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In this issue

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Deductibility of interest within a tax group

Pursuant to Sec 11 (1) 4 of the Austrian Corporate Income Tax Act (CITA) interest in connection with the acquisition of a participation is not tax deductible if this participation was acquired from an affiliated company. Recently the Austrian Fiscal Court (AFC) answered in two decisions the question whether the disallowance of interest applies also within a tax group contradictorily.

Decisions

On 22 October 2015 the AFC Klagenfurt accepted the tax deductibility of interest expenses arising in the course of an intra-group acquisition, despite the fact that Sec 11 (1) 4 CITA explicitly rejects the deductibility of interest in connection with the acquisition of participations from an affiliated company. The court argued that interest expense within a tax group is not related to tax-free dividends, since the group member´s income is subject to taxation at the level of the group parent. According to the AFC Klagenfurt, the disallowance of an interest deduction does not apply insofar as the tax-free dividend of a group member is not higher than its taxable income. However, if the tax-free dividend exceeds the taxable income of the group member, a deduction of interest is not possible to such an extent. The Austrian tax administration filed an appeal against this decision.

On 6 June 2016 the AFC Vienna decided contrarily in a similar case. However, in this case the corresponding interest income for the loan of the acquisition of the participation by a group member was even taxed by another Austrian group member within the same tax group. The AFC Vienna denied the deductibility of interest despite the existence of a tax group, since the wording of the law does not differentiate between interest paid to domestic (group) and foreign recipients. Therefore, the court argued that a teleological interpretation aiming at eliminating double taxation within a group is obsolete. An appeal was filed by the taxpayer to the Constitutional Court and the Supreme Administrative Court.

Implications

In the near future, the Supreme Administrative Court and the Constitutional Court will have to discuss the question whether the general deduction disallowance for interest income in connection with the acquisition of participations from an affiliated company is too extensive and therefore contradicts the purpose of the law.

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Austrian Supreme Administrative Court (VwGH): attribution of losses from tax-exempt foreign group members to the group parent

In a recent decision (case 2014/13/0029) the VwGH states that a tax exemption (due to tax holidays) of a foreign group member does not interfere with the attribution of losses from a foreign group member to the Austrian group parent. A different understanding can be found in the Austrian tax guidelines. The VwGH justifies its decision based on the fact that a recaptured taxation of foreign profits with which the losses can be (fictively) set off represents a more appropriate solution in the case of tax holidays rather than simply excluding the losses from attribution to the group parent.

Background

The decision of the VwGH is based on the legal position before the 1st Stability Act 2012, when it was possible to attribute foreign losses calculated only in accordance with Austrian tax law. Now the foreign loss has to be calculated in accordance with foreign tax law as well as Austrian tax law. Only the so calculated lower amount can be attributed to the Austrian group parent. The tax loss is limited to the amount of losses actually suffered based on foreign tax law. It is the interpretation of the Austrian Ministry of Finance that in the case of tax holidays the tax loss attributed to the Austrian group parent is nil. Further, only foreign losses from group members resident in EU member states and in states having entered into a comprehensive administrative assistance arrangement with Austria are attributable.

Implications

Because of this VwGH decision (based on the legal position before the 1st Stability Act 2012), it could be arguable even now (legal position after the 1st Stability Act 2012) that foreign losses – calculated in accordance with Austrian tax law – from foreign group members which are tax exempt can still be attributed to the Austrian group parent. The requirement stated in the literature is that the foreign losses be part of a loss carry-forward or similar in the foreign country.

The tax authorities have not commented on this decision yet.

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Envisaged exchange of information regarding cross-border rulings and advance pricing arrangements

Introduction

On October 17, 2016 the Austrian Ministry of Finance issued an information letter on the envisaged automatic or, respectively, compulsory spontaneous exchange of information regarding tax rulings and advance pricing arrangements. The exchange of information shall include any issued, amended or renewed rulings and advance pricing arrangements relating to cross-border transactions or to the question whether or not activities carried out by a person in another jurisdiction create a permanent establishment. In particular, unilateral transfer pricing rulings according to § 118 of the Austrian Federal Fiscal Code as well as written information provided by the tax authorities, which is only binding according to the principle of good faith, are in the scope of the planned exchange of information.

The reason behind a systematic communication of such information is not that rulings or advance pricing arrangements are per se qualified as preferential or that they are endangered to classify as illegal state aid by the EU commission, but because they directly or indirectly impact the tax position of the transaction partner of the intercompany transaction concerned in the other state. In this respect, the OECD states in item 109 of the final report on BEPS measure no. 5,"If the terms of such agreements are not available to the tax administrations dealing with related taxpayers, then there can be mismatches in how two ends of a transaction are priced and taxed with the result that profits go untaxed resulting in base erosion or profit shifting concerns."

Exchange with EU and non-EU states

Pursuant to the Mutual Assistance Directive (EU) 2015/2376 as amended on December 8, 2015, EU member states shall exchange information on advance cross-border rulings or advance pricing arrangements on a mandatory, automatic basis. The information to be communicated by a member state shall comprise basic information, as outlined under § 7 item 6 EU Mutual Assistance Act. The above information shall be exchanged, using a standard form, between the competent tax authorities of all other member states; further, a limited set of basic information shall also be communicated to the European Commission. The provisions on the mandatory exchange of information do however not apply to rulings exclusively concerning the tax affairs of one or more natural persons.

The information letter further specifies that information on rulings and advance pricing agreements will also be exchanged with countries outside the EU, if there is an agreement regarding a comprehensive mutual exchange of information in place which allows the provision of information to third parties. In particular, Article 7 of the Convention on Mutual Administrative Assistance in Tax-related Matters (Federal Law Gazette II No. 193/2014) as well as double tax treaties containing administrative assistance clauses reflecting Article 26 of the OECD Model Tax Treaty are thereto to be considered relevant and thus qualify as a basis for a compulsory spontaneous exchange of information. The spontaneous exchange of information shall cover basic information according to annex C of the final report regarding BEPS measure no. 5.

The information letter provides for regular intervals concerning the exchange of information, whereby it distinguishes between already existing and new rulings and advance pricing agreements. Based on our interpretation of the law, there still remains some ambiguity with regards to the tax authority's interpretation of the stipulated entry-into-force rules. The compulsory spontaneous exchange of information and especially its entry into force with countries outside the EU may thus prove to be tricky.

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Supreme Administrative Court decision: consideration of operating expenses when determining withholding tax on personnel lease of employees

In its decision of 15 September 2016 (GZ 2013/15/0136), the Supreme Administrative Court comments on the correct calculation of withholding tax on the provision of employees. According to this, operating expenses that are in direct connection with revenues must be considered.

In the underlying case employees of two Portuguese corporations were leased to an Austrian company, which was invoiced with a profit surcharge of approximately 10%. Although requested to do so, the Austrian company did not submit a certificate of residence for the Portuguese corporations to the relevant Austrian tax authority.

According to Austrian law, Portuguese companies are subject to limited income tax liability, whereas income from the provision of employees is subject to withholding of 20% of gross payments made by the debtor of the income (the Austrian company). In this case the debtor of the income is responsible for withholding and paying the tax amounts.

Using the gross payments as basis for assessment without considering the payments in direct connection with them (salary expenses), may result in the fact that a service provider resident in another EU member state is taxed at a higher rate in the tax withholding procedure than a locally resident service provider. This would be opposed to the freedom to provide services.

In the present case the question was whether the exercise of the freedom to provide services is linked to the existence of a certificate of residence. However, the Supreme Administrative Court rejected this, because the only relevant fact for making use of the freedom to provide services is that a corporation was founded according to the regulations of a member state and has its statutory seat, its headquarters, or its head office within the EU. A certificate of residence is thus not mandatory for the applicability of the freedom to provide services.

Furthermore, it was necessary to find a regulation to calculate the withholding tax which does not oppose to the freedom to provide services. In this context, the Supreme Administrative Court ruled that the gross income is to be reduced by the payments in direct connection with the provision of employees (salary expenses), provided they have been disclosed to the withholding agent. On this basis, the appropriate tax rate of 25% is to be applied. However, the withholding tax may amount to a maximum of 20% of gross payments.

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The tax-related key points of the Federal Government's new work programme 2017/18

In January 2017, the Austrian Federal Government agreed on a new work programme. We herewith present you the key points of the tax-related plans included in this work programme.

- The research premium shall be raised from 12% to 14% as of 1 January 2018.
- In favour of investments in physical assets (e.g. machines, but excluding buildings and passenger cars), companies with more than 250 employees shall be able to claim an accelerated depreciation to the amount of 30% (alternative implementation as investment growth premium). It is planned to restrict the measures to the period from 1 March to 31 December 2017, in order to create a targeted incentive for investments in the year 2017. Small and medium-sized companies profit from the previously decided investment growth premium for the years 2017 and 2018.
- A set of measures to avoid profit shifting shall be presented until the end of June, in order to ensure efficient taxation of foreign enterprises, especially in the online sector, in the future. Specific plans are for example to expand the advertising tax to the online sector and to reduce the tax rate.
- To compensate for bracket creep, as of 1 January 2019, the lowest two tax brackets of EUR 11,000 and EUR 18,000 shall be indexed automatically starting from a cumulative inflation of 5%.
- Halving of flight tax as of 1 January 2018.
- To create additional jobs, an employment bonus shall be introduced as of 1 July 2017 limited to 3 years. Companies will be refunded 50% of incidental wage costs for each additionally created job in the coming 3 years.
- Assets shall be mobilised as of 1 September 2017 by measures such as strengthening the potential influence of the beneficiary, as far as provided by the founder's intentions.

We will keep you informed about the legal implementation of the individual issues.

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Recent Changes in Value Added Tax

The Tax Amendments Act 2016 as well as the Update 2016 on the VAT Guidelines were recently published in the respective final version. Following are the most important changes that were implemented:

Tax Amendments Act:
The short-term rental of immovable property (i.e. for a continuous period of not more than 14 days) is compulsorily subject to VAT and the exemption for the rent of immovable property does not apply. This rule applies when the landlord uses the real estate only for supplies entitling to input VAT deduction (including other short-term leases) or for residential purposes.

This rule was implemented to avoid a pro-rata calculation in cases where short-term rentals were provided to persons not entitled to input VAT deduction (e.g. rent of space for weddings or events of banks/insurances).

Update 2016:
With regard to the definition of real estate, both the VAT Act and the VAT Guidelines (rec. 639v ff) now refer to EU Directive 1042/2013. As a consequence, the definition of real estate is no longer based on the Austrian Real Estate Transfer Tax Act. The new wording should not lead to any changes.

Furthermore, as of January 1, 2017, the judgement of the CJEU "Larentia + Minerva" shall be applied in Austria, i.e. partnerships can be VAT group members.

Last but not least, the Update 2016 incorporates current case law, e.g. on the principle of uniformity of services in connection with additional items in newspaper subscriptions (VwGH 27.5.2015, 2012/13/0029), on tax exemption for the conversion of Bitcoins (CJEU 22.10.2015, Rs C-264/14, Hedqvist), on the CJEU ruling Mapfre asistencia and Mapfre warranty for the provision of insurance (CJEU 16.7.2015, Rs C-584/13) as well as on invoices (VwGH 23.12.2015, 2012/13/0007; CJEU 15.9.2016, Rs C-416/14, Barlis 06).

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Energy tax refund: Possibility to apply for an adjustment of prior years?

Under Austrian tax law, both service providers and enterprises operating primarily in the manufacturing of goods were entitled to claim an energy tax rebate, until the Ancillary Budget Act 2011 excluded service providers and led to a less favourable calculation mechanism for production enterprises. However, in a case following the preliminary ruling by the European Court of Justice (ECJ), the Austrian Fiscal Court (BFG) Linz held that the amendment had not yet entered into force, meaning that an adjustment for the past might be possible. In this respect see also our contribution in ATN no. 54. Currently, an appeal lodged by the tax administration is pending before the Supreme Administrative Court.

The possibility of applying for an adjustment varies and depends on the client´s individual situation:

- Both service providers and production enterprises that have not submitted an application in the past can file one retrospectively for up to 5 years, meaning that an application for the fiscal year 2012 has to be filed until the end of 2017.
- Enterprises that have already applied for a refund and received an assessment notice may file an application to repeal the former assessment notice. This is only possible within one year after receipt of the assessment notice.
- For cases where an assessment notice was received and the one-year period has already elapsed, tax literature and case law provide arguments for a retroactive adjustment of the last five years. Since this question is under dispute, taxpayers might be required to defend their position in court.

Clients regularly applying for an energy tax refund are advised to closely monitor the proceedings.

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Cross-border active and passive leases between group-entities

In order to assess cross-border personnel leases correctly, it is essential to distinguish between passive and active leases. The Federal Ministry of Finance recently announced some guidelines thereon (EAS 3375).

Passive lease

If a passive lease is in place, an (economic) employer as per article 15, paragraph 2 of the OECD Model Tax Convention is constituted in the host state. This was confirmed by the Austrian Supreme Administrative Court (2009/13/0031).

In case of a passive lease, a personnel lease agreement is set up between the home company and the host company. The host company usually requests the assignment. The home company agrees that its personnel works on behalf of the host company, and the benefit of the assignees forms an integral part of the host company's business. It is not intended to provide an active service via the home company and is therefore considered a passive lease of the home company.

When an assignment qualifies as passive lease, the right to levy taxes on the employment income of the assignee is allocated to the host state as of day 1 of the assignment, irrespective if the assignee is present in the host state for a period exceeding 183 days. Presently there is no PE risk for the home company in general.

Active lease

An active lease is in place when the assignment is in the interest of the home company. An essential indicator of an active lease is that the home company remains having the instruction authority and supervision over the assignee.

If the assignment qualifies as an active lease and does not exceed 183 days, the right to levy taxes on the employment income of the assignee usually remains with the state of residence of the assignee. There is however a risk that a PE of the home company is created in the host state. We recommend to always analyse this as it impacts taxation rights.

Conclusion

To determine whether a passive or active lease is in place, each individual case should be assessed by taking into account the applicable facts and circumstances. If the employee is working for the benefit of the host company and the host company has the authority over the employee, these are usually indicators of a passive lease. If the benefit remains with the home company, an active lease seems to be in place.

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Austrian Tax Facts and Figures

Taxation of corporations

Corporate income tax rate (Basis – adjusted statutory accounts)	25%
Dividend withholding tax	27.5/ 25%
Witholding tax on licences/royalties	20%
Interest witholding tax	0%
Significant allowances	
Research & Development (R&D) (premium in cash)	12%

Non-deductible expenses (examples)	
Long-term accruals	3.5% per year
Interest and royalties paid to lowtaxed group companies	
Interest of debt-push down	
Tax loss carry forwards	
Losses may be carried forward for an indefinite period of time	
Usage of tax losses: 75% of taxable income	

Double taxation agreements
with 89 countries – mainly exemption method

International participation exemption for holding companies	
Conditions: Investments 10%, 1 year holding	
Dividends and Capital gains	0%
Dividend EC portfolio (shares) < 10%	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 tax cost
Foreign participations if EU-resident or third countries with comprehensive assistance agreement
Losses of foreign participations may be offset against profits of group leader up to 75%

Income in EUR	in 2017
0 to 11,000	0%
11,001 to 18,000	25%
18,001 to 31,000	35%
31,001 to 60,000	42%
60,001 to 90,000	48%
90,001 to 1,000,000	50%
above 1,000,000	55%

Social security on monthly earnings up to € 4,980			
Employer's share	up to 21.48%	Payroll related taxes	approx. 8.0%
Employee's share	up to 18.12%		
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 (Accommodation, art, cinema etc.)	13%
Reduced rate (Food, rent, public transportation etc.)	10%
VAT refund for foreign enterprises – available up to June 30 of the following year and for EU enterprises up to September 30 of the following year.	

Other taxes

Real estate transfer tax	0.5 – 3.5%
Stamp duties	
- Assignment agreements	0.8%
- Rent agreements	1.0%
- Suretyship agreements	1.0%

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We encourage feedback on the newsletter and the content. Equally, we welcome any of your thoughts on topics that you would like to see addressed in future issues.

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