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Abstract: This article aims to give an overview of the rules concerning taxation of companies in Sweden and of trends in the taxation of companies that have been evident in the last few years. It focuses in particular on issues that are connected with the so-called BEPS discussion, for instance interest deduction limitations, CFC rules, general anti-avoidance rules and other rules intended to protect the national tax base. It also sets out to describe other important features of the Swedish tax legislation in regard to companies, such as the rules on taxation of inbound and outbound dividends, interest and royalty.

1. Introduction to the Swedish corporate income tax

As a main rule, all income derived by an enterprise is taxable and all expenses relating to the carrying on of a business are deductible. Expenses are deductible and income taxable when the expense or income is recognized according to generally accepted accounting principles, unless there is a specific provision in the tax legislation that determines the time for recognizing the income or expense. However, some types of income are, under certain conditions, tax exempt and some expenses are non-deductible according to specific provisions in the tax legislation.

Swedish legal entities such as limited liability companies (Sw. *Aktiebolag*) are subject to corporate income tax at a single rate of 22 per cent. The international trend of tax base broadening combined with a lowering of the nominal tax rate has been evident in Sweden for some. This development took a huge leap with the tax reform of 1991, which meant that tax rates were drastically reduced and the base considerably broadened, and several more steps in that direction have been taken since then. In the last decade, the corporate tax rate has been lowered on two occasions. With effect from 1 January 2009, the tax rate was lowered from 28 per cent to 26.3 per cent. On 1 January 2013, the tax rate was reduced again, this time to 22 per cent. Recent efforts to broaden the tax base include interest deduction limitations, which were introduced in 2009 and extended in 2013 (see section 4.3 below).

Under certain conditions, profits of one company in a group can be set off against losses of another company in the group by means of so-called group contribution. A group contribution is basically a payment that is deductible for the paying company and taxable for the recipient, normally effectuated by means of recording a claim in the books of the recipient and a corresponding debt in the books of the payer when the annual accounts are prepared.

Losses can be carried forward indefinitely. In the event of a change of control of a company with losses carried forward, the losses may be subject to permanent or temporary limitations.

Companies are entitled to defer taxation of up to 25 per cent of their taxable income for a period of maximum six years. A notional income is computed on basis of the deferral to prevent the taxpayer from receiving an interest free tax credit. However, as a result of the deferral, income can be set off against losses arising in later years when the deferral is reversed, in effect creating a limited carry back of losses.

The most important deviation from the main rule that income is taxable and expenses deductible is that capital gains and dividends on shares in the corporate sector are typically tax exempt and that capital losses on such shares are typically non-deductible (see section 2.1 below). The reason for this deviation is to avoid double taxation or double deduction at the corporate level (e.g. that income earned by a subsidiary is subject to corporate tax at the level of the subsidiary and is taxed once more in connection with a distribution of the net profits to the parent company or that a loss is deductible for a subsidiary and deductible once more when the subsidiary is sold). Another important deviation is the interest deduction limitation rules, which mean that deduction of interest expense on loans to associated enterprises is denied, unless certain conditions are fulfilled.

In this context it can be noted that a proposal for a reform of the Swedish corporate tax was presented by the Committee on Corporate Income Taxation on 12 June 2014. The proposal is intended to enter into effect on 1 January 2016. According to the proposal, interest costs exceeding interest income ("net financial expense") will be non-deductible. Instead, all enterprises will be allowed a basic allowance of 25 per cent of the taxable income, so that only 75 per cent of the taxable income will be subject to the Swedish corporate tax of 22 per cent. In effect this means that the corporate tax rate for enterprises that do not have any net financial expense is lowered from 22 per cent to 16.5 per cent, whereas enterprises that according to the current rules can deduct net financial expense in excess of the basic allowance face an increase of the tax burden.[1]

2. Rules that act as incentives for establishment of companies

2.1. Participation exemption

Sweden does not have any specific holding company regime, but as mentioned above, capital gains and dividends on shares are typically exempt from tax. This follows from the Swedish rules on participation exemption in chapter 24 and chapter 25 a of the Swedish Income Tax Act of 1999 (Sw. *Inkomstskattelagen*, below referred to as "ITA"). Somewhat simplified, the tax exemption applies if the shares are held by a Swedish limited liability company and are:

A. unlisted, or
B. listed, and i) held for business reasons or represent at least 10 per cent of the company's voting rights, and ii) are held for at least one year before they are sold.

The tax exemption for unlisted shares does not require any holding period or any minimum per centage of the capital or votes.

As for shares held in foreign companies, the foreign company must correspond to a Swedish limited liability company in order for the participation exemption to apply.[2] According to case law, this is the case if the foreign company is liable to tax (no minimum level of taxation of the foreign company seems to be required) and if the foreign company law is reasonably similar to the Swedish regulation in respect of limited liability companies, for instance in regard to limited liability of the owners.[3]

1 For more information on the proposal by the Committee on Corporate Income Taxation, see David Kleist & Pernilla Rendahl, Swedish Tax news, in this issue.

2 According to ch. 2 sec. 2 ITA, terms and expressions in ITA comprise corresponding foreign notions unless the provision in question specifically points out that it only refers Swedish notions.

3 See for instance the court case RÅ 2009 ref. 100.

Capital losses on the above mentioned categories of shares are not deductible.

The capital gains tax exemption applies also to shares that are attributable to a permanent establishment in Sweden and held by foreign companies resident within the European Economic Area.

Special rules apply to a sale of shares in companies where the value of cash and other liquid assets exceeds 50 per cent of the consideration for the shares. The seller may be taxed on the gross receipts of such a sale. This special taxation can, however, be avoided by filing a special tax return and by the fulfilment of certain other formalities. It can be noted that these rules do not apply to the disposal of shares in a foreign company, provided that the foreign company does not have a permanent establishment in Sweden and does not hold shares in companies that are liable to tax in Sweden.

2.2. Taxation of interest, dividends and royalties paid to non-resident taxpayers

2.2.1. Interest

There is no Swedish withholding tax on interest paid to non-resident lenders. This means that interest can be paid to a non-resident lender without taxation in Sweden regardless of whether the lender is resident outside the European Economic Area or even resident in a low tax jurisdiction.

2.2.2. Dividends

According to the Withholding Tax Act of 1970 (Sw. *Kupongskattelagen*), dividends distributed to non-resident shareholders are subject to withholding tax at a rate of 30 per cent. However, generous exemptions apply in respect of corporate shareholders, meaning that dividends paid to non-resident corporate shareholders are typically exempt from withholding tax. The exemptions are not limited to those stated in Council Directive 2011/96/EU (the "Parent-Subsidiary Directive"), but apply also for instance in relation to corporate shareholders outside the European Economic Area and to corporate shareholders holding less than 10 per cent of the shares in an unlisted Swedish limited liability company.

According to the Withholding Tax Act, dividends received by a foreign company are exempt from withholding tax under the following conditions:

A) For unlisted shares:
   i) The holder is subject to taxation similar to that applying to Swedish limited liability companies or is covered by a double tax treaty, and

    - ii) the holder is deemed as corresponding to a Swedish limited liability company, a Swedish co-operative economic association (Sw. *Ekonomisk Förening*) or a Swedish foundation (Sw. *Stiftelse*) which is not exempt from tax.
- B) For listed shares:
    - i) The holder is subject to taxation similar to that applying to Swedish limited liability companies or is covered by a double tax treaty,
    - ii) the holder is deemed to correspond to a Swedish limited liability company, a Swedish co-operative economic association or a Swedish foundation which is not exempt from tax,
    - iii) the shareholding represents at least 10 per cent of the distributing company's voting rights, and
    - iv) the shares have been held for at least one year.

In addition, an exemption under the Withholding Tax Act also applies in respect of companies covered by the Parent-Subsidiary Directive that hold at least 10 per cent of the shares in a Swedish limited liability company.

2.2.3. Royalties and other payments for the use of assets

Under Swedish domestic law, consideration for the use of tangible or intangible assets – for instance royalty and lease payments – paid to a non-resident taxpayer is as a main rule taxable in Sweden.[4] However, Sweden does not apply a withholding tax on the gross amount. Instead, the foreign company is taxed as if the payments were attributable to a permanent establishment of the foreign company in Sweden. This means that the foreign company is taxed on its net income, i.e. the royalty or lease income is regarded as income attributable to a permanent establishment and expenses connected with the income is deductible. This means for instance that under a back-to-back structure only a profit margin determined according to the arm's length principle is taxable in Sweden as outgoing royalty or lease payments made by the non-resident taxpayer would in principle be deductible.

Subject to certain conditions, royalty and lease payments made to associated enterprises within the EU are exempted under Swedish domestic law due to the implementation of Council Directive 2003/49/EC (the »I + R Directive").[5] One condition is that the non-resident taxpayer is a company which is covered by the I + R Directive. The exemption only applies if the non-resident taxpayer re-

4 Ch. 6 sec. 11 para. 2 ITA.
5 Ch. 6 a ITA.

ceives the royalty or lease payments on its own behalf (Sw. "*för egen del*", the English version of the I + R Directive uses the expression »beneficial owner").

2.2.4. *Reduced rates under double tax treaties*

Even if the exemptions under Swedish domestic law for outbound dividends, royalty and leasing payments would not be applicable, a reduced rate or total tax exemption may apply on the basis of provisions in a double tax treaty that Sweden has entered into with the state in question.

Sweden has an extensive treaty network, comprising around 80 comprehensive double tax treaties and a number of partial double tax treaties.[6] With some minor exceptions, Swedish double tax treaties generally conform to the articles of the OECD convention.

2.2.5. *Summary*

To sum up, Sweden does not have any specific regime for holding companies. However, the general rules on taxation of inbound and outbound dividends and interest as well as the rules on taxation of capital gains on shares means that Swedish limited liability companies have some important attributes for serving as holding companies. Moreover, Sweden has an extensive network of double tax treaties. However, Sweden has not established itself as a holding company location in the same was as some other jurisdictions, such as the Netherlands, that introduced participation exemption rules several years ahead of Sweden.

3. Rules intended as incentives for investment

3.1. Accelerated depreciation

According to chapter 18 ITA, the depreciation of machinery and equipment is 30 per cent of the aggregate book value of all such assets at the beginning of the year. Should a straight-line depreciation of 20 per cent per annum of all such assets result in a lower book value in any year, the depreciation may be increased accordingly. The same rules apply to intangible assets that have been acquired from another person. The acquisition value of machinery and equipment acquired for less than half the basic amount for national social security purposes (i.e. in 2014 acquired for less than SEK 22,200) or expected to have

6 According to Claes Hammarstedt and Eveliina Kiviniemi, Konkurrenskraften i Sveriges skatteavtal, Svenskt Näringsliv 2010, pp. 8-9, in 2010 there were 81 signed comprehensive double tax treaties in place.

an economic life of no more than three years can be deducted immediately. Assets that can be assumed to have a lasting value, for instance works of art, cannot be depreciated at all.

This means that machinery and equipment as well as intangible assets acquired from another person can generally be depreciated within a five year period, regardless of whether the economic life of the assets is longer.

Expenses relating to construction and reconstruction of a building shall typically be included in the acquisition value of the building and depreciated using as straight-line depreciation of 2-5 per cent per annum, depending on the use of the building. However, expenses for reconstruction may be deducted immediately if they can be considered normal for the business conducted by the taxpayer, provided that they do not constitute a material change of the building. For instance, adjustments of premises in connection with a change of tenant can typically be deducted immediately.

3.2. Investment deduction

In order to improve the access to capital for small sized enterprises, a deduction for investment in shares in Swedish limited liability companies, Swedish co-operative associations and corresponding foreign entities has been introduced in chapter 43 ITA. Individuals are allowed to deduct from their income from capital an amount corresponding to half the investment amount, but there is a cap of SEK 650,000. As the tax rate on income from capital is 30 per cent, the potential tax saving is 15 per cent of the investment amount, but due to the cap the tax saving is at most SEK 195,000. The investment shall be made in connection with the formation of the enterprise or in connection with a new share issue. Certain other requirements also apply.

4. Specific anti-tax avoidance rules

4.1. Transfer pricing rules

The Swedish rule on cross-border transfer pricing has been essentially unchanged since the 1960s. The rule provides that if the income of a Swedish enterprise, due to the fact that the enterprise has entered in an agreement with another enterprise on other than arm's length terms, is lower than would otherwise be the case, then the income shall be computed as if those terms did not exist, provided that (i) the contracting party is not liable to tax in Sweden, (ii) it can be assumed that the enterprises are associated, and (iii) it does not follow from the circumstances of the case that the terms have been agreed on due to other reasons than the fact that the enterprises are associated.[7]

In accordance with the international trend in this field, the focus of the legislator in recent year has been on documentation requirements.[8]

A number of transfer pricing disputes have been decided by courts in the last few years. Many of them have concerned deduction of interest by Swedish enterprises in private equity fund structures and in particular the question whether the interest rates on shareholder loans to Swedish enterprises have exceeded the arm's length rate.[9]

4.2. Exit taxes

Taxation is triggered when an asset is no longer subject to Swedish corporate tax. This may for instance be the case when Sweden enters into a new double tax treaty, when an asset is transferred from Sweden to another country or when the owner of an asset changes his state of residence for treaty purposes from Sweden to another state, if this means that Sweden's taxing right ceases, either according to Swedish domestic law or because the relevant double tax treaty precludes Sweden from taxing income relating to the asset. In such case, the taxable income of the owner shall be computed as if the asset had been sold at market value.[10]

However, if taxation takes place as a result of Sweden being precluded from taxing income relating to an asset because of a double tax treaty with another state in the European Economic Area, the taxpayer is eligible for a respite on the tax payment. Respite is received one year at a time.[11]

4.3. Interest deduction limitations

Sweden has no thin capitalisation rules. Until 1 January 2009 Swedish tax legislation did not provide for any limitations to the deduction of interest expense as long as the interest rate was determined on an arm's length basis.

However, that all changed on 1 January 2009 when interest deduction limitations applicable to loans between associated enterprises

7 Ch. 14 sec 19 ITA.

8 See e.g. Mikael Hall and Olov Persson, Svensk Skattetidning 2007, Dokumentationsskyldighet avseende internprissättning, No. 2, pp. 147-156.

9 See e.g. case No. 3684-3686-11 from the Administrative Court of Appeal in Stockholm.

10 Ch. 22 sec. 5 items 2, 4 and 5 ITA.

11 Ch. 63 sec. 14 of the Swedish Tax Procedural Act of 2011 (Sw. skatteförfarandelagen).

were introduced. Furthermore, the interest deduction limitations were given a significantly wider scope on 1 January 2013 when the legislation was once again amended. The previous interest deduction limitations targeted loans between associated enterprises relating to the financing of an intra-group acquisition of shares. The new limitations apply to any loans between associated enterprises. Furthermore, the previously applicable "safe haven" which allowed deduction of interest when the beneficial owner of the interest income was subject to at least 10 per cent tax, has been modified so that deduction, under certain circumstances, can be denied even if the 10 per cent condition is fulfilled.[12]

Under the new interest deduction limitation rules, interest expense on loans between associated enterprises is as a main rule non-deductible unless the person who is actually entitled to the income is subject to at least 10 per cent tax. According to the preparatory works, the phrase "actually entitled to the income" shall correspond to the expression "beneficial owner".[13] Furthermore, even if the beneficial owner is subject to 10 per cent tax or more, deduction may be denied if the main reason for the loan is to gain a substantial tax benefit.

The 10 per cent requirement looks at the tax that would have applied if the interest income were the only income of the beneficial owner of the interest. Other income and losses from the operations of the beneficial owner are disregarded. However, if deductions can be made which would not have been available in Sweden, for instance basic allowances or notional interest deduction, that is taken into account for the purpose of determining the tax rate that applies to the interest income.

Moreover, regardless of the 10 per cent requirement, interest may be deducted if the beneficial owner of the interest is resident in the European Economic Area or in a state with which Sweden has entered into a comprehensive double tax treaty, provided that the borrower can prove that the loan is essentially motivated on commercial grounds. For the purpose of determining whether there are sufficient commercial grounds for the loan, the rules state that it should be taken into account whether the financing could have been made in the form of a contribution instead of a loan.

The rules also contain several anti-avoidance provisions. For instance interest on back-to-back loans via an external party may be

12 The interest deduction limitations are found in ch. 24 secs. 10 a - 10 f ITA. For a description of the interest deduction limitations, see e.g. Lars Samuelsson, Regeringens slutliga förslag om effektivare ränteavdragsbegränsningar, Skattenytt 2012, No. 12, pp. 820-830.

13 Government Bill 2008/09:65, p. 61.

non-deductible even though such interest does not fall within the scope of the main rule as the external party is not an associated enterprise.

However, it can be noted that there is no specific restriction on deduction of interest on loans relating to tax exempt investments. This means that interest costs relating to financing of an acquisition of shares in a company can typically be deducted (assuming that the interest deduction limitations do not apply), regardless of whether a sale of the shares would give rise to any taxable income. Such deduction can be set off against the profits of an acquired enterprise according to the rules on so-called group contribution.

4.4. The concept of beneficial owner and treaty shopping

Swedish double tax treaties conform to the OECD model in most respects and consequently typically require that the beneficial owner of outbound dividends, interest and royalty is a resident of the other state in order for the limitations on Sweden's taxing rights as a source state to apply. However, the beneficial owner concept is unknown to the Swedish legal system and very few cases dealing with that concept have been decided.[14]

Furthermore, in Sweden the beneficial owner requirement of tax treaties is likely to play a less prominent role than in many other states. This is due to the fact that Sweden does not impose tax on interest paid to non-resident lenders and that exemptions from withholding tax on dividends typically apply under Swedish domestic legislation when dividends are paid to a foreign company (see sections 2.2.1 and 2.2.2 above), regardless of whether that company is beneficial owner of the dividends. Moreover, in regard to royalty paid to non-resident taxpayers, Sweden does not impose a withholding tax on the gross amount (see section 2.2.3 above). Instead, the non-resident taxpayer is taxed as if the payments were attributable to a permanent establishment in Sweden. This means that the non-resident taxpayer is taxed on its net income, i.e. the royalty income is regarded as income attributable to a permanent establishment and expenses connected with the income are deductible. Under for instance a back-to-back structure only a profit margin determined according to the

14 See case No. 1772-11 from the Administrative Court of Appeal in Sundsvall. Furthermore, see HFD 2012 not. 24 from the Swedish Supreme Administrative Court regarding the interpretation of the expression "actually entitled to the income" in the Swedish interest deduction limitation rules, which according to the preparatory works shall correspond to the expression beneficial owner. The case is commented on in David Kleist, First Swedish Case on Beneficial Owner, Intertax 2013, No. 3, pp. 159-163.

arm's length principle would be taxable in Sweden as outgoing royalty payments are in principle deductible. In other words, due to Swedish domestic law there is less need for relying on tax treaty benefits in respect of dividends, interest and royalty than in many other states, meaning that there is less need to determine whether the beneficial owner of the income is a resident of a contracting state.[15]

4.5. CFC legislation

In order to discourage the use of legal entities in low tax jurisdictions for tax planning purposes, the so-called CFC rules in chapter 39 a ITA provide that a resident shareholder that holds an interest in a "controlled foreign company" (CFC) is in certain cases subject to Swedish corporate tax on its portion of the profits of the CFC entity. In other words, the foreign entity is treated as transparent for tax purposes. The Swedish CFC rules were introduced in 1990 and have been amended on several occasions, one of the most important amendments being that the rules since 2004 apply to direct as well as indirect ownership of low taxed foreign companies.[16]

The CFC rules apply to direct or indirect holdings of at least 25 per cent (capital or voting rights) of low taxed foreign companies. A foreign company is deemed to be low taxed if the foreign tax is less than 55 per cent of the tax that would have been imposed if the foreign entity had been a Swedish limited liability company, i.e. it is deemed low taxed if it is subject to a tax rate of less than 12.1 per cent, assuming that the taxable income according to the foreign tax legislation equals the taxable income under Swedish law.

A general exemption from CFC taxation applies to companies in countries on a special "white list", with the exception of certain businesses in some cases.

Examples of countries not included on the white list are the Channel Islands, Isle of Man and Liechtenstein. Notable exceptions of businesses that may be subject to CFC taxation even if the country is on the white list is banking, financial and insurance business (Switzerland), intra group banking, financing and insurance business (Ireland) and intra group captive insurance (Luxembourg).

4.6. General anti-avoidance rules

Swedish tax legislation contains general anti-avoidance rules in the Anti-Avoidance Act of 1995 (sw. *lagen mot skatteflykt*), which applies

15 David Kleist, Begreppet beneficial owner och dess relevans i svensk skatterätt, Svensk Skattetidning 2013, No. 1, pp. 34-59

16 For a description of the Swedish CFC rules, see Mattias Dahlberg, Internationell beskattning, Studentlitteratur 2012, pp. 185-213.

for the purpose of determining the taxable income of a taxpayer. The Anti-Avoidance Act is applicable if (i) the action taken by the taxpayer (or contributed to by the taxpayer) is part of a scheme that results in a material tax saving for the taxpayer, (ii) the tax saving can, based on the circumstances, be assumed to have constituted the main reason for the scheme, and (iii) determining the taxable income on basis of the scheme would be contrary to the intent of the legislation, determined on basis of the general design of the tax legislation and on the specific provisions that have been circumvented by means of the scheme.

If the law is deemed applicable, the taxable income shall primarily be determined as if the actions in question had not been taken, but alternative ways of determining the income also exist, which means that it can be difficult for a taxpayer to predict the outcome of application of the Anti-Avoidance Act.

In addition, although no clearly formulated anti-avoidance rule has developed in case law, there is also a case law based general anti-avoidance doctrine. However, in recent years there seems to have been a shift from to use of case law based anti-avoidance to statutory anti-avoidance, as the Anti-Avoidance Act has been deemed applicable in a number of rulings by the Swedish Supreme Administrative Court in recent years.

The Anti-Avoidance Act contains several vague criteria. Furthermore, the application of the Anti-Avoidance Act presupposes that an intent different from that which follows from the text of the Income Tax Act can be determined. As a consequence, there has been a debate going on since the introduction of the Anti-Avoidance Act as regards the inadequate foreseeability in the application of the provisions of the Anti-Avoidance Act.[17]

5. Exchange of information

In recent years, Sweden has entered into information exchange agreements with a number of low tax jurisdictions such as Liechtenstein, Bahamas and Monaco. Furthermore, information exchange clauses have been included in double tax treaties with several states

17 See e.g. Mats Tjernberg & John Neway Herrman, Regeringsrätten och skatteflyktslagen – mönster eller monster? Skattenytt 2011, No. 3, pp. 158-167.

known for bank secrecy, most notably in the double tax treaty with Switzerland.[18]

The discussion in Sweden so far has mainly been focused on the exchange of information relating to individuals, and the increased pressure on individuals to freely provide information to the Swedish Tax Agency in order to avoid prosecution and tax surcharges created by the new means of obtaining information from tax authorities in other states. The relevance for protecting the Swedish corporate tax base of the increased opportunities of exchanging information remains to be seen.

18 For an account of the development in the area of exchange of information, see Ulrika Gustafsson Myslinski, *Den senaste utvecklingen på informationsutbytesområdet*, Svensk Skattetidning 2010, No. 3, pp. 290-307. In regard to the double tax treaty with Switzerland, see Christina Svanhagen, *Ändringar i skatteavtalet med Schweiz*, Svensk Skattetidning 2012, No. 8, pp. 644-657.