parent company ?	No	Yes	N/A	N/A	No	No	No	No	No	No	No	No
Would a loss upon sale/liquidation of the foreign subsidiary be tax deductible at the parent company ?	No	No	N/A	N/A	Yes	No	No	No	Yes	No	No	Yes
6. Between legal entity and partnership												
The tax system of Corp.1 allows for a deduction of foreign partnership losses:												
(a) If partnership = Permanent Establishment	Yes	No	No	Yes	No	Yes	No	No	No	No	Yes	Yes
(b) If partnership = is NOT deemed to be Permanent Establishment	Yes	No	No	Yes	No	Yes	No	No	No	No	Yes	Yes
If the reporter's country allows for foreign losses deduction, how are foreign losses being calculated:												
Is there a need to restate the loss of the foreign partnership by applying the mother company country tax rules?	Yes	N/A	N/A	N/A	N/A	Yes	N/A	N/A	N/A	N/A	Yes	Yes
If the reporter's country recognises foreign losses, are there any recapture rules?	Yes	N/A	N/A	N/A	N/A	Yes	N/A	N/A	N/A	N/A	Yes	Yes
C. Outwards (cross border) take over of losses: your country as home country of overseas subsidiary.												
7. Within one legal entity												
The tax system allows for deduction of losses of Corp. 1 in the home-country of the 'activities' in case activities = Permanent Establishment	No		No	No	No		No	No	No	No	No	No
8. Between two legal entities												
The tax system of Corp.2 allows deduction of losses of foreign Corp. 1?	No		No	No	No		No	No	No	No	No	No
9. Between partnership and corporation												
The tax system of the partnership allows deduction of losses of Corp. 1 or Corp.2 If partnership = Permanent Establishment	No	No	No	No	No	No	No	No	No	No	No	No

Legend:

- **IT**: Italy; **LT:** Lithuania; **LV**: Latvia; **LU**: Luxembourg; **MA**: Malta; **NE**: Netherlands; **PT**: Portugal; **RO**: Romania; **SI**: Slovenia; **SK**: Republic Slovak; **SW**: Sweden; **UK**: United Kingdom
- **Ultd**: unlimited

4. CONCLUSIONS AND RECOMMENDATIONS

4.1 Conclusions

FEE survey indicates that there are substantial differences in treatment of domestic and foreign losses amongst Member States and that European businesses encounter significant difficulties with loss compensation. The EU has yet to achieve the envisaged harmonisation of tax treatment of foreign losses.

The range of different domestic provisions on loss compensation is detrimental to the efficient functioning of the Internal Market and is an obstacle to cross border activity in the broader sense as it imposes a substantial compliance burden on businesses that are expanding internationally.

This situation is against the principle of free establishment as it implies a bias in favour of domestic investment owing to the fact that loss compensation is available domestically but not always in cross border situations. Besides, it provides a clear incentive to invest in Member States with large home markets allowing expansion possibilities.

The recent decisions of the ECJ highlight the considerable uncertainties surrounding the extent to which Member States' tax systems comply with the principles enshrined in the EC Treaty. In such circumstances, it is essential that Member States co-operate in order to reformulate their tax policies in advance so that these comply with the EC Treaty, rather than responding after the event and on an ad-hoc basis to the judgements of the ECJ.

4.2 Recommendations

In relation to loss compensation issues FEE has therefore the following Recommendations to remove the tax barriers to an efficient Internal Market:

FEE Recommendations

- **At national level:**

- FEE is in favour of carry back of losses as it provides an incentive to businesses and is according the principle of *tax equity*.

- Carry forward of losses is a common principle in EU taxation. FEE is in favour of an unlimited or long period for allowing carry forward of losses, as this encourages a long-term perspective in investment, large scale projects, and the growth in employment, in line with the Lisbon objective for 2010 " to become the most competitive and dynamic knowledge based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion".

- FEE recommends allowing loss compensation between two corporations at national level as this is in accordance with the principle of *tax neutrality*. FEE believes that the tax treatment of groups should be identical regardless of their legal structure (subsidiaries, P.E., etc), in order to avoid that taxation influence the choice of the legal form of businesses.

- The most common system to allow loss compensation between two corporations at national level is tax consolidation. A trend can be also observed in Europe towards tax consolidation, as some countries are in progress of adopting this method. FEE points out that such method encourages third parties investment and employee participation, facilitates growth through take-overs and fosters the growth of SMEs towards more structured business models.

- FEE recommends that deduction of losses between corporations and a partnership be allowed in order to protect the economic unity of the business regardless of the legal structure.

- FEE is in favour of an optional transparency regime. The legal regime of partnerships in fact allows take-overs also where consolidation is not possible: there is no need of a majority of shares to be able to get a relief for losses.

FEE Recommendations

◆ **At international level:**

- FEE recommends that the tax credit method be followed at international level. In case the tax exemption method *has* to be adopted, FEE recommends that the foreign Permanent Establishment losses be deducted using appropriate recapture rules.
- FEE recognises the lack of provisions at European level on international group relief and therefore fosters that in the very short term the European Commission launch a Recommendation providing guidance for rules consistent for both international and domestic loss compensation, even though the ECJ decision on the Marks & Spencer case will in any case provide guidance on the issue.
- FEE would encourage the adoption of an international tax consolidation model at EU level.
- FEE recommends that the tax treatment of foreign partnerships be the same as the tax treatment of domestic partnerships, i.e. partnerships should be tax transparent, so as to avoid any barriers to international joint ventures.
- In the long term FEE is in favour of the creation of a European Common Consolidated Tax Base, excluding at the same time any harmonisation in tax rates which could create a distortion in the Internal Market.

PART II

5. ANSWERS BY COUNTRY

As follows you can find the answers by country[14] to the questionnaire on cross border loss compensation.

The questionnaire was designed to analyse and compare the different systems of cross-border take over of losses within the EU Member States.

To gain full insight in these systems, the first set of questions (A) is addressed to take over of losses **within one** country: *'in-country take over of losses'*.

The second set of questions (B) is addressed to cross-border take over of losses.

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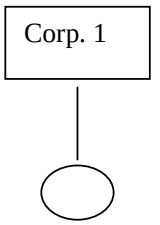
A. In-country take over of losses

1. *Within one legal entity*



: activity

Does the tax system recognize:

(a) Carry back of losses (if yes, state maximum years)

Austria

No carry-back of losses allowed.

Belgium

No.

Cyprus

No.

[14] Hungary, Lithuania and the Slovak Republic have not provided an answer to the full questionnaire but only to the summarising matrixes on page 25 onwards. Therefore they are not included in this section of the paper.

Czech Republic

No.

Denmark

No.

Estonia

No.

Finland

According to Finnish tax legislation it is not possible to carry back losses.

France

Yes.

According to French tax law, corporations may opt to carry back the losses to the last 3 financial years' taxed profits which have not been distributed. The carry back gives a tax credit which may be reimbursed if it is not used to pay corporation income tax at the end of a 5 years period.

Germany

It is only possible to carry back losses to the year before realisation. Since the beginning of 2001, the carry back of losses is limited up to one million German marks per year. Between 1999 and 2000 the limit was two million German marks per year. Up to 1998 it was ten million German marks per year. But in opposite to the current regulation, losses must be carried back to the second year before realisation.

Legal norm: Sec 10d Para. 1 Income Tax Act (EStG)

Ireland

Yes. 1 year.

Italy

No, the Italian tax system does not recognise any carry back of losses.

Latvia

No.

Luxembourg

No.

Malta

Not possible.

The Netherlands

Yes, 3 years.

Portugal

No.

Romania

No, the Romanian legislation does not allow to carry back the losses.

Slovenia

No.

Spain

In Spain carry back of losses is not allowed.

Sweden

No.

UK

Yes, one year.

On cessation, terminal loss relief is available which allows the loss to be carried back up to three years relieving the later years first. Loss relief is given against trading profits after trade charges have been deducted.

(b) Carry forward of losses (if yes, state maximum of years)

Austria

There is no time limit on the carry-forward of losses. However, there is one restriction: in general, only 75% of a year's current profit can be sheltered from taxation by loss carry-forwards, whereas 25% of a year's current profits is subject to tax even if there are loss carry-forwards available. Certain capital gains (e.g. gains from the sale of a business) can be fully sheltered by tax loss carry-forwards.

Belgium

Yes. Unlimited.

Cyprus

Yes, without any time limitation.

Czech Republic

Yes – 5 years (5 taxable periods after the period when the loss has been incurred).

Denmark

Yes, unlimited.

Estonia

No.
In Estonia a resident legal person do not pay income tax on income and consequently carry back or forward of losses is not applicable for tax purposes.

Finland

Losses can be carried forward during ten subsequent years. When more than 50 per cent of the shares of the Company change ownership for other reason than inheritance or bequest during the year the loss is shown or thereafter, the right to carry forward the losses is forfeited. If such a majority share transfer has taken place in a company owning at least 20 percent of the shares in the Company, the shares in the Company are deemed to have been transferred (indirect change). However, upon application of the taxpayer, the Regional Tax Office may grant a permission to utilise the forfeited tax losses. In order to receive the permission, the taxpayer must present valid and non-tax related business reasons in favour of the ownership change.

France

Yes. French tax law distinguishes two kinds of tax losses:

- The "ordinary tax losses" which may be carried forward for 5 years.
- The "ARD" ("Amortissements réputés différés") which are losses resulting from the depreciation of capital assets practiced by corporations. The ARD may be carried forward with no time limit. However, in principle, in case of transfers of activity (sales or purchases), ARD are transformed in ordinary losses.

The carry forward is not possible in case of major change of the taxable entity's activity. Likewise, in case of a merger, the losses of the absorbed company cannot be transferred to the absorbing company unless special approval has been obtained from the Tax Authorities.

Germany

The residual part of the losses, which cannot be carried back, has to be carried forward. Therefore a limitation, e.g. a maximum of years or a financial range, is not set up.

Legal norm: Sec. 10d Para. 2 Income Tax Act (EStG)

Ireland

Yes. Indefinitely (but must be same trade).

Italy

Yes, losses may be carried forward to reduce income in not more than five subsequent tax periods. However, if a loss is derived in the first 3 tax years from the beginning of the company's business activity, it may be carried forward indefinitely.

Losses may not be carried forward if the majority of the voting rights of the company is transferred and if in the taxable period in which the transfer occurs or in any of the two preceding or following periods, the activity of the company is changed from the one originating losses.

Latvia

Yes, in chronological order during maximum of 5 consecutive years.

Luxembourg

Yes, unlimited.

Malta

Trading losses are available for indefinite carry forward. They may only be set off against income from the same trading activity.

The Netherlands

Yes, unlimited (unless more than 30% change of share ownership).

Portugal

Yes, up to a maximum of 6 financial years.

Romania

Yes, for 5 consecutive years.

Slovenia

5 Years.

Spain

Carry forward of losses are allowed with a maximum of 15 years.

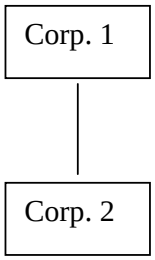
Sweden

Yes (no limit).

UK

Yes, unlimited.
However, there is an anti avoidance provision which denies loss carry forward where there is both a change in ownership and a major change in the nature or conduct of the trade. The test of change is a period three years before and three years after the change in ownership. If the facts show that such a change has occurred then there is no carry forward beyond the change in ownership.

2. *Between two or more legal entities*



Does the tax system recognize take over of losses between two corporations? (If yes, state method: *fiscal unity, transfer of losses or other method?*)

Austria

Generally no recognition of losses between two separate corporate entities, except in case of "Organschaft" (fiscal unity).

Organschaft is possible only between parent company and subsidiary if the following conditions have to be fulfilled cumulatively:

(i) Parent company must own at least 75% of the share capital of subsidiary ("financial integration")
(ii) Subsidiary must effectively be managed and controlled by parent company ("organisational integration"); general requirement that at least one executive officer of parent company ("Geschäftsführer", "Vorstand") is also an executive officer of subsidiary ("Geschäftsführer", "Vorstand"); parent company assumes certain administrative tasks for sub (e.g. accounting, marketing, HR etc)
(iii) Subsidiary is integrated into the business of the parent company, i.e. supports and furthers the business of the parent company ("business integration"); this usually requires that the subsidiary is buying from or selling to the parent company. A holding company is deemed not to have a business of its own: if the parent company is a mere holding company (even if it manages several subsidiaries) no "Organschaft" is possible with its subsidiaries.
(iv) There must be a profit and loss assumption agreement ("Ergebnisübernahmevertrag") between the parent and the subsidiary; under such agreement the parent company would assume the statutory income or cover any statutory loss of the subsidiary so that the subsidiary has a zero income for statutory purposes; the profit and loss assumption agreement mus be concluded for a period of at least 5 years.

Conditions (i), (ii) and (iii) must be met as of the beginning of the subsidiary's fiscal year for which "Organschaft" is to be applied for the first time; condition (iv) has to be met before the end of the subsidiary's fiscal year for which "Organschaft" is to be applied for the first time. If one of the

conditions (i) – (iii) is not fully met then this can be compensated by the other conditions being very strongly met (i.e. if business integration is weak then this can be compensated by say 100% financial integration).

Belgium

No.

Cyprus

Yes, if the companies are members of the same group. Companies are considered as members of the same group if one is 75% subsidiary of the other or both are by 75% subsidiaries of a third company.

Czech Republic

Yes – 5 years (5 taxable periods after the period when the loss has been incurred).

No.

Denmark

Yes – joint taxation system.

Estonia

No

In Estonia a resident legal person do not pay income tax on income and consequently carry back or forward of losses is not applicable for tax purposes.

Finland

There is no group taxation in Finland and all the group companies are taxed separately. Group contribution is, however, available, when the Finnish parent company (limited liability company = corporation) owns at least 90 % of the share capital of the Finnish subsidiary (limited liability company = corporation) and when both companies carry on business activity as defined in the Business Income Tax Act. Group contribution is available also between two Finnish subsidiaries (sister companies), if the ownership requirement is met through the parent company. In the latter case the parent company may also be a foreign company situated in a tax treaty country.

It is also required that the accounting periods of both companies end at the same date and that the required ownership has come into being before the beginning of the accounting period in question.

Group contribution can be given by the parent company to its subsidiary or vice versa and from one subsidiary to another. Both the distributing company and the recipient company must be Finnish companies.

The group contribution given by either a parent company or a subsidiary is deducted from the taxable income of the contributing company and added to the taxable income of the recipient company.

France

The take over of losses between two or more corporations is possible within the tax consolidation system ("intégration fiscale"). French companies of a group may opt for this system if the French parent company holds at least 95% of the capital and the voting rights of its French subsidiaries. Under tax consolidation, the subsidiaries are treated for tax purposes as branches of the parent company. Their profits or losses are then included in the parent company's tax profit (or losses) on which corporate income tax is assessed.

Germany

The German corporate tax act (KStG) offers an option to transfer losses between two or more corporations. This option is called "Organschaft", which is a special agreement establishing the relationship between two companies with their own legal personalities. The intention is, to allow the parent company under certain conditions to take over the losses of the subsidiary. It is not a true tax consolidation but a loss absorption by the parent. The basic condition for the required agreement is the financial dependence of one corporation (dominated-corporation) on another corporation (dominating-corporation), which requires ownership of more than 50% of the shares in the subsidiary. As a result of the agreement or contract, profits or losses realised by the dominated corporation are transferred to the dominating corporation. The profit and loss absorption contract is valid for civil law purposes.

Legal norm: Sec. 14 to 19 corporation tax act (KStG)

Ireland

Yes. Transfer of losses (same year). Companies must be in same group or part of consortium.

Italy

The take over of losses between two or more corporations is possible in Italy since the fiscal year 2004 within the National tax consolidation system ("Consolidato nazionale"). The Italians companies of a group may opt for this tax system if the Italian parent company holds directly or indirectly a control share of the capital and the voting rights of its subsidiaries. Under the National Tax Consolidation, the taxable income is the sum of all tax profit and losses of the parent company and its subsidiaries. The parent company can take over the resulting losses. The losses created before choosing this tax system, can be used only by the corporation that created them.

Furthermore, the take over of losses between two corporations is possible since the fiscal year 2004 within the Tax Transparent system ("Trasparenza Fiscale"). Italians companies can opt for this system if their partners are corporations that hold at least 10% but not more than 50% of the capital and the voting rights. Under the Tax Transparent system the tax profits or losses from the controlled corporations are attributed to each partner, without regard to actual receipt thereof, in proportion to his participation in the profits. Losses are attributed to each partner in proportion to his participation in the profits but within the limit of participation in the net equity of subsidiary.

Latvia

Transfer of losses between 2 entities under common control where control is ensured through at least 90% ownership.

Luxembourg

Yes, by way of fiscal unity.

Malta

Yes – Group relief is provided for under Maltese fiscal law. Thus losses may be surrendered between companies in the group so long as they all have coinciding financial year ends.

This is possible ONLY if the group structure requirements are respected.

The Netherlands

De-jure: No.
De-facto: Yes, via fiscal unity concept, though limited for pre-unity losses.

Portugal

No. But, it is to be noted that where a resident company has, according to commercial law, full control on other resident companies, the group of companies thus constituted may represent an unit for taxation purposes to be operated on a consolidated basis.

Romania

In Romania there is no recognition of losses between two separate companies and there is no group taxation, as group companies are taxed separately.

Slovenia

Yes, but only in case of group taxation, when group is formed by corporations which are connected with 90% ownership.

Spain

The Spanish legislation provides that losses should be compensated with future profits only by the corporation that has generated them. But in case of tax consolidation (fiscal unity), the Spanish tax system recognizes the possibility of taking over losses between two different corporations.

Sweden

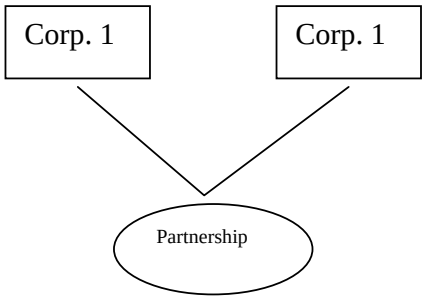
Yes, by transfer of profits (so-called "koncernbidrag"). Domestic groups can bring about a netting of profits and losses by group contributions ("koncernbidrag"). Group contributions are deductible for the contributor and taxable for the recipient. (Such contributions are also allowed between Swedish subsidiaries where there is a foreign parent resident in a EU-country.)

UK

In the UK, group relief enables the surrender of losses between two (or more) companies in the same group provided a 75% or more ownership test is passed. Group relief is set against total profits. It requires a surrender and claim notification to the Inland Revenue and is for current period losses only. If the accounting periods are not co-terminus then time apportionment occurs. Losses can go up or down and sideways so long as the group structure is 75% or more.

In addition, within the UK, there is a concept called a consortium company. The consortium company can surrender losses to its shareholder companies provided the claimant shareholder company has more than 5% of the shareholding. Similarly, the shareholding company can surrender losses to the consortium company. There are complex rules but generally the loss surrendered is the lesser of the %profit or loss. Supposing a loss of 100 was made by the consortium and the parent has a 60% shareholding then up to 60% of the loss could be surrendered to the parent shareholding company PROVIDED all the other shareholding companies in the consortium agree.

3. Between corporations and partnership



Does the tax system recognize take over of losses between corporations and a partnership? (if yes, state method: *fiscal unity, transfer of losses or other method?*)

Austria

Partnerships are generally transparent and losses incurred are allocated directly to the partners (Corp 1 and Corp 2 in the above example) and can be used to offset taxable income of the partners from other sources.

However, when the partnership is deemed to be a "tax shelter" losses incurred in such a partnership can be offset only against subsequent profits from the same partnership. A partnership is deemed to be a "tax shelter" if the main purpose of participating in the partnership is the tax advantage (§2a Income Tax Act).

Belgium

No fiscal unity principle.

If the partnership is not a juridical entity on its own, the results are divided between the partners.

Cyprus

No.

Czech Republic

No.

Denmark

We take it that one of the above Corp. 1 should be Corp. 2.
Yes – partly deduction according to ownership.

Estonia

No.

In Estonia a resident legal person do not pay income tax on income and consequently carry back or forward of losses is not applicable for tax purposes.

Partnership in Estonia is a legal person.

Finland

Group contribution described above is not available between a Finnish partnership and a Finnish limited liability company (corporation). A loss of a partnership can not be transferred to its partner company.

France

Yes.

According to our tax system, partnerships are not taxable entities. They are treated as transparent entities. Their profit (or losses) are included in the partners' profit (or losses) in proportion to their financial rights.

Please note that the tax transparency of partnerships is quite relative. Thus, partnerships must carry forward the "ARD" they may constitute on their own coming profits. In such a case, the losses which have been carried forward cannot be included in the partners' profit (or losses).

Germany

It is although possible to create an "Organschaft" between a corporation and a partnership. But there is the restriction that the partnership could only participate as a dominating "corporation". The losses could only be transferred from the corporation to the partnership. Legal norm: v. No. 2

Since partnerships are generally treated as transparent for tax purposes, losses of the partnership will automatically be considered for corporate income tax purposes at the level of the parent. Losses can only be considered up to the capital account for limited partners. For municipal trade income tax a transfer of losses from a partnership to its partners is not possible.

Ireland

No. A partnership itself is not taxed, but the partners are. If the companies are in a group or consortium, see 2 above.

Italy

Till December 2003 as a matter of fact the take over of losses between corporations and a partnership is not possible since the Italian Supreme Court has established that a corporation (società di capitali) can not be partner of a partnership (società di persone) under domestic law.

Since the fiscal year 2004 a new company's civil law has established that a corporation can be a partner of a partnership.

According to our tax system partnerships are not taxable entities. This means that the income is attributed to the corporation partner, without regard to actual receipt thereof, in proportion to his participation in the profits. Losses are attributed to each partner in proportion to his share. If the losses of a limited partnership exceed the partnership's capital, and the corporation is a limited partner, the losses exceeding the partnership's capital are not deductible by the corporation.

Latvia

Transfer of losses in cases when partnership is a corporate income taxpayer (as opposed to personal income tax payer).

Luxembourg

Take over is automatic as partnerships are fiscally transparent. Income is assessed with the partners.

The Netherlands

If transparent partnership, direct allocation of losses to partners.

Malta

No.

Portugal

No.

Romania

The losses as well as the profits of a partnership which is not a juridical entity are allocated directly to the partners in proportion to their financial rights.

Slovenia

No.

Spain

The Spanish Tax system does not provide the possibility to take over losses between Spanish corporation and a Spanish partnership.

Sweden

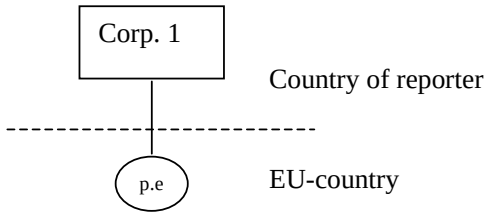
Partnerships are not subject to income tax, but their income is taxed at the partner level.

UK

Yes. Losses can be transferred. In addition, within the UK we have a concept called a consortium company. The consortium company can surrender losses to its shareholder companies provided the claimant shareholder company has more than 5% of the shareholding. Similarly, the shareholding company can surrender losses to the consortium company. There are complex rules but generally the loss surrendered is the lesser of the % profit or loss. Supposing a loss of 100 was made by the consortium and the parent has a 60% shareholding then up to 60% of the loss could be surrendered to the parent shareholding company PROVIDED all the other shareholding companies in the consortium agree.

B. Inwards (cross border) take over of losses: country of reporter as home country of mother corporation

4. Within one legal entity



Does the tax system recognize foreign losses in the home-country:

1. If foreign activity = permanent establishment

Austria

Losses of foreign P.E. can be offset against profits of the head office in Austria. In case the foreign P.E. turns profitable and can avail itself of loss carry-forwards the foreign losses claimed as a deduction in Austria have to be added back to taxable income of the head office (recapture) so there is no doubt-dip of loss carry-forwards.

Belgium

Yes.

Cyprus

No.

Czech Republic

No.

Denmark

Yes.

Estonia

N/A.

Finland

Losses of a foreign permanent establishment can be deducted in the Finnish corporation for Finnish tax purposes. The mentioned losses can also be part of the loss confirmed in Finland. However, the aforementioned rule does not apply, if there is a tax treaty between the two countries and exemption method is used in the taxation of business income. Normally, however, the double taxation of business income is avoided by credit method in the tax treaties concluded by Finland.

The time period for the right to utilise tax losses in Finland is ten subsequent tax years. Due to the change of ownership the right to utilise the tax losses is forfeited unless an exceptional permission is granted by the tax authorities.

France

No, in principle (see below).

Germany

According to the existing tax treaties with the EC membership countries, Germany has not the right to tax profits of permanent establishments in EC-countries. Nevertheless until 1998 it was possible to claim foreign losses under certain conditions. But in 1999 this regulation was disposed. There is no longer a possibility to recognize losses from foreign P.E.'s in Germany.

Legal norm (until 1998): Sec. 2 Para. 3 income tax act (EStG)

Ireland

Yes.

Italy

The Italian tax system is based on the worldwide income principle; consequently, profits deriving from the activity carried on by a foreign P.E. are taxable at the Italian mother corporation in the home country. For the same reason, losses of a foreign P.E. should be deductible from the Italian mother corporation income. It has to be noted, however, that the Supreme Court (Sez. I, Sent. n° 11918 dated 14 December 1990) has denied such deductibility.

Latvia

Income of foreign PE-s is taxable according to rules of the respective foreign country and tax convention if available. In general all income and expense is included in the annual CIT computation, but it is required to prepare separate CIT computation for PE based on Latvian rules.

No specific rules are set for tax loss In practice by interpretation of the law tax loss of foreign PE is taken to parent company, however these are rare occasions and usually treatment is agreed with tax authorities on case by case basis.

Luxembourg

Tax treaties with EU countries are based on exemption method. So losses are not offset. However, they reduce local taxation by influencing the tax rate applicable on local income. Applicable tax rate on local income is defined by reference to total income (local + exempt).

Malta

Loss relief is available if the Corp 1 is a parent/subsidiary of the Malta Company.

The Netherlands

Yes.

Portugal

Yes. Resident entities are liable on the worldwide income.

Romania

No, the losses of a foreign P.E. are deductible only from the next 5 consecutive years profits of that specific P.E.

Slovenia

Yes.

Spain

Yes, the Spanish tax legislation recognises foreign losses.

Sweden

Yes (according to internal legislation, according to tax treaty se below point 10).

UK

Yes.

2. If foreign activity = not permanent establishment

Austria

In this case losses incurred by the foreign P.E. are recognised at the Austrian head office.

Belgium

Yes.

Cyprus

No.

Czech Republic

No.

Denmark

Yes.

Estonia

No.

In Estonia a resident legal person do not pay income tax on income and consequently carry back or forward of losses is not applicable for tax purposes.

Finland

Losses of foreign activity can be deducted in the Finnish corporation for Finnish tax purposes.

The taxable income or loss of a foreign P.E. or activity is primarily calculated on the basis of Finnish tax rules. In principle, the income of the foreign P.E. is regarded as taxable income in Finland and the expenses of the foreign P.E. as tax deductions in Finland (when credit method is in use). There are no specific regulations concerning the "double dip". There are no rules in the Finnish tax legislation concerning the liquidation of a foreign P.E., either.

France

Yes, in principle (see below).

Specified:
According to Article 209 – I of the French Tax Code, activities carried on abroad by a French company through a foreign branch are exempt from corporate income tax. The French definition of foreign branch is similar to that of the permanent establishment (within the meaning of OECD Treaty). However, it also includes "complete business cycles" performed outside of France, i.e. both purchase and sale abroad of the same goods made abroad.

Correspondingly, no tax credit is available in France for the foreign tax paid abroad. Likewise the tax losses realized by foreign branches cannot be included in the French company's tax profit (or losses) on which corporate income tax is assessed.

This general rule may not apply in the event of application of the CFC rules (Article 209 B of the French Tax Code: for more details, see CFC questionnaire) or of the "worldwide income taxation" system:

French companies which have received special approval from the Tax Authorities are taxed on their worldwide income, i.e. including the profit (or losses) of foreign branches ("bénéfice mondial"). They also may elect to calculate their taxable profits by adding to their own profits the profits (or the losses) of the French or foreign companies in which they directly or indirectly hold, subject to certain exceptions, at least 50% of the voting rights ("bénéfice consolidé").

Under "worldwide income taxation" system, foreign recognised losses are calculated by applying the French tax rules. "Double-dip" is not avoided.

In both cases, the foreign taxes comparable to the French corporate income tax may be used as a credit in France.

Such approvals have been granted by the Tax Authorities only on a very limited basis (around 10 groups at the present time).

Germany

When the applicable tax treaty concedes the right to tax the foreign activity to Germany, generally the whole positive and negative income will be recognised. Generally means that there are several restrictions made up. In Sec. 2 Par. 1 of the income tax act (EStG) a list of negative income from several sources, which will not be recognised by German tax authorities, is made up.

Additionally Sec. 2 Par. 2 of the income tax act (EStG) outlines exceptions to this list. Necessarily the losses must be assigned to the listed categories. Therefore it is important to know that the income of a corporation is in case of Sec. 2 income tax act (EStG) not generally qualified as income from trade or business, like it is done in the corporation tax act (KStG). But Sec. 2 of the income tax act is not applicable in case of an existing tax treaty. According to this, losses from EC – countries will generally be recognised, if the foreign activity is not a permanent establishment and Germany has got the right of taxation.

Ireland

No.

Italy

In this case due to the fact that the foreign "activity" is not carried on neither by a P.E. nor by a controlled corporation, these losses would be considered as "costs" of the mother corporation, deductible in respect of the domestic rules concerning the calculation of business income.

Latvia

If foreign activity is not a permanent establishment, CIT payable in Latvia can be reduced by tax paid abroad (to be supported with documentary evidence), but there is no regulation in respect of loss, therefore it is included to arrive at taxable income in the home country.

Luxembourg

If the tax treaty provides that the right to taxation lies with Luxembourg, income is treated in the same way as Luxembourg income. Else (e.g. Income from real estate) the answer is the same as for B.4.1.

Malta

Same as 1 above.

The Netherlands

Yes.

Portugal

No.

Romania

Yes. According to the Romanian Tax Act the revenues and the expenses of a foreign activity that is not a permanent establishment are considered as a part of the revenues and the expenses of the Romanian mother company. Consequently, the loss of the foreign activity can be used to offset the profit of the head office in Romania.

Slovenia

No.

Spain

Yes, the Spanish legislation recognises foreign losses.

Sweden

Yes.

UK

No.

If the reporter's country recognises foreign losses: how are foreign recognised losses being calculated (is there a need to restate the loss of the foreign P.E. by applying the head office country tax rules)? How is a "double-dip" (using the same loss in both countries) avoided?

Austria

Foreign P.E. losses have to be restated using Austrian tax rules.

No "double dip" possible (see below recapture rules).

Belgium

There is a need to restate the loss of the foreign permanent establishment by applying the Belgian tax rules.

Cyprus

Not applicable.

Czech Republic

N/A

Denmark

Losses must be calculated according to Danish law. No expense can be deducted in Denmark if it can be deducted in foreign income.

Estonia

N/A.

Finland

The taxable income or loss of a foreign P.E. or activity is primarily calculated on the basis of Finnish tax rules. In principle, the income of the foreign P.E. is regarded as taxable income in Finland and the expenses of the foreign P.E. as tax deductions in Finland (when credit method is in use). There are no specific regulations concerning the "double dip".

France

N/A (except under worldwide taxation system: see above).

Germany

The losses of foreign activities recognised in Germany have to be calculated by applying the German tax rules.Therefore German valuation provisions and accounting principles must be used. There is not any special norm to avoid a "double-dip".

Ireland

Foreign losses computed under Irish rules. "Double-dip" possible. If the foreign loss is from a separate trade, more restrictive use of losses.

Italy

In the Italian tax system, the loss of the foreign P.E. has to be restate by applying the mother company country tax rules. No rules are provided for avoiding a "double dip".

Latvia

See comment to question 1 above.

Luxembourg

No recognition of losses. Foreign income is assessed according to national rules in order to determine the tax rate applicable to worldwide income.

Malta

Yes according to Maltese tax rules.

The Netherlands

Apply Dutch rules to compute losses.

Portugal

It is necessary to restate the loss of the foreign permanent establishment applying the Portuguese tax rules.

Romania

When the foreign activity is not a P.E. the loss is calculated by applying the Romanian tax rules.

Slovenia

There is a need to restate the loss of the foreign P.E. by applying the head office country tax rules. Tax liabilities of the reporter are reduced for taxes, paid in the P.E. country.

Spain

The Spanish tax legislation provides the possibility of taking over foreign losses, recognising them by integrating the loss in the taxable base of the Spanish company, according to the Spanish tax rules.

There is no provision to avoid “double tip”.

Sweden

- Yes, there is a need to apply Swedish tax rules.
- Normally there is no “double-dip” as the loss in P.E.-country will be carry forward.

UK

By restating under UK tax rules.

If the reporter's country recognises foreign losses: What are the recapture rules (e.g. what happens when there are subsequent profits in the foreign P.E., when the foreign P.E. is liquidated, when a certain number of years has elapsed, etc)?

Austria

Subsequent profits of the foreign P.E. will also be taxable.

Belgium

Future profits will be added to the reporters local income for the amount of the losses originally deducted.

Cyprus

Not applicable.

Czech Republic

No.

Denmark

Recapture when subsequent profits or sale/liquidation whichever comes first.

Estonia

N/A.

Finland

There are no rules in the Finnish tax legislation concerning the liquidation of a foreign P.E., either.

France

N/A.

Germany

Recapture rules are not set up (v. No. 4 P. 1).

Ireland

Future profits taxable: if losses already used no shelter for profits.

Italy

The Italian tax system does not provide for any "recapture rule" of the foreign losses as a consequence of the subsequent events involving the P.E.

Latvia

No specific rules are set for such occasion, treatment to be agreed with tax authorities for each particular case.

Luxembourg

N/A.

Malta

N/A.

The Netherlands

After profits: no exemption, until losses are completely offset.

Portugal

N/A.

Romania

N/A.

Slovenia

Subsequent profits are reduced by previous losses (only for P.E.). When P.E. is liquidated, its previous losses may not reduced tax liabilities of the reporter.

Spain

The Spanish Corporate Income Tax Act provides that the profits from foreign permanent establishments remain exempt, when the conditions provided by law are fulfilled. In case there are subsequent profits in the foreign entity that produced the losses taken over by the Spanish mother company, these profits will be taxed until they surpass losses.

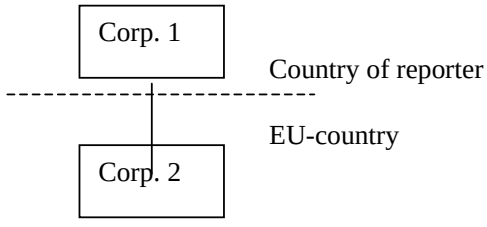
Sweden

- There are no specific recapture rules. Future profit (that exceeds the carry forward loss) will be taxed in Sweden.
- There is no time limit.

UK

N/A.

5. Between two legal entities



Does the tax system of Corp.1 recognize losses of foreign corporation? partnership?:

Austria

Losses from a foreign corporate entity are not recognised (cross-border "Organschaft" is not possible) but according to legislation proposed by the government will be recognised beginning as of January 1, 2005.

Losses incurred in a foreign partnership are treated in the same way as losses from a foreign P.E. in case the foreign partnership is deemed transparent according to Austrian tax rules (irrespective of how the partnership is being treated in its home country).

Belgium

No.

Cyprus

No.

Czech Republic

No.

Denmark

Yes – under joint taxation.

Estonia

No.

In Estonia a resident legal person do not pay income tax on income and consequently carry back or forward of losses is not applicable for tax purposes.

Finland

Finnish tax system does not recognise the losses of foreign corporation. The losses of foreign partnership can, however, be deducted against the taxable income from the partnership during ten subsequent years in accordance with the regulations concerning the carry forward losses (see above). The losses are calculated in accordance with the Finnish tax regulations. There are no regulations concerning the “double dip”.

The liquidation of a foreign corporation or partnership is taxed in accordance with the regulations concerning corresponding Finnish entities. When liquidating a corporation, the assets of the corporation are deemed to have been sold at their fair market value. When liquidating a partnership, the real estate, buildings, securities and rights are deemed to have been sold at their fair market value. The rest of the assets of the partnership are deemed to have been sold at their original acquisition price or fair market value if the latter is less than the acquisition price. The articles concerning capital gain in the tax treaties decide, which country is allowed to tax the possible liquidation gain.

In the Finnish tax reform, which concerning liquidation losses, came into force on 19 May 2004, significant limits were set on the option to claim deductions for liquidation losses from limited liability companies located in Finland, in the EU and in countries that have a tax treaty with Finland. This is due to the fact that corresponding capital and liquidation gains are tax exempt. Generally, corporate shareholders can deduct liquidation losses of corporate bodies only if their ownership in the liquidated company is less than 10% and they have held the shares for more than 1 year.

A loss upon sale/liquidation of a Finnish or foreign partnership is tax deductible at the Finnish parent company, but only against capital gains accrued in the loss year and during five subsequent years.

Write-down of an investment, other than fixed asset shares, may also be tax deductible when the requirements stated in the tax law concerning the deductibility of white-down are met. Due to the aforementioned tax reform, write-down of fixed asset shares is not any more tax deductible.

France

No, unless the worldwide taxation system applies (see above).

Germany

There is no legal option recognising losses of foreign corporations in Germany. An "Organschaft" (v. No. 2) is not applicable in this case. Even a write down of shares is prohibited for tax purposes.

Ireland

Foreign corporation: No.
Foreign partnership: See answer 3 above.

Italy

Generally under the Italian tax system the losses of foreign corporation and partnership are not deductible, but since the fiscal year 2004, the Italian Income Tax law, offers an option to tax the income of foreign corporation in Italy by the Italian corporation partner without regard to actual receipt thereof. In this tax system profits and losses of the foreign corporation are attributed to the Italian corporation partner in proportion to his participation.

This option, called "Base Unica Imponibile per il Gruppo di imprese non residenti ("International tax consolidation system"), must be exercised for at least five years.

The conditions to apply this option are the following:

1. the Italian parent corporation must hold directly or indirectly a control share of the capital and the voting rights of foreign subsidiaries.
2. the option must be exercised for all foreign companies hold by the Italian parent corporation;
3. all the corporations must have the same fiscal year;
4. the Statement of all corporations must be submitted to an auditing procedure by a certified auditor.

The option for this tax system must be validate by the Italian Fiscal Authority.

Latvia

No.

Luxembourg

Not for corporations. For partnerships see answer B.4.1. and B.4.2.

Malta

No.

The Netherlands

No, cross border fiscal unity is not possible.

Portugal

No.

Romania

No.

Slovenia

No.

Spain

The Spanish Tax system does not recognise losses from foreign corporations or foreign partnerships except when the securities portfolio depreciation mechanism is applicable.

Sweden

Corporation; No.
Partnership; See point 6 below.

UK

Foreign corporation	- no
Partnership	- yes

If the reporter's country recognises foreign losses: how are foreign recognised losses calculated (is there a need to restate the loss of the foreign P.E. by applying the head office country tax rules)? How is a "double-dip" (using the same loss in both countries) avoided ?

Austria

Foreign losses have to be restated applying Austrian tax rules.

Belgium

N/A.

Cyprus

N/A.

Czech Republic

N/A.

Denmark

Losses must be calculated according to Danish law. No expense can be deducted in Denmark if it can be deducted in foreign income.

Estonia

N/A.

Finland

The losses are calculated in accordance with the Finnish tax regulations. There are no regulations concerning the “double dip”.

France

N/A.

Germany

N/A.

Ireland

Under Irish rules. Double dip possible.

Italy

The loss of the foreign corporation must be calculated applying the mother company country tax rules. No rules are provided for avoiding a “double dip”.

Latvia

N/A.

Luxembourg

N/A.

Malta

N/A.

The Netherlands

N/A.

Portugal

N/A.

Romania

N/A.

Slovenia

N/A.

Spain

As commented in the previous point, with the securities portfolio depreciation mechanism provided by the section 12.3 of the Spanish Corporate Income Tax Act. The Spanish legislation provides (section 12.3 of the Spanish Corporate Income Tax Act) that this mechanism is applicable when:

A. In case of listed securities (in a national or a foreign stock exchange market), the accountancy provision entered will be tax deductible except when the participated corporation is resident in a country considered as a Tax Haven and in case the securities are the capital stock of the taxpayer.

The provision for depreciation of the securities portfolio could be accounted in case the market value is less than the acquisition value.

B. In case of non listed securities, there is a limit for the deductible depreciation accounted, which is:

the deductible depreciation < book value at the 1st day of the year – book value at the end of the year (taking into account all contributions and returns made during the year).

In case of foreign participated corporations we have to take into account the rules provided to avoid international double taxation.

Sweden

Partnership: see point 6 below.

UK

Losses would need to be recalculated under UK rules.

If the reporter's country recognises foreign losses: What are the recapture rules (e.g. what happens when there are subsequent profits in the foreign partnership, when the foreign partnership is liquidated, when a certain number of years has elapsed etc)?

Austria

Same rules as for a P.E. apply to foreign partnerships (if partnership is deemed transparent).

Belgium

N/A.

Cyprus

N/A.

Czech Republic

N/A.

Denmark

Recapture when subsequent profits or sale/liquidation whichever comes first.

Estonia

N/A.

Finland

The liquidation of a foreign corporation or partnership is taxed in accordance with the regulations concerning corresponding Finnish entities. When liquidating a corporation, the assets of the corporation are deemed to have been sold at their fair market value. When liquidating a partnership, the real estate, buildings, securities and rights are deemed to have been sold at their fair market value. The rest of the assets of the partnership are deemed to have been sold at their original acquisition price or fair market value if the latter is less than the acquisition price. The articles concerning capital gain in the tax treaties decide, which country is allowed to tax the possible liquidation gain.

France

N/A.

Germany

N/A.

Ireland

Any future profits taxed on same basis that losses allowed.

Italy

The Italian tax system doesn't provide for any "recapture rule" of the foreign losses as a consequence of the subsequent events involving the foreign corporations.

In case of interruption of "International tax consolidation system", before five years, the losses still not used by the Italian parent corporation are reduced proportionally to the ratio composed by the losses of the non resident company and the total losses of the companies involved. This provision is applicable even if the Italian parent corporation looses the control in the capital of the foreign subsidiary before five years.

Latvia

N/A.

Luxembourg

N/A.

Malta

N/A.

The Netherlands

N/A.

Portugal

N/A.

Romania

N/A.

Slovenia

N/A.

Spain

In case of subsequent profits after the losses have been taken over by the securities portfolio depreciation mechanism, what the Spanish company should do is to move back the depreciation provided.

Sweden

Partnership: see point 6 below.

UK

Profits taxed in UK – no recapture on liquidation or time basis.

Would a write-down of the investment in the foreign subsidiary or a loss upon sale/liquidation of the foreign subsidiary be tax deductible at the parent company?

Austria

Gains and losses from the sale of a foreign subsidiary are not taxable/not tax deductible; however, losses from the liquidation or bankruptcy of a foreign subsidiary can be claimed as a deduction over a 7-year period to the extent these losses exceed the tax-exempt dividends received in the 5 preceding years. The Austrian parent company can elect alternatively to have capital gains and capital losses from the sale of a foreign subsidiary fully taxable or tax deductible.

Belgium

Write downs of investment in a foreign subsidiary are only deductible in case of liquidation or bankruptcy and limited to the capital paid up.

Cyprus

No.

Czech Republic

No.

Denmark

Generally no – but if the period of ownership is less than three years a loss can be carried forward and offset against future gains on shares owned less than three years.

Estonia

N/A.

Finland

As a rule, a loss upon sale/liquidation of a share in a foreign corporation or partnership is tax deductible at the parent company in Finland. Write-down of an investment may also be tax deductibles when the requirements stated in the tax law concerning the deductibility of write-down are met.

France

Yes.

Germany

Neither a write-down of the investment, nor a loss upon sale/liquidation will be deductible in Germany.

Legal norm: Sec. 8b Para. 3 corporation tax act (KStG).

Ireland

Write-down: No.
Sale: Yes, but against other capital gains.

Italy

By the fiscal year 2004 the write down of the investment (the participation) in a foreign subsidiary is not fiscally deductible by the parent company, and the loss upon sale (of the share capital) and liquidation of the foreign subsidiary are not fiscally deductible at the mother company.

Latvia

Write-down of an investments is non-deductible

Loss upon sale/liquidations of foreign subsidiary is:

- deductible under common rules if the occasion of sale is one-off by substance (i.e. not normal activity and the only transaction of this type in the financial year) and if the investment has been held for at least 12 months prior to disposal;
- available for set-off against gains from sale of non-public securities in chronological order during 5 consecutive years.

Luxembourg

Yes.

Malta

No.

The Netherlands

Write down only in case of liquidation of subsidiary.

Portugal

N/A.

Romania

No.

Slovenia

N/A.

Spain

Yes, in case the securities portfolio depreciation is applicable.

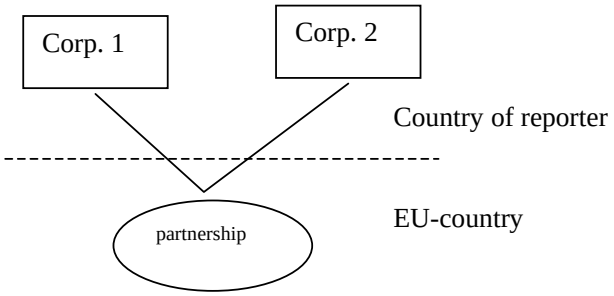
Sweden

No (if not inventory). For partnership see below point 6.

UK

Generally no – unless fully written down and negligible value claim made for capital gains tax purposes.

6. Between legal entity and partnership



Does the tax system of Corp.1 recognize losses of foreign partnership:

(a) If the partnership = permanent establishment

Austria

Losses from the sale / liquidation of a foreign P.E. or partnership are treated in the same way as current income / loss from the foreign P.E. or partnership: losses from a participation in a foreign partnership will generally be recognised in Austria (with subsequent recapture if profits are arising from the participation in the foreign partnership).

Belgium

See "foreign establishment" above.

Cyprus

No.

Czech Republic

No.

Denmark

Yes - partly deduction according to ownership.

Estonia

N/A.

Finland

The losses are recognised, see 5 above. However, the losses are not recognised both as losses of a P.E. and losses of a foreign partnership.

France

No.

Germany

See No. 4 P. 1.

Ireland

Yes, as at answer 3 above, this is considered for each partner.

Italy

In this case, the same considerations of point 4.1 apply.

Latvia

Income of foreign PE-s is taxable according to rules of the respective foreign country and tax convention if available. In general all income and expense is included in the annual CIT computation, but it is required to prepare separate CIT computation for PE based on Latvian rules.

No specific rules are set for tax loss. In practice by interpretation of the law tax loss of foreign PE is taken to parent company, however these are rare occasions and usually treatment is agreed with tax authorities on case by case basis.

Luxembourg

See B.4.1.

Malta

No.

The Netherlands

Yes, see foreign establishment.

Portugal

No.

Romania

N/A.

Slovenia

No.

Spain

Yes, Spanish tax system recognises losses from a foreign partnership.

Sweden

Yes.

UK

Yes.

(b) If the partnership = not permanent establishment

Austria

This depends. In general the loss will be recognised.

Belgium

See “foreign establishment” above.

Cyprus

No.

Czech Republic

No.

Denmark

Yes - partly deduction according to ownership.

Estonia

In Estonia a resident legal person do not pay income tax on income and consequently carry back or forward of losses is not applicable for tax purposes.

Finland

The losses are recognised, see 5 above.

Losses are calculated in accordance with the Finnish tax regulations. Concerning the double dip and liquidation, see 5 above.

France

Yes.

Please note that this matter is not clearly settled.

Germany

See No. 4 P. 2.

Ireland

No.

Italy

In this case, the same consideration of point 4.2 apply.

Latvia

Yes.

Luxembourg

See B.4.2.

Malta

No.

The Netherlands

Yes, if partnership is transparent entity.

Portugal

No.

Romania

N/A.

Slovenia

No.

Spain

Yes, the Spanish tax system recognises losses from a foreign partnership.

Sweden

Yes.

UK

Yes – but only if carrying on a trade.

If the reporter's country recognises foreign losses: how are foreign recognised losses being calculated (is there a need to restate the loss of the foreign P.E. by applying the head office country tax rules)? How is a "double-dip" (using the same loss in both countries) avoided ?

Austria

Foreign losses to be restated according to Austrian tax rules.

Belgium

See “foreign establishment” above.

Cyprus

N/A.

Czech Republic

N/A.

Denmark

Losses must be calculated according to Danish law.
No expense can be deducted in Denmark if it can be deducted in foreign income.

Estonia

N/A.

Finland

Losses are calculated in accordance with the Finnish tax regulations. Concerning the double dip and liquidation, see 5 above.

France

N/A.

Germany

See No. 4.

Ireland

Under Irish rules. Double dip possible.

Italy

N/A.

Latvia

See comment to (a) above.

Luxembourg

N/A.

Malta

N/A.

The Netherlands

Calculation: see foreign establishment.

Portugal

N/A.

Romania

N/A

Slovenia

N/A.

Spain

The recognition system provided is the integration of the loss in the taxable base of the Spanish company following the Spanish tax rules.

There is no legal provision to avoid “double dip”.

Sweden

Yes, there is a need to apply Swedish tax rules.
See above point 4.2.

UK

Recalculate under UK rules. Generally no double dip rules.

If the reporter's country recognises foreign losses: What are the recapture rules (e.g. what happens when there are subsequent profits in the foreign P.E., when the foreign P.E. is liquidated, when a certain number of years has elapsed etc)?

Austria

Recapture only when there is a profit.

Belgium

See "foreign establishment" above.

Cyprus

N/A.

Czech Republic

N/A.

Denmark

Recapture when subsequent profits or sale/liquidation whichever comes first.

Estonia

N/A.

Finland

See 5 above.

France

N/A.

Germany

See No. 4.

Ireland

Future profits taxable: if losses already used no shelter for profits.

Italy

N/A.

Latvia

No specific rules are set for such occasion, treatment to be agreed with tax authorities for each particular case

Luxembourg

N/A.

Malta

N/A.

The Netherlands

Recapture: see foreign establishment.

Portugal

N/A.

Romania

N/A

Slovenia

N/A.

Spain

The Spanish Corporate Income Tax Act provides that the profits from foreign permanent establishments remain exempt in case the partnership would be a P.E., when the conditions provided by law are fulfilled, subsequent profits of the P.E. will be taxed until losses are completely offset.

When the partnership is not a P.E., the profits will be directly taxed. There is no exemption applicable.

Sweden

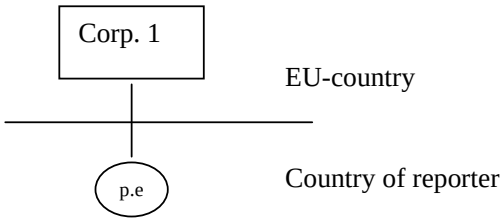
See above point 4.2.
- A subsequent profit in a foreign partnership will be taxed in Sweden.
- If a foreign partnership is liquidated there is a capital gains taxation. The acquisition price is adjusted with deductible losses (taxable profits, withdrawals and contributions).
- No time limit.

UK

Profits taxable in UK – otherwise no recapture.

C. Outwards (cross border) take over of losses: your country as home country of daughter comp.

7. Within one legal entity



Does the tax system recognize losses of Corp. 1 in the home-country of the 'activities':

(a) If activity = permanent establishment

Austria

No.

Belgium

No.

Cyprus

No.

Czech Republic

No.

Denmark

No.

Estonia

N/A.

Finland

The losses of foreign corporation are not recognised.

France

Only the losses incurred by the permanent establishment are recognized.

Germany

The German tax law only recognises losses of the activities in connection with the limited tax liability of the corporation.

In this case only the losses of the permanent establishment will be recognised and can be carried forward or offset against other taxable income in Germany if this is not subject just to withholding tax at source.

Ireland

Yes.

Italy

No.

Latvia

No.

Luxembourg

No.

Malta

No.

The Netherlands

No.

Portugal

No.

Romania

No.

Slovenia

No.

Spain

The Spanish legislation does not recognise the losses of the foreign mother company when the Spanish daughter entity is a P.E.

Sweden

No.

UK

No.

(b) If activity = not permanent establishment

Austria

No.

Belgium

No.

Cyprus

No.

Czech Republic

No.

Denmark

No.

Estonia

In Estonia a resident legal person and registered P.E. do not pay income tax on income and consequently carry back or forward of losses is not applicable for tax purposes.

Finland

The losses of foreign corporation are not recognised.

France

No.

Germany

Only losses realised in connection with activities, which lead to a limited tax liability and are not subject to a withholding at source will be recognized.

Ireland

No.

Italy

No.

Latvia

No.

Luxembourg

No.

Malta

No.

The Netherlands

No.

Portugal

No.

Romania

No.

Slovenia

No.

Spain

In case the Spanish daughter entity is not a P.E., the Spanish legislation does not provide the recognition of the losses of the foreign mother company, either.

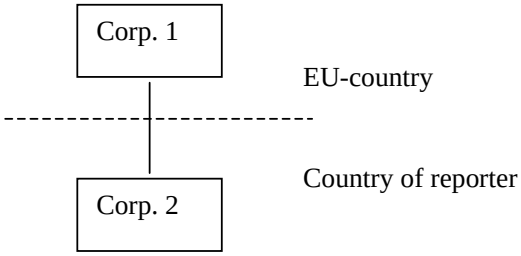
Sweden

No.

UK

No.

8. Between two legal entities



Does the tax system of Corp.2 recognize losses of foreign Corp. 1?

Austria

No.

Belgium

No.

Cyprus

No.

Czech Republic

No.

Denmark

No.

Estonia

No.

In Estonia a resident legal person do not pay income tax on income and consequently carry back or forward of losses is not applicable for tax purposes.

Finland

The losses of foreign corporation are not recognised.

France

No.

Germany

It does not exist any legal possibility.

Ireland

No.

Italy

No.

Latvia

No.

Luxembourg

No.

Malta

No

The Netherlands

No.

Portugal

No.

Romania

No.

Slovenia

No.

Spain

The Spanish legislation does not recognises the losses of a foreign company when the Spanish entity is a daughter company.

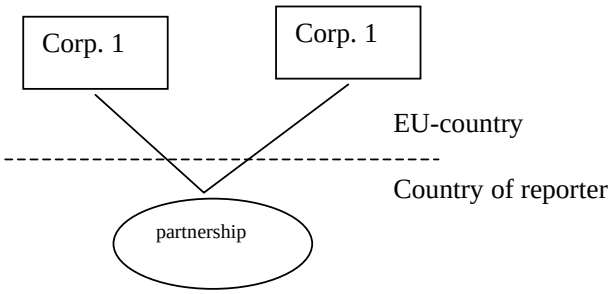
Sweden

No.

UK

No.

9. Between partnership and corporation



Does the tax system of the partnership recognize losses of Corp. 1 or Corp.2?:

(a) If the partnership = permanent establishment

Austria

No.

Belgium

No.

Cyprus

No.

Czech Republic

No.

Denmark

No.

Estonia

N/A.

Finland

The losses of foreign corporation are not recognised.

France

No.

Germany

See No. 7. P (a).

Ireland

Yes. Losses of partners recognised separately.

Italy

No.

Latvia

No.

Luxembourg

No.

Malta

No.

The Netherlands

No.

Portugal

No.

Romania

No.

Slovenia

No.

Spain

The Spanish legislation about take over of losses, does not allow the recognition of losses of foreign corporation by Spanish partnerships which are P.E.

Sweden

Partnerships are not subject to income tax, but their income is taxed at the partner level.

UK

No.

(b) If the partnership = not permanent establishment

Austria

No.

Belgium

No.

Cyprus

No.

Czech Republic

No.

Denmark

No.

Estonia

N/A.

Finland

The losses of foreign corporation are not recognised.

France

No.

Germany

See No. 7. P (b).

Ireland

No.

Italy

No.

Latvia

No.

Luxembourg

No.

Malta

No.

The Netherlands

No.

Portugal

No.

Romania

No.

Slovenia

No.

Spain

In case the Spanish partnership is not a P.E., the Spanish legislation about take over of losses, does not allow the recognition of losses of foreign corporation, either.

Sweden

Partnerships are not subject to income tax, but their income is taxed at the partner level.

UK

No.

10. When losses arise in a foreign P.E. or partnership the tax treatment could be different depending on whether the applicable tax treaty operates the exemption or the credit method for foreign income Is this the same for your country?

Austria

Austria has changed its rules and now allows the recognition of losses irrespective of whether the treaty operates under the exemption or the credit method.

Belgium

N/A.

Cyprus

N/A.

Czech Republic

No.

Denmark

No - see questions 4 and 6.

Estonia

N/A.

Finland

Yes, see 4 above.

France

N/A.

Germany

The former Sec. 2 Para. 3 income tax act (EStG) presumed the exemption from the German taxation by the applicable tax treaty (cf. No. 4 P. 1).

But at the moment there does not exist a similar regulation in Germany. Independent of a tax treaty the losses of a foreign P.E. cannot be considered in Germany.

Ireland

Ireland only operates the credit method for foreign tax on branches.

Italy

No, all Italian tax treaties operate under the credit system.

Latvia

No specific rules are set.

Luxembourg

No Treaty with EU countries has credit system. The general rule is that foreign income subject to credit method forms a subtotal that may not be negative. Therefore, losses may only be offset or carried forward within that category.

Malta

Income from a foreign P.E. is taxable in Malta (the worldwide basis of assessment). Losses arising in a branch can be relieved.

The Netherlands

No.

Portugal

No.

Romania

In Romania, irrespective of whether the treaty operates under the exemption or the credit method, the rule is that foreign income is subject to credit method.

Slovenia

Yes.

Spain

The Spanish legislation about the take over of losses does not take into account the tax treatment provided by Tax Treaties to avoid double taxation.

Sweden

Yes.

UK

N/A.