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In this issue

1 Direct Taxes
New filing regulations for Financial Statements as at 31 December 2007 and increase of fines starting from 1 July 2006
by Eva Maria Koenigshofer

2 Interesting opportunities for investors provided by Austrian DTAs
by Christof Woerndl and Robert Pfeiffer

3 A modest home can create a residence for income tax purposes in Austria
by Gabriela Fertl

Indirect Taxes
3 Stamp Duties
by Christof Woerndl and Alexandrer Lechner

4 VAT fraud – Carousels and Missing Traders
by Gerald Dipplinger

Expatriates
4 Harmonization of Travel Expenses across the Corporate Group
by Ulrike Vidovitsch and Lisa Beisteiner

5 Compulsory Registration of Foreign Company Car in Austria – Possible Violation of EC-Law
by Ulrike Vidovitsch and Lisa Beisteiner

6 International Assignments – Applicability of Austrian Labor Law
by Lisa Beisteiner

Expatriates
7 Transaction costs in a share deal
by Guelay Karatas

8 Austrian Tax Facts & Figures

Direct Taxes

New filing regulations for Financial Statements as at 31 December 2007 and increase of fines starting from 1 July 2006

With effect from a balance sheet date of 31 December 2007, all financial statements must be submitted electronically to the commercial register. Only companies whose revenues do not exceed EUR 70,000 in the last twelve months before balance sheet date are exempted, and they may continue to file in paper form.

Furthermore, fines for non or late disclosure of the financial statements have been increased from 1 July 2006. The commercial court can impose additional fines, depending on the size of the company if the legal representatives do not follow the electronic filing obligations. For a medium sized company the fine is tripled, for a large sized company it is increased six fold to EUR 3,600. These increased fines also apply for financial statements which are not filed yet or which have to be submitted before 30 September 2006.

As accounts have to be filed within 9 months of the balance sheet date, and the first balance sheets affected are those for 31 December 2007 and onwards, the effect of the new electronic filing requirement will not commence until the end of September 2007.

In addition to the Publizitätsrichtlinie-Gesetz the Gerichtsgebührengesetz has been renewed. If the financial statement is filed in electronic form, one can save costs of EUR 44 per year.

Until the obligation of electronic filing becomes effective, three copies of the financial statements have to be filed. After the introduction of the new requirements, only one copy must be filed.

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Interesting opportunities for investors provided by Austrian DTAs

Certain Austrian Double Taxation Agreements (DTA) contain exemption- and matching credit-provisions for interest income, thereby reducing or eliminating Austrian tax.

As a general rule, interest income received by an Austrian corporate entity is subject to 25% income tax. Withholding taxes imposed by the source state is generally credited against the Austrian tax burden.

Some DTAs however provide for beneficial exceptions to that rule: two different types of exemption can be distinguished.

Tax exemption from Austrian tax (applies vis-à-vis Argentina, Greece, Brazil and Pakistan)
Under this scheme, only the state of source has the taxation right. All interest income arising in the other contracting state is therefore tax exempt in Austria. In return, expenses related to the exempt investment are not tax deductible in Austria. While the DTAs with Argentina and Pakistan provide for an exemption of all interest income, the exemption contained in the DTAs with Greece and Brazil is generally limited to government bonds. Note, however, that Brazilian sourced interest income that does not benefit from the exemption, should be covered by the matching credit provision (see below).

Matching Credit Provisions (e.g. Brazil, Thailand, Korea, Malaysia)
Under these provisions, Austria grants a tax credit for foreign withholding taxes irrespective of whether such withholding taxes were actually levied. The Austrian tax burden will be reduced by the full amount of the matching credit even if the state of source either imposes no withholding tax at all or imposes withholding tax at a lower rate. DTAs with a matching credit of 25% thus generally lead to a full tax exemption in Austria.

Source State	Tax benefits available to Austrian resident entities
Argentina	Total Exemption of all Argentinian sourced interest income in Austria.
Brazil	Interest from Brazilian government bonds or interest paid from a debtor corporation fully owned by the Brazilian government is exempt from Austrian taxation. All other interest income received from Brazilian debtors benefits from a matching credit of 25%. Therefore, Austria essentially does not levy corporate income tax on interest payments from Brazil.
China	Matching Credit of 10%, i.e. Austria basically levies 15% corporate income tax on the interest.
Greece	Interest from Greek government bonds is exempt from Austrian taxation.
Indonesia	Matching credit of 15%.
Israel	Interest income received from Israeli debtors benefits from a matching credit of 15% provided that the Israeli tax administration grants tax benefits on interest income to the investor.
Korea	Matching Credit of 15%.
Malaysia	Malaysian qualifying bonds benefit from a matching credit of 15%.
Malta	Matching Credit of 5%.
Mongolia	Matching Credit of 10%.
Pakistan	All interest arising in Pakistan and paid to an Austrian resident may exclusively be taxed in Pakistan.
Thailand	Interest income received from Thai debtors benefits from a matching credit of 25%, i.e. Austria basically does not levy additional corporate income tax.
Tunisia	Matching Credit of 10%.
Turkey	Matching Credit of 10%.

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A modest home can create a residence for income tax purposes in Austria

Taxpayers may have a residence available in several countries. The fact that a small apartment in Austria is only used for temporary visits will establish a tax residence and will lead to unlimited income tax liability in Austria. This position was again confirmed in a recent decision of the Supreme Court.

Resident taxpayers are subject to unlimited income tax liability with their worldwide income in Austria.

A fiscal residence according to the General Fiscal Code ("Bundesabgabenordnung") is an apartment/house that is occupied by the taxpayer with the intention to use and keep it for private residential purpose. The taxpayer must be in a position to use the Austrian property at any time without having to make considerable changes beforehand. The size and the interior equipment of the domicile have to correspond to the living circumstances of the taxpayer in order to be regarded as a tax home.

But the Austrian Tax Law does not require that a tax home must correspond to the social standard, the representative needs or to the personal economic situation of the taxpayer. The opinion of a taxpayer that a small and modest flat of only two rooms in Austria does not correspond to his living circumstances or does not meet his requirements for personal comfort is not decisive.

A tax domicile is considered according to objective criteria. If there are rooms available and if they are properly equipped for personal residential use, a tax residence in Austria will be created.

It cannot be argued that the property is only available to the spouse of the taxpayer based on the fact that the Austrian apartment is rented by the spouse. Further evidence is necessary in order to argue that the domicile of the spouse does not serve as a home for both spouses and will thus not create tax residence for the taxpayer.

The private residential use is not limited to permanent or regular use. Even casual and limited use of a home in Austria by the individual can create a tax residence.

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Indirect Taxes

Stamp Duties

This article shall provide a brief description of the latest developments and news in the field of Austrian stamp duty.

Stamp duty mitigation standards

As a general rule, loan agreements give rise to 0.8 % stamp duty if a written agreement is signed in Austria or, if signed abroad, the loan has a nexus in Austria. For shareholder loans a special regulation exists: the stamp duty is triggered by the mere bookeeping entry at subsidiary level. An Austrian taxpayer tried to avoid creating such shareholder loan by the following structure: The shareholder A granted a loan to its indirect subsidiary C, who forwarded the loan to the direct subsidiary B. Though the obvious goal was to mitigate the stamp duty exposure, the transactions have not been planned well: The shareholder instructed the bank to carry out the cash transactions on the same day in identical amounts, while no loan agreements were set up. As a consequence the Austrian tax authorities ignored the loan between A and C and considered the transaction as a taxable shareholder loan between A and B.

To protect legal transactions from being reinterpreted by the Austrian tax authorities, the following guidelines are recommended: ensure there is

- clear evidence of the transactions, creating legal proof of the transaction,
- careful execution of the transaction as laid down in the mitigation strategy.

Stamp duties and tax abuse?

Tax abuse is assumed where a combination of legal transactions has a sole tax avoidance purpose. In abusive cases, the tax is levied in accordance with the underlying real economic activities. In the course of an appeal procedure an independent tax court recently stated that the avoidance of stamp duty per se cannot be seen as abusive.

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VAT fraud – Carousels and Missing Traders

The joint proposal of Austria and Germany to apply the reverse-charge system on all supplies of goods and services between businesses to fight against VAT fraud in the EU was denied by the Commission in July 2006. However, recent cases in Germany show that the organised VAT fraud is not on the decline. Due to the legislation in Austria, not only the state but also honest businesses may be affected by the activities of tax evaders.

"Whoever robs a bank nowadays shows that he has no idea about VAT". This statement of an Austrian tax officer shows the current attractiveness of organised VAT fraud in Austria and in the EU. The Austrian Finance Ministry assumes the loss due to VAT evasion to be approx. EUR 850 million per year. In Germany the VAT loss in 2005 due to fraud is estimated to be approx. EUR 17 billion. In August this year a major case was revealed in Germany with a potential loss of EUR 150 million.

Currently there are three main types of VAT fraud: The black economy, falsification of invoices and the so-called carousel fraud or missing traders fraud (2% of the total VAT income p.a. is lost due to carousel fraud in Germany).

How does carousel fraud work? If a company (X) purchases goods from abroad, no VAT should be charged as the transaction is either zero-rated as import or intra-Community supply of goods in the country of origin. X then sells the goods to a domestic recipient (Y) charging local VAT. Y sells the goods to a recipient situated abroad (EU or non-EU recipient) without charging VAT (zero-rated export or intra-Community supply of goods). Due to these transactions, Y is always in a credit position as Y receives invoices with VAT and issues invoices without VAT. Y receives therefore a VAT refund from the tax administration whereas X who is liable for the VAT charged vanishes or goes bankrupt without paying the VAT to the tax office ("missing trader").

There are many variations to this basic case. The term carousel derives from the fact that in a lot of cases, the foreign recipient of Y is at the same time the supplier of X. Thus, the goods can be circled around many times which increases both the amount of input VAT refunded and loss for the tax administration (at least 20 Mio EUR per carousel). Additional traders can be included in the carousel to make the detection by the tax administration more difficult.

Not only the tax administration but also honest businesses can be affected by carousel fraud: If the missing trader happens to be a non-resident company which sells goods to a company in Austria, the recipient in Austria is liable for the VAT not paid by the non-resident supplier. Therefore, in this case the recipient in Austria should withhold the VAT charged by the non-resident supplier and pay it over the tax account of the recipient. In all cases, the identity of new business partners should be checked closely before starting business with them.

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Expatriates

Harmonization of Travel Expenses across the Corporate Group

Companies planning to introduce uniform guidelines on the reimbursement of travel expenses have to take into consideration labor and tax law provisions effective in Austria.

In order to cut administration costs, many groups implement uniform guidelines on the compensation of expenses incurred in the course of business trips. Frequently the question arises whether daily allowances according to labour law can be replaced by reimbursement against the presentation of receipts.

For employees working in Austria any such regulation needs to respect the employee's minimum entitlement as concerns travel expenses refunds (based on labour law), as well as taking into account statutory tax restrictions on the amounts which can be reimbursed before they are conside-

red as salary for wage tax and social security purposes.

The employees' labor law entitlement (preconditions for reimbursement and amount refunded) is generally based on the applicable collective bargaining agreement (CBA), if any, or any plant agreements or general guidelines in place. Failing any such regulations, travel expense reimbursements can also be agreed on individually in the single employment contracts. The provisions set out in the CBA are mandatory and employers are required to draft any internal terms of reference or work contract along the lines set herein. Specifying the terms of reimbursement in a general directive is recommended, as the subject can be dealt with consistently and covering all employees. However, the employer should reserve the right to unilaterally amend such guidelines, which can be devised as an annex to the individual employment contracts.

Furthermore, reimbursements will only be treated as tax exempt and not subject to social security contributions, so long as the following restrictions set by the Austrian Act on Income Tax (cf. § 26 Z 4 EStG) are not exceeded: Firstly, the travel in question needs to be a business trip for the purposes of § 26 Z 4, which is the case if either the definition of any applicable CBA or else the definition set out in the EStG itself is met. Secondly, the maximum amounts as stipulated in the EStG must not be exceeded; different amounts apply to business travel within Austria and business trips abroad, respectively.

As regards business trips within Austria the full per diems (daily allowances) for tax law purposes are currently Euro 26.40; overnight allowances are restricted to Euro 15.00, unless any higher amount can be evidenced on the basis of receipts. Per diems can no longer be paid free of tax as soon as the business trip's destination becomes a new "centre of employment activity". A new centre will be regarded as established where the employee continuously renders services at or at least regularly returns to a particular destination for more than five days; subsequently a waiting period of six months applies. A new centre of employment activity is also created if the employee irregularly returns to one destination for more than 15 days within one calendar year.

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Compulsory Registration of Foreign Company Car in Austria – Possible Violation of EC-Law

The Austrian statutory obligation to register a company car provided to the Austrian employee by his foreign employer is possibly at variance with the provision of Art 39 EC on the free movement of people.

The directly applicable provision of Art 39 EC guarantees the free movement of people throughout the member states of the European Community. Ranking among the EC primary legislation it takes priority of application over any conflicting national law. Thus member states are obliged to refrain from applying any contradicting national regulations and have to replace said national legislation by rules conforming to European law.

Where a worker domiciled in Austria is being employed by a legal company established in a second member state of the EU and is rendering the services due in the course of his employment relationship in the second state's territory, he is to be regarded as exercising his right of free movement of people. Any Austrian provisions, including those on the registration of a company car made available to the employee by his foreign employer, for example the Austrian Act on the Use of Motor Vehicles (KFG) and the Austrian Act on Taxation of the Standard Consumption of Motor Vehicles (NoVAG) – are to be judged in the light of Art 39 EC.

Recently, after several decisions handed down by the Court of Justice of the European Communities (ECJ, cf. e.g. RS C-232/01) the conformity with European law of those Austrian provisions, which require registration of the company car, has been drawn into question.

Accordingly, if an Austrian-based employee is being granted a company car by his employer legally established in a second EU-Member State for business as well as for private use – the vehicle being registered in the second state only – and said employee subsequently uses the vehicle in the second state's territory as well as for journeys to his Austrian home, the

obligation to register the car in Austria could be at variance with Art 39 EC. ECJ proceedings formally dealing with the Austrian case at hand have not been initiated as yet.

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International Assignments – Applicability of Austrian Labor Law

In the event that an employee is assigned to Austria his labor contract will be governed by the mandatory provisions of Austrian employment law if the assignment is not temporary. This applies in particular to minimum wages, provisions on giving notice, restrictions on working time, annual vacation entitlement etc.

As generally known, Austrian law abounds with mandatory provisions regulating employment relationships. When assigning employees to Austria, however, the underlying contracts can be designed as to prevent these provisions from becoming applicable. According to the European Convention on the law applicable to contractual obligations of June 19, 1980 (ECC) it first needs to be determined whether the assignment at hand qualifies as a genuine – that is a temporary – assignment. In such cases Austrian labor law is generally inapplicable; assignment arrangements thus can be shaped so as to reflect their quality as merely temporary. However, should the assignment not be temporary, the full range of Austrian employment law applies; Austrian mandatory provisions (Art 6 sec. 1 ECC) cannot be waived even in case of choice of law of a third state.

In designing an international assignment the following should be taken into account:

- If the assignment is entered into for a limited time period only, this may indicate a genuine assignment; in general, assignments covering longer periods, however, can be seen as “temporary“, too.
- In order to support the “temporary” nature of the assignment, the focus of the employment relationship needs to remain in the home country eg by means of continuous organizational integration or continuous duties to report; there should be a clear intention that the employment will resume in the home country in the foreseeable future.
- In circumstances where the employee is obliged to perform his main services in the course of his employment relationship in Austria und the parties do apparently not envisage him taking up work in his “home country“ at all, the assignment is not temporary. This also holds true if the employee takes part in mere occupational training in his “home country“ prior to his assignment to Austria.
- Should the task assigned to the employee require long-term commitment in order to be accomplished, the assignment will not be regarded as temporary (as eg the management of an Austrian subsidiary. However, management solely for training purposes may be temporary as in such cases the assignment’s purpose is limited to a certain period of time).
- If the assignment is limited to a specific purpose after the accomplishment of which the assignee will return to his home country (eg project-oriented work) the assignment shall be regarded as temporary.
- Should the employment contract in the “home country“ be of a limited time period or should it be terminated on the occasion of the “assignment”, this indicates a permanent place of work in Austria. Should the employment contract in the home country be entered into for an unlimited time period and provide for the assignee’s return to the home country and his resumption of work there, this suggests a temporary assignment.
- A precondition for a temporary assignment is a habitual place of work in the home country prior to the assignment, but does not require that work in performance of the employment contract has actually been carried out there already. The conclusion and simultaneous suspension of the “home country“ employment contract indicates the relocation of the habitual place of work to Austria. Apart from that the home country-employment contract can generally be suspended for the duration of the assignment, without precluding the temporary nature of the assignment.

It should be emphasized that even if the assignment qualifies as temporary, Austrian qualified mandatory provisions (Art 7 sec. 1 ECC; eg Act on the Protection of Pregnant Women and Mothers) will be effective for the assignee if “the situation” evidences a sufficiently close connection to Austria.

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Transaction costs in a share deal

A share deal triggers different tax consequences than an asset deal – also with regard to tax deductibility of transaction costs such as due diligence costs, advisory fees and finance costs. Structuring an acquisition should therefore consider transaction costs to ensure maximum tax deductions.

As a general rule for a share deal, the purchaser's tax basis of the shares acquired includes the purchase price for the shares plus incidental acquisition costs. There is no tax depreciation for the shares. A write-off in connection with an impairment in value of the acquired shares can, under certain circumstances, be expensed tax effectively over seven years. Alternatively, an amortization of goodwill over a period of 15 years is possible within the Austrian group taxation regime under certain conditions.

Transaction costs directly incurred for the acquisition of shares are seen as incidental acquisition costs. Such costs are therefore not tax deductible, but have to be capitalized and increase the acquisition costs of the shares acquired. On the other hand, costs for the preparation of a potential acquisition, that do not directly arise in connection with the subsequent acquisition, are tax deductible. Therefore, it is essential to distinguish between costs that arise before a final decision about the acquisition of the target is made and such costs that arise subsequently. Based on these basic principles the tax effects of typical transaction costs are as follows:

- Costs for drafting the contracts, broker provisions and notary costs etc. are deemed to be directly linked with the acquisition and therefore are never tax deductible in a share deal.

- While broker provisions are deemed to be directly linked with the acquisition, provisions and other costs arising in connection with the financing of the purchase price are not seen as incidental acquisition costs. Therefore, such costs do not increase the tax basis of the shares acquired. Instead, costs arising in connection with the raising of equity are immediately tax deductible. Regarding debt financing such costs have to be capitalized and amortized over the loan or credit period.

- In practice, a major part of transaction costs result from a due diligence. Typically, the purpose of a due diligence is to evaluate if the acquisition of an existing business is feasible for the potential purchaser. Therefore, due diligence costs are not automatically incidental acquisition costs but might be tax deductible. However, this depends on the circumstances of the case and the purpose of the due diligence. If the purchaser has already made the final decision regarding the acquisition and the purpose of the due diligence is merely to determine the final purchase price, tax deduction might be at risk and could be challenged in a tax audit.

To ensure tax deductibility of due diligence costs, careful structuring is essential – especially if the purchaser is a business group or investment fund. It is important to note that transaction costs that are first borne by an already existing group company and recharged to a newly established acquisition vehicle subsequent to the acquisition might not be seen as preparatory, indirectly acquisition related costs at the level of the acquisition vehicle. Experience of recent tax inspections are that such costs are treated as non tax deductible incidental acquisition costs at the level of the acquisition vehicle by Austrian tax inspectors.

With regard to transaction costs the purchaser should therefore ensure that the acquisition vehicle is established at an early stage of the transaction process. The acquisition vehicle should directly engage the advisors and bear the costs for financing the acquisition of the shares.

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Austrian Tax Facts & Figures

Taxation of corporations

Corporate income tax rate (Basis – adjusted statutory accounts)	25%	Non-deductible expenses (examples)	
Dividend withholding tax	25%	Long-term accruals	20%
Witholding tax on licences/royalties	20%	Business meals	50%
Interest	0%	Excessive car expenses for luxury cars	
Significant allowances		Tax loss carry forwards	
Research & Development (R&D) (Alternatively premiums in cash: 8%)	up to 35%	Losses may be carried forward for an indefinite period of time	
Learning & Education (L&E) (Alternatively premiums in cash: 6%)	up to 20%	Usage of tax losses: 75% of taxable income	

Double taxation agreements

with 68 countries – mainly exemption method

International participation exemption for holding companies	
Conditions: Investments >10%, 1 year holding	
Dividends	0%
Capital gains	0%
Thin capitalization rules	None
CFC rules	None

Group taxation

valid from January 2005

Consolidation of tax losses with taxable profits
Conditions: Qualifying participations > 50%
Group agreement and agreement on allocation of cost
Losses of foreign participations may be offset against profits of group leader

Annual taxable		Income Tax		Effective Tax Rate	Marginal Tax Rate
to	€ 10,000	€ 0		0%	0%
over to	€ 10,000 € 25,000	$\frac{(EK - 10{,}000) \times 5{,}750}{15{,}000}$		0 - 23%	38.333%
over to	€ 25,000 € 51,000	$\frac{(EK - 25{,}000) \times 11{,}335}{26{,}000}$	+ 5,750	23 - 33.5%	43.596%
over	€ 51,000	(EK - 51,000) x 50%	+ 17,085	> 33.5%	50%

Social security on monthly earnings up to EUR 3,630			
Employer's share	up to 21.9%	Payroll related taxes	approx. 8.0%
Employee's share	up to 18.0%		
Income cap for social security contributions, social security totalisation agreements with various states			

Value added tax

in line with the 6th EU directive

Standard rate	20%
Reduced rate (Food, rent, public transportation etc.)	10%
VAT refund for foreign enterprises – available up to June 30 of the following year.	

Other taxes

Real estate transfer tax	3.5%
Capital tax	1.0%
Stamp duties - Loan agreements	0.8%
Rent agreements	1.0%

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