

Article

Robert Pålsson*

The taxpayer's intentions: Subjective prerequisites in tax law**

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Abstract: Tax legislation contains references to taxpayer's intentions with their transactions. The acquisition or sale of an asset may be treated differently, for example, depending on the purpose of the person holding it. This article contains a discussion of the concept of subjective prerequisites, with particular emphasis on the role they can play in tax law. How the terms *intention* and *purpose* are actually used in the Swedish Income Tax Act (ITA) is also explored.

Keywords: Income tax; Swedish income tax; legislative technique; subjectivity; subjective prerequisites

1 Introduction

1.1 Purpose of the article

The purpose of this article is to investigate the concept of subjective prerequisites from a tax law perspective. First, I discuss the notion of subjective prerequisites, with particular emphasis on the role they can play in tax law. Secondly, I investigate ways in which the terms *intention* and *purpose* are actually used in the Swedish Income Tax Act (ITA).¹ These two terms may represent, but do not necessarily represent, subjectively oriented concepts that refer to the personal circumstances of the taxpayer. This article is one in a series of studies on the technique of statutory

tax legislation that has been published in Sweden in recent years (e.g., Hultqvist *et al.* 2014).

1.2 To investigate tax legislation technique

This study is conducted from a Swedish tax law perspective. This means, that it is the Swedish discourse and regulations that set the scope and serve as a point of departure for my investigation. The principles and technical methods used in the statutory tax law can be investigated in several ways. For example, in Swedish research it is relatively common for systematics and disposition to be used as starting points and for evaluation. More language-oriented analyses is another option. (See, e.g., Wahlgren 2014.) Indeed, the legislative technique has been treated extensively (see, e.g., Alhager 1999; Endicott 2000; Hellner 1991; Moëll 2003; Strömholm 1996; Wahlgren 2014, also Wintgens 2002, 2005, in which a large number of other references can be found).

Regardless of the approach chosen, the common method of jurisprudence in Sweden implies that statements in preparatory works and case law are aligned with the legal text, partly in order to determine the current law, but mainly to check consistency and likely achievement of legislative goals.² Analyses of this type are particularly important in all the Nordic tax systems, which depend largely on statutory law and rely on such principles as the legality principle for safeguarding taxpayers' rights.

It is also common to investigate the compatibility of legislation with the Swedish constitutional principle of legality that it is expected to rest upon. More social-science-oriented analyses can of course be made, for example, by identifying the latent norms and ideologies involved in the gender aspects of statutory tax law.

*Corresponding Author: Robert Pålsson: Professor of Tax Law, School of Business, Economics and Law, University of Gothenburg, Sweden; Email: robert.pahlsson@law.gu.se

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1 References to statutory law refer to the Income Tax Act (ITA) (Swed. inkomstskattelagen 1999: 1229), unless otherwise stated.

2 It must be underlined here that preparatory works, such as motivations contained in Government bills, are considered important sources of law in the Nordic legal systems, especially in Sweden.

1.3 General about the accuracy of tax provisions

It is a truism that accuracy in statutory law is important. Precision facilitates common understanding. Thus, it can be expected to enhance efficiency as well as legal certainty. In a constitutional perspective, a certain measure of precision is necessary for the legality principle to be met (Hultqvist 2015, 2016).

In studies of tax legislation, there is a reason to pay attention to and problematize the difference between two extremes on an imaginary scale. At one end are the standard assessments and at the other end are particularly vague prerequisites. Standard assessments are quantifications and calculation models that simply replace reality, and thus produce estimates that allow taxation, for example, calculating the value of a company car for tax purposes.³ The Swedish ITA contains a number of such templates, and they deserve a separate investigation.

At the other end of the imaginary precision scale, we find such vague expressions as *business purpose* and the *de facto* delegation for discretionary exemptions, decided by the tax administration. Discretionary exemptions have been subjected to investigation in a Swedish dissertation, whereas the concept of business purpose has been treated in at least one recent article (Alhager 1999; Hultqvist 2012). Indeed, this *de facto* shift of power from the legislature to the courts and tax administration underlines the need for further investigation.

A conceptually different type of solution, which is also representative of particularly vague legislative techniques, are the subjective prerequisites that seemingly refer to the will or ambition of the taxpayer. In this article, I have chosen to investigate the use of the terms' intention and purpose in the ITA.

2 Outline of the study

The objective of a reference in the ITA to the taxpayer's intent or purpose may be, but does not have to be, that the taxpayer's reason for conducting a transaction is of importance in deciding how the transaction should be treated when tax law is applied. As I demonstrate, it is also possible to use these terms in other contexts.

This survey is conducted in three steps. First, I provide a general discussion about the nature of subjective prerequisites. In Step 2, I present an inventory of the occurrence of certain expressions in the ITA. The inventory shows a large number of references to purpose and intent. The idea of the inventory is partly to show the large number of potentially subjective prerequisites that can be found in the ITA, but mainly to enable identification of prerequisites that are particularly suitable for further analysis.

Based on the inventory, Step 3 is a selection of references that raise the question of whether the law refers to the taxpayer's will, and how this may be determined. Subsequently, I clarify the extent to which these references constitute subjective prerequisites.

3 The character of the subjective prerequisite

3.1 Defining the concept

For the purpose of this study, it is not necessary to construct a clinically sharp definition of the concept of subjective prerequisites. Therefore, this article does not present an extensive investigation of the use of the term in literature. Such an investigation would take up much space, and it would probably show that the terminology on subjective and objective prerequisites is rather inconsistent.

But it is, however, necessary to pinpoint the phenomenon with satisfactory precision. The term *subjective prerequisite* refers here to legal descriptions that aim at such personal circumstances of a subject as will and ambition. Specifically, I analyze the terms purpose and intention as possible subjective prerequisites.⁴

There may of course be other subjective prerequisites than those I have chosen to investigate here. One possible example is the use of the term *business purpose* in the controversial Swedish restrictions on interest deductions.⁵ Although the commercial practice obviously requires an objectively oriented analysis, the taxpayer's reasons appear as a reference to personal grounds for a transaction or other choice of activity. The concept of business purpose, however, falls outside the article's scope. (See instead, e.g., Hultqvist 2012.)

³ See the Swedish *Inkomstskattelagen* (IL) (Income Tax Act (ITA) Ch. 61 Sec. 5 (Swed.).

⁴ Swed. *syfte*, *ändamål* and *avsikt*, including certain forms of them.

⁵ See the Swedish *Inkomstskattelagen* (IL) (Income Tax Act (ITA) Ch. 24 Sec. 10 a – 10 e (Swed.).

It also deserves mention that subjectively oriented descriptions exist in the EU law, such as the directive on parent companies and subsidiaries and the Anti-Tax Avoidance Directive (ATAD).⁶ In addition, a test of "principal purpose" is part of the multilateral instrument, based on the Base Erosion Profit Shifting (BEPS) Action Plan 15, which has been prepared for ratification (Kleist 2016).⁷

3.2 Subjective prerequisites in other fields of law

It should be emphasized that subjective prerequisites in tax law should not be regarded as having the same meaning as subjective prerequisites in criminal law, where the term originated. The notion of criminal intent has been highly developed in criminal law. When examining the fundamental requirement of criminal intent, the aim is to assess what went on in the perpetrator's head. In principle, the Swedish criminal law concept of intent comprises direct intent, insight, and indifference (*e.g.*, Asp *et al.* 2013).

In his dissertation, Christer Silfverberg (1992) describes in detail how the approach in gift tax law can be traced to the concept of civil law. Furthermore, observations on the significance of subjective prerequisites can also be found in accounting law literature (Kellgren 2016).

In Swedish law, it is well known that a completed gift is considered to presuppose the intention of the donor to enrich the recipient at the donor's own expense. Gradually, however, an approach developed by which a gift was considered to exist if the circumstances that marked the gift would, to an external viewer, appear to be an act of generosity. The evolution of law thus went from the notion of a purely subjective prerequisite to a conception according to which the transferee's intentions were assessed from objective starting points (Silfverberg 1992). This illustrates the "objectification" of the subjective prerequisite of

tax law, and rendering difficult a comparison with criminal law.

There are several judgments in Swedish gift tax practice that show an approach whereby the gift concept is constructed with presumptions, and based on objective criteria (Silfverberg 1992).⁸ The analysis is complicated, however, by the fact that the Supreme Court sometimes has used a language that reveals the conception that the court is dealing with "real", individually based subjective prerequisites. The court explains, for example, that "it must have been clear" to the donor that the transaction in question would entail a certain transfer of wealth. This reference forms part of the *ratio decidendi*, and illustrates the subtle difference between "real" subjective facts and those facts the existence of which is determined on objective grounds (Grosskopf 1981; Silfverberg 1992).⁹

The idea that subjective legal facts should be observed with objective methods may also be found in accounting law, for example, with references such as *management intent*. A reasonable assumption, however, is that this term does not represent a free choice for the management. Instead, it is likely that such intentions, in order to appear reasonable, must be seen in a context. This context can be based, for example, on the company's business plan, business model, results and position, depending on the current question (Bokföringsnämnden 2012; EFRAG 2013).

3.3 The subjective prerequisite in the Tax Avoidance Act

At first glance, it may be assumed that the notion of objectivity that has come to characterize the perception of the gift concept in Swedish law also characterizes the view toward subjective prerequisites in general in tax law. But although this is undoubtedly a common view among tax lawyers, it is far from sure, and is one of the questions investigated in this paper. In principle, this view means

⁶ See Council Directive (EU) 2015/121 of 27 January 2015 amending Directive 2011/96/EU on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, and Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.

⁷ BEPS—Base Erosion Profit Shifting—is an extensive OECD project aimed at stabilizing tax bases. An agreement on The Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting was reached in November 2016. The formal signing is expected to take place during 2017.

⁸ See, for example, *Högsta Domstolen* (HD) (Supreme Court) NJA 1944 s. 10, NJA 1980 s. 642, where the court identified a relevant gift intention directed towards a limited company in which the donor owned shares. The ruling has since then, and up to October 28th 2016 formed the basis for systematic tax planning for real estate transactions and was recently confirmed by *Högsta Förvaltningsdomstolen* (HFD) (Supreme Administrative Court) HFD 2015 ref. 48, although the Supreme Court changed its practice in NJA 2013 s. 886. However, this tax planning technique is no longer possible, as the legislature issued a notice on the forthcoming legislation to be given retroactive effect on October 28th, 2016.

⁹ See *Högsta Domstolen* (HD) (Supreme Court) NJA 1980 s. 642 I.

that, in order to determine the taxpayer's intention, the economic impact of the business transactions in question must be analyzed, along with any other objectively observable consequences of the transactions.

This method is particularly clear in the application of tax avoidance rules. The third provision in Sec. 2 of the Tax Avoidance Act requires that the tax benefit arising from the taxpayer's activities can be assumed to be the dominant reason for the procedure. At the latest amendment to the law, which was implemented in 1998, the requirement was changed from the "main" reason to the "dominating" reason.¹⁰ With the amendment, the legislature wished to underline the fact that the law could be applied even if the legal actions were taken partly for commercial reasons.¹¹

It follows from statements in the preparatory works that the subjective prerequisite in the Tax Avoidance Act is meant to be applied objectively. The emphasis is on the intention of the taxpayer as would be perceived by an outside viewer (Rosander 2007).¹² The provision is not usually considered problematic by the Supreme Administrative Court (SAC).

For example, if a transaction or series of transactions does not have any other consequences than a reduction of the taxpayer's tax in relation to what would have been the case if the transactions were not made, the taxpayer's purpose for the transactions is assumed to be tax avoidance. The assessment may also contain a comparison of the business transaction in question with other transactions that are perceived as being closer to normal.

The assessment is done without attempting to investigate what the individual in question actually knew or thought, and it is therefore perceived not as a test of subjective circumstances, but of objectively observable factors. On the other hand, it follows from the wording that knowledge or assumptions about the taxpayer's individual ambitions and insights are allowed to change the assessment, if they become known. I contend, however, that a tax-driven purpose is often presumed in cases in which tax avoidance laws are applied, and therefore such individual aspects are not usually examined.

3.4 Tentative conclusion

In summary, and in principle, we can distinguish between (1) subjective prerequisites, the presence of which

is judged, preferably, on subjective grounds (based, for example, on what the taxpayers state about motives) or on assumptions about how this person thought or felt; and (2) subjective prerequisites, the presence of which is assessed, preferably, on objective grounds (based, for example, on observations of how a person acted) possibly in comparison to a perceived normal standard.

Both possibilities are considered in the following analysis. I also take into consideration the possibility that there may be degree differences in specific situations.

3.5 The problem of comparison standard

In order to determine the taxpayer's intentions on objective grounds, it may be necessary to make a comparison with the hypothetical actions of a person who did not have a tax benefit as an essential purpose. This comparison resembles how one is forced to think within the law of torts, to determine if someone has been negligent. A logical prerequisite for these operations is the availability of a kind of ideal person.

It is hardly surprising that tax lawyers try to determine the taxpayer's purpose based on how things appear in the eyes of an outside viewer. The question, rather, is if there really is another way to do it. If, for example, it is actually clarified that an individual's purpose with a transaction was A, but the circumstances viewed from the outside indicate that the purpose was B, then how should the circumstances be assessed? Note that because there is no disagreement about what is proven, this question is actually a matter of law and not a question of the facts.

4 Inventory of subjective prerequisites in the ITA

4.1 Introduction with delimitations

This inventory constitutes the second step of the survey. References are made to provisions where the keywords occur, along with brief descriptions of the rules. The provisions selected for further investigation are described in greater detail in Section 5 of this paper.

Please note that the inventory of subjective prerequisites is not intended to be exhaustive, but is based on a selection of keywords, which, in turn, rests on the following delimitation. Note also that I have placed the complete inventory in an appendix to the article.

¹⁰ Swed. *huvudsaklig* and *överbäggande* respectively.

¹¹ See Proposition (Prop.) 1996/97:170 p. 43 (Swed. Government bill).

¹² See Proposition (Prop.) 1982/83:84 p. 18 (Swed. Government bill).

I have omitted references to the keywords where the context clearly shows that they cannot reasonably represent subjective prerequisites—where they do not appear to relate to the circumstances of the taxpayer or any other subject, for example, in municipal income tax for municipal purposes in Ch. 1 Sec. 4, Para. 2.¹³ Another example is a so-called single land/plot business, which is considered commenced upon the sale of the fifth plot in accordance with Ch. 27 Sec. 15. In addition, rules in which a subjective prerequisite may be presupposed also fall outside the scope of the article, the most obvious example, perhaps, being Ch. 13 Sec. 1 Para 1. Under this rule, business income is defined as commercial activities that are conducted 'professionally and independently'. According to case law, this expression contains a demand for the purpose of profit (Påhlsson 2014).¹⁴

4.2 Specification of the keywords used in this study

As previously mentioned, the keywords used in the inventory correspond to the English words intention and purpose. The variations applied in the search correspond to *intention, intends, intended, intended for, purpose, and profit purpose*.¹⁵ To the extent that the terms together can be said to form a single subjective prerequisite, I will, of course, treat them in context and only once. An example is the expression *intended for another purpose*, in Ch. 19 Sec. 10.

The total number of hits in the ITA on the keywords is 317.

It is clear that the keywords often occur without reference to the circumstances of the taxpayer or others. In such cases, it is normally obvious, from a Swedish language perspective, that they cannot implicate a subjective prerequisite. The clearest example corresponds to the expression *intended for*, with 201 hits in the ITA (including regulations on special entry-into-force rules). In almost all of these 201 hits, the term simply refers to an object, an asset, or a particular income. Such hits have not been included in the inventory.

However, this demarcation is not always obvious. If the legal text attaches particular importance to whether a building is intended for residential purposes, for example,

it can be said that this ultimately relates to the purpose of a subject. But at the same time, it is obvious that the prerequisite aims at an objectively identifiable circumstance regarding the character of the building.¹⁶

As far as possible, therefore, I left out these kinds of references and sought to concentrate the inventory on prerequisites that could really be interpreted as subjective on the taxpayer's side (*i.e.*, prerequisites that actually give the impression of referring to what the taxpayers may have thought, liked, or meant with their dispositions).

Because the limitations are based on my own choices, the inventory should not be considered exhaustive. The number of hits that remain, however, when I have made my selection so large that an interesting analysis can be made of such expressions in the text that could be perceived as references to the taxpayer's subjective will.

4.3 The use of subjective prerequisites in different areas of income taxation

My goal in this study is to analyze the extent to which certain expressions in the ITA do in fact respond to subjective circumstances related to the taxpayer. To obtain an overview of the places identified in the ITA and to facilitate comparisons, the following subdivisions may be motivated. As previously mentioned, the complete inventory is placed in an appendix.

I have made the following three types of observations that I consider might be of interest to further investigators. It may be noted that references are made with respect to purpose and intention of (1) natural persons and taxpayers who are legal. Furthermore, it is clear that references are made (2) within the framework of rules that are applicable to all three income types. Under the ITA, there are three income schedules (*i.e.*, earned income, business income, and capital income, Påhlsson 2014). Finally, (3) it appears that the references are aimed at contributions, acquisitions, and income-generating activities made by the taxpayer or another person.

The places in the ITA that were identified in the inventory (see appendix) may thus be categorized in the following way:

Legal person 14

Natural person 13

¹³ Hereafter all references to statutory law refer to the Swedish Income tax Act (ITA) unless otherwise stated.

¹⁴ See also, *e.g.*, Ch. 44 Sec. 9.

¹⁵ Swed. *syfte, vinstsyfte, syftar, avsikt, avser, avsett, avsedd, avsedda* och *ändamål*.

¹⁶ The regulation regarding the fixed asset-building inventory (Swed. byggnadsinventarier) in Ch. 19 Sec. 7 serves as an example. I have, however, included the rule in Ch. 20 Sec. 8 on immediate deduction for assets intended for use during a limited number of years.

Both legal and natural person 3
 Earned income 3
 Business income 23
 Capital income 3
 Business and capital income 1
 Capital contribution 6
 Acquisition 5
 Income-generating activities 19

It can thus be concluded that the references to purpose and intention identified in this study have considerable, albeit uneven spread with regard to the type of taxpayer, income type, and activity. However, references related to business dominate.

5 Analysis of a selection of potential subjective prerequisites

5.1 Selection method

In the previous section, I made a substantially quantitative classification in objectively defined legal categories (e.g., legal/natural person, income types, etc.). This provided an overview of what can be categorized as potential subjective prerequisites. Space does not allow for every such place in the ITA to be subject to an in-depth analysis; nor does the quantitative classification in legal categories provide sufficient basis for a selection.

Against this background, there is reason to conduct a more thorough qualitative categorization. Indeed, even within the listed potential subjective prerequisites, the terms "intention" and "purpose" are used in different ways. It is possible to distinguish between the use of these expressions where the subject, usually the taxpayer, is noted, and where the terms are used in passive form.

I have chosen the following three categories as a qualitative breakdown that serves the objective of this article:

1. cases in which the expression explicitly states that the purpose or intention of the taxpayer (or other person) is of particular significance;
2. cases in which the expression uses intention or purpose in passive form or otherwise, but obviously suggests a meaning corresponding to 1; and
3. other situations that use the terms *purpose* and *intention*.

In the following analysis, I have chosen a number of expressions from Categories 1 and 2, as the probability

to find "real" subjective prerequisites is greatest in these groups.

In the analysis of references in the following sections, a number of questions are asked. Is the purpose or intention of the taxpayer always determined on objective grounds or is there sometimes room for "real" subjectivity? To what extent, if at all, are the individual conditions of the taxpayer taken into account? What is being said in preliminary works or case law?

Although the overall purpose of this article is to identify prerequisites that aim at the will of a particular subject, I have not excluded expressions in which the term's purpose or intention appear to be aimed at a taxpayer who is a legal person. The notion of legal personality is indeed a so-called institutional fact, which lacks a reference in the physical world.

Because legal persons cannot have a conscious will, it is interesting if it appears that the legal system in any way assumes that they do. Because a legal entity cannot have intentions attributed to it, the concept may be purely ideological, in the sense of false beliefs, but it may also refer to the intentions of a CEO or members of the Board.

5.2 Presentation of provisions to be investigated more closely

Using the criteria in the previous section, not many places in the ITA remain. Indeed, it would appear that the number of potential subjective prerequisites is significantly less than what is implied of the terms purpose and intention in the ITA.

In the following sections, I have analyzed a small number of expressions in the ITA, all of which clearly convey the impression of aiming for the purpose or intention of the taxpayer or other subject with an acquisition, capital contribution, or income-generating activity. Some are tax avoidance rules, and some are ordinary rules.

For each expression, I examine: (1) whether it is reasonable to speak of it as a subjective prerequisite, (2) whether application means that the circumstances are assessed on objective grounds, and (3) whether there is room for actual subjective elements (i.e., if the individual purpose or intention of a particular person can be relevant). Finally, I summarize my conclusions and provide criticism of the subjective prerequisite as a legislative technique.

5.3 Definition of liquid assets in the shell company rules

The shell company provisions are in Ch. 25a (legal persons) and Ch. 49 (natural persons), respectively. The rules were introduced relating to the introduction of participation exemption in 2003 (Påhlsson 2014). The term shell company refers to a limited company whose assets are mainly "liquid". The definition in Ch. 25a Sec. 9 Para. 2 is very complex. It is based on the value of liquid assets in relation to the price of shares in a company. The term liquid assets covers assets such as cash, bank holdings, financial instruments, and similar assets (Påhlsson 2014).

Because the specific purpose of this special regulation is to counter economic crime, it is thus a matter of law enforcement by means of tax law.¹⁷ The rules constitute a presumption, the applicability of which is determined on entirely objective grounds, observable by an outside spectator. It follows clearly from the preparatory works that this is the objective of the legislation.¹⁸ The idea is simply to prevent circumvention of the shell company rule.

In principle, the main rule is meant to work mechanically.¹⁹ The reference to taxpayers' purpose with the acquisition is to enable them to disprove the presumption (i.e., to show that taxpayers did not aim to evade the shell company rule). It seems to be a subjective prerequisite, therefore, in the sense that I have given the expression.²⁰

The conclusion is that this is indeed a subjective prerequisite, which as a rule, is tested on objectively observable circumstances. But it also presents the possibility of individual aspects being considered, thereby adding to the uncertainty that characterizes this area, whereby a dispensation provision called the "valve rule" has resulted in a *de facto* delegation of legislative space to the tax administration.²¹ Such uncertainty may seem to be fundamentally negative for the uniformity of enforcement of the law, although it provides an opportunity in its construction to "save" taxpayers from undue results.

¹⁷ See Proposition (Prop.) 2001/02:165 p. 49 (Swed.).

¹⁸ See Proposition (Prop.) 2002/03:96 p. 116-17. In the submitted bill, the burden of proof was on SKV, but this was considered inappropriate. Stock certificates relating to metals that are unrelated to the ordinary/actual activities of the divested company are given as examples of assets that could be covered by the rule.

¹⁹ See Prop. 2001/02:165 p. 49.

²⁰ See above at Section 3.

²¹ The rule is located in Ch. 25 a Sec. 13 and Ch. 49 Sec. 12, respectively. The views of the tax administration can be found at <http://www4.skatteverket.se/rattsligvagledning/edition/2016.10/331706.html#h-Nyanskaftade-tillgangar-likstalls-ibland-med-konter> (accessed 10 October 2016).

5.4 Unintended tax advantage resulting from plot sales

The term plot sales refers to the sale of land without buildings or other permanent constructions. The rule in Ch. 27 Sec. 16 Para. 3 illustrates the uncertainty and lack of predictability that can result from vague statutory laws in general and vague tax avoidance rules in particular. There are no less than three expressions in the same sentence, each of which can be attributed to different meanings.

The background is the provision in the first paragraph of the article. According to this, when the remainder of the plots is realized in a single sale, the sale is considered not to be a part of the real estate enterprise. Instead, the transaction is to be treated in accordance with the provisions on capital gains, which provide for a lower tax rate.²²

However, the article's current third paragraph provides an exception to this rule on capital gains taxation. The proceeds of the final plot disposal are to be taxed as a business activity "if the transaction can be assumed to have taken place essentially with the intention of achieving an unintended tax benefit to the taxpayer, the acquirer, or to someone with whom one of them has an affiliated interest."²³ The term "can be assumed" seems to mean that the taxpayer's purpose is to be deemed by an external viewer. This indicates that individual aspects are not to be considered, but that the assessment is to be made on objectively observable grounds.

The preparatory works discuss what is meant by unintended tax benefits. It is emphasized that the more favorable taxation could be utilized in a manner contrary to the purpose of the rules. Two examples are given: first, that the plots are transferred on favorable terms to a company controlled by the taxpayer or its affiliates; and second, that the plots are sold within the family.²⁴

The statement strongly suggests that transactions of this kind are based on objective criteria leading to the conclusion that the taxpayer's purpose was to achieve the unintended tax benefit. So far, the subjective prerequisites appear to be fully consistent with the common idea that

²² A significant difference for so called simple plot sales compared to other activities where real estate is considered as stock assets, occurs where the simple plot rules apply, operations can cease, and stock assets can return to capital assets. (See Ch. 27 Sec. 17.)

²³ Earlier tax avoidance rules talk about "unauthorized" tax benefits (Swed. *obehöriga*). The term "unauthorized" does not appear to be used in recent legislation. The older terminology is also used in Sec. 4 Para. 3 of the Coupon Tax Act (withholding tax).

²⁴ See Proposition (Prop.) 1967:153 p. 156-57 (Swed.).

the existence of such subjective facts is established on objective grounds.

It is also emphasized that a company may well have commercial reasons for the transaction; therefore, the transaction can be acceptable. It seems to have been the thought of the legislators that a credible statement of the taxpayer may be sufficient, at least unless other circumstances directly oppose it. This conclusion may be supported by the view expressed by the Supreme Administrative Court in the case RÅ 2000 ref. 31 I—that the costs incurred by a limited company need not normally be reviewed, but are presumed to be justified.

The conclusion is that the current provision contains a subjective prerequisite of the common objective character.²⁵ But even though it is a tax avoidance rule, there is clearly room for considering the taxpayer's assertion of economically justified conduct.

5.5 Effect of capital contribution on interest distribution

The rules in Ch. 33 regarding the so called positive interest distribution provide that a standard assessment return on an estimated capital base is shifted from business income to capital income, where it is taxed at a lower rate. Correspondingly, under certain conditions, the rules provide for a negative interest distribution in case of a negative capital base (Pålsson 2014).

The calculation of the capital base accounts for durable contributions to the capital base. According to Ch. 33 Sec. 8, however, this does not apply to contributions "for a purpose other than to permanently increase the capital of the business."²⁶ Although a passive form is used, the only possible subject is the taxpayer.

The rules were changed in 1996. Previously, it was stated that the provision included contributions that "may be assumed" to have been made for another purpose. The term "assumed" may well be said to have pinpointed the purpose of the contribution, as it would appear to an external viewer.

The question is: What kind of subjective prerequisite are we dealing with today? The preparatory works clarify that the legal requirements for a contribution do not necessarily imply that it must be permanent: "On the other hand, it must be a longer period of time, extending at least several years. Thus, the purpose is crucial for the assessment, although unforeseen events may later cause the contribution to be withdrawn."²⁷

Against this background, it seems obvious that it is the personal aspiration of the individual taxpayer with the contribution that is primarily to be taken into account. If the taxpayer's intention is that the contribution will work in the company for a few years, this is enough for it to be included in the capital base. This interpretation is in line with the purpose of the interest distribution regime, which is to prevent the balance sheet from being temporarily distorted on the date when the financial statements are fixed.

The preparatory works also state that it is the taxpayer who has the burden to prove purpose.²⁸ This is reasonable of course, although it does not solve all issues regarding the burden of proof. Nothing is said, for example, about when the taxpayer will have to fulfill the burden of proof. And how can one, at the time of the contribution, prove that the funds will remain and work for sufficient time? When there is no permanent requirement, it can hardly be considered necessary for the taxpayer to enter into a definite agreement regarding a particular investment.

In conclusion, the nature of the contribution is likely to be found only through a post-transaction check.²⁹ Taxpayers who disagree with the tax administration can leave the funds in the business and will, according to procedural rules, be entitled for six years to appeal any decision that goes against them. Moreover, if the funds have been left in business for at least a few years, this means, at least according to the preparatory works, that the purpose of the contribution was sufficiently permanent.

In the light of these reflections, it is still reasonable to assume that the taxpayer's purpose will be assessed on ob-

²⁵ The plot sales rules were introduced in 1967. See SFS 1967:748, 1967: BevU153 (parliamentary committee), Prop. 1967:153 och Statens Offentliga Utredningar (SOU) 1966:23 och 24 (inquiry initiated by Government) (Swed.).

²⁶ The corresponding rules for partnerships and for expansion funds are in Ch. 33 Sec. 19, Ch. 34 Sec. 7, and Ch. 34 Sec. 13. A governmental inquiry has suggested that a system for nonpermanent contributions is sustained. See Statens Offentliga Utredningar (SOU) 2014:68 p. 133 (Swed.).

²⁷ See Proposition (Prop.) 1996/97:12 p. 52 (Swed.). The official motivations for the legislation are also accounted for on the tax administration's website. See: <http://www4.skatteverket.se/rattsligvagledning/edition/2016.10/331592.html#h-Tillskott-foregaende-ar> (accessed 18 October 2016).

²⁸ Ibid.

²⁹ The preparatory works provide an example of supplements that should reduce the allocation base, referring to the amount of money the trader is deemed to have put into the business at the end of a year, for example, to prevent a temporary liquidity crisis, for example—which the trader subsequently withdraws when liquidity has improved. Ibid.

jective grounds (*i.e.*, against the assumed "normal behavior"). It is likely that the duration of the contribution will be decisive, but there is definitely some room for exception in specific cases.

In practice, it is reasonable to assume that contributions are legitimate unless the funds have been withdrawn when the tax return is filed. In view of this, the wording appears to provide scope for an individual subjective assessment. In my view, the entrepreneur's own business considerations should normally be accepted, which means that the presence of a contribution should normally be assumed to have a lasting purpose.³⁰ Therefore, it is not self-evident that the common idea of assessing subjective prerequisites on objective grounds should apply here.

Yet, there is a possible limitation: The Tax Board for preliminary rulings has linked the assessment to what is stated in Ch. 13 Sec. 7 Para. 2 regarding the expansion funds that are considered "belonging to the business". The question in the case was whether a business could be used as a long-term "savings deposit" for private capital. Such an estimate of the taxpayers' contribution to their businesses can in fact be done at any time.³¹ In this case, the Tax Board found that the expansion funds did not belong to the business. However, the preliminary ruling was not appealed.

5.6 Sustainable capital contributions for the purpose of calculating the 'basis for the threshold amount'

The Swedish tax regime for close companies has been outlined in English (Pålsson 2014).³² The so-called threshold amount is a tool used to deem income from a close company either as earned or capital income. When calculating the threshold amount, the basis, according to Ch. 57, Sec. 12, is reduced with such contributions that were made for a purpose other than the permanent provision of capital to the company.

When calculating the year's threshold amount, it is beneficial for the shareholders if their acquisition cost is high at the beginning of the year. Some years ago, the tax administration directed the legislature's attention toward

extensive tax planning, whereby owners of close companies temporarily inflated their acquisition costs with the help of loans, in order to calculate higher threshold amounts. This would secure a larger part of the year's dividend being taxed at a lower rate (*i.e.*, as capital income). To prevent this, the law was subsequently changed.

The original proposal meant that all capital contributions submitted two years before the start of the tax year should be omitted. However, the government and several representatives for industry believed that this would be detrimental to the capital supply of smaller companies.³³

In the preparatory works, the government refers, among other things, to the supplementary rule in the rules on interest distribution.³⁴ The rule in Ch. 57 Sec. 12, however, was formulated differently, as it was not limited to contributions made in the previous year. Contributions provided in previous years were also considered potentially profitable in connection with tax planning and were therefore covered by the scope of the new legislation. Furthermore, the motivation in the government bill states that a reference point for the assessment of whether the contribution is considered to be sufficiently permanent is that it be intended for use in the company for at least a two-year period.³⁵

The rule can be regarded as maintaining a subjective prerequisite, with some scope for an assessment based on taxpayer's individual circumstances, as they have the chance to specify a credible use of the contribution for two years. If the question arises shortly after the contribution has been made, then the statement itself may suffice. The prerequisite is then subjective, because it is the individual intent of the taxpayer that determines the tax result. If some time has elapsed, a retroactive check is possible. Evidently, this will result in a more objective assessment. The preparatory works explicitly state, however, that the contribution need not have been put to use in the business in order for it to be considered.³⁶

³⁰ See *Högsta förvaltningsdomstolen* (HFD) (Supreme Administrative Court, SAC) RÅ 2000 ref. 31 I (Swed.).

³¹ See the advance tax ruling by *Skatterättsnämnden* (Tax Board) delivered on 7 January 2016 (dnr 118-14/D) (Swed.).

³² "The term close company is used in English in International tax law for small limited companies where the owners are usually active in the business."

³³ See Proposition (Prop.) 2011/12:1 p. 436 (Swed.).

³⁴ See Ch 33 Sec. 8 and above at Section 5.5.

³⁵ See Prop. 2011/12:1 p. 437.

³⁶ *Ibid.* The Tax Avoidance Act may still apply, however. See, for example, *Kammarrätten i Sundsvall* (Court of Appeal in Sundsvall) case 501-503-14, 12 May 2015.

5.7 The residential property concept takes into consideration the intention to reside

Ch. 2 Sec. 8 contains a definition of the term private residence. This concept is decisive for whether a home is to be taxed within the capital or business income schedules. The rule applies to real estate and to the Swedish form for ownership of flats.

The term "private residence" also encompasses two types of property: housing that is being used for private housing; and housing that the owner is not currently using, but in the future, he intends to have it for self-use or for use by close relatives.³⁷ Both types of housing are taxed in the same way within the capital income schedule.

It should be noted that the provision serves as a tax law demarcation principle and not as a tax avoidance rule. According to the preparatory works, however, a mere statement from taxpayers about their intention should not be sufficient. In addition, it must be possible to observe the intention in some way.³⁸ Evidently, this is in line with the general conception of how subjective prerequisites are to be evaluated in tax law, *i.e.* on objective grounds.

But the provision is open to interpretation problems (Pålsson 1993; Lodin *et al.* 2015). The relevant time frame is unclear. Is a holiday home in Spain to be treated as a private residence if the taxpayer intends to settle there, to retire in ten years, say, and until then to rent it? And what if the taxpayer claims that the property is held in order to provide children with a home in the future?

A requirement that objectively observable circumstances should support a statement of intent must comply with the principle that the legislature cannot request the impossible. Otherwise, the subjective prerequisite becomes illusory. It is stated consistently in the preparatory works that a home may well have been rented out for a long time, but that the owner may still intend to settle in it in the future.³⁹

Even if a home is sold shortly after the purchase, it may well have been the taxpayer's intention to settle in it. This could be the case, for example, if a condominium flat

were acquired by someone who is later refused membership in the condominium association and must therefore sell the flat.⁴⁰ Please note that the circumstances say nothing about the taxpayer's intention for purchasing the property, which may well have been for speculative purposes.

Against this background, the taxpayer's claims, in accordance with the examples mentioned above, should normally be accepted. Thus, this prerequisite must be regarded as subjective, with a relatively large scope for consideration of individual factors. Indeed, the credible claims of the owners and close relatives are to be considered, provided the circumstances at least do not contradict the claims. If, however, observable circumstances speak against the taxpayers' assertions of their intentions, the claim should be ignored.

Finally, it should be noted that there is an additional demarcation rule regarding real estate that treats purpose. According to Ch. 2 Sec. 13, the concept of residential property also includes land if the intention is to build a private residence on it. The provision also refers to the private housing rules in sections 10-12, but not to the provision discussed above in this section.

The rule in Ch. 2 Sec. 13 is addressed in the preliminary works, which, to some extent, confuses the information about residential property and residential buildings. In this case, it seems clear from the preparatory works that objective circumstances are to form the basis for the assessment.⁴¹

5.8 The fulfilment requirement for public foundations and other associations

Under the ITA, income received by some bodies and associations, such as foundations, is largely tax exempt. Tax exemption presupposes, however, that the income is used for the organization's explicit purpose. Ch. 7 Sec. 6 provides that trusts, non-profit associations, and religious communities shall use their income in pursuit of the public interest (the fulfilment requirement). Pursuant to Ch. 7 Sec. 7, when assessing whether the fulfilment requirement is met, consideration shall be given to revenue consisting of support, gifts, inheritance, or other contributions "only if it is apparent from the circumstances that they are intended to be used directly for the activities."

³⁷ The relatives indicated are defined in Ch. 2 Sec. 22.

³⁸ See Proposition (Prop.) 1989/90:110 p. 500 and Proposition (Prop.) 1990/91:54 p. 191. In addition, see *Kammarrätten i Göteborg* (Court of Appeal in Gothenburg) case 4719-11, 13 January 2013. This case concerned the owner of a building firm who had privately bought, renovated, and subsequently (after eight months) sold two condominium flats. The sales were taxed as business income, despite the owner claiming that he had intended to reside permanently in the flats.

³⁹ See Proposition (Prop.) 1989/90: p. 645.

⁴⁰ It follows from the Supreme Administrative Court's case law that capital gains taxation still applies. See HFD 2014 ref. 78.

⁴¹ See Prop. 1989/90:110 p. 501.

The preliminary work sets out whose intention is relevant. The importance of the intention is also expressed in an interesting way.

An amount shall be deemed as revenue only if it is apparent that the donor's intention is that the amount may be used directly for public service activities. This may be apparent from the circumstances even though the intention cannot be determined immediately. For example, it may be assumed that gifts of small amounts, especially for collection activities, can be used directly. For foundations, contributions are often intended to be added to the capital. In these and similar cases of fundraising, the return on the contributions received shall be included first paragraph.⁴²

The statement clarifies that the intention should be determined in the manner normally assumed in the field of tax law, namely on objective grounds. In addition, a presumption is established for smaller amounts. No explicit mention is made in the preparatory works, however, to account for the purpose of an individual. It would appear that the consideration was not presupposed in the legislative process. Therefore, the following reflections may be emphasized.

The lack of reflection in the preparatory works on the subjective nature of the prerequisite in question implies that both approaches are compatible with the wording. It is thus possible, in a difficult case, to consider the taxpayers' claims regarding their intentions, even if their claims are not supported by objectively observable circumstances. It may also be that it is not contradicted and that the taxpayer's statement simply gives a credible impression.

5.9 Tax-free educational benefit for those at risk of becoming unemployed

Pursuant to Ch. 11 Sec. 17, the benefit of paid education for the taxpayer, provided for the taxpayer to continue work, is tax exempt if there is a risk of the taxpayer becoming unemployed within five years. It is the taxpayer who has the burden of proof that there is a situation that the rule is aimed at, for example, the employer has notified a workers' union of possible redundancies, or that the employer is considering them.⁴³

When the provision was extended in 2014, a new paragraph was added: "The first paragraph also applies if the taxpayer intends to get another job with the same employer."

In the preparatory works to the new wording, it was mentioned that the provision should also "state that it is applicable if the taxpayer is to be given another job with the same employer (RÅ 2002 note 96)."⁴⁴

In the Supreme Administrative Court case RÅ 2002 not. 96, the provision was applied in its earlier version, before the introduction of the second paragraph. It was deemed applicable in a case in which, as a part of a major restructuring in a county, a nurse gave up her employment in order to be able to obtain (other) continued employment as a more qualified nurse with the same county council. The implication of the restructuring was, in practice, that the county council wanted more highly skilled nurses and fewer nurses with lesser education. Thus, the county council did not intend to reduce the proportion of healthcare personnel in the real sense—merely to change the skills of a part of the staff. In the absence of additional education, however, the nurse was in danger of being dismissed by and prevented from obtaining employment with the county council.

The SAC stated in the RÅ 2002 not. 96: "The wording of Sec. 32 Para. 3 of the Municipal Tax Act does not prevent the provision from being applicable also in cases where the person concerned is to receive another employment from the same employer". The extension of the provision in 2014 was obviously a codification of what already applied according to case law. The conclusion is that the provision is intended only to clarify that if there is a risk of unemployment, it does not matter who the employer is. Thus, it does not contain a subjective prerequisite in the meaning that the expression has been given here: A person's intention is irrelevant to the legal effect. The relevant ambition of the measures is the one mentioned in the first paragraph, namely that the taxpayer may continue to be employed.

5.10 Loss due to deliberate underpricing

Ch. 44 Sec. 24 provides that if an asset is sold at a price below market value, a capital loss is deemed to arise only if it is apparent from the circumstances that the seller did not intend to increase the buyer's wealth. As in the case of Ch. 7 Sec. 7, therefore, it is stated in the wording that it is to be determined on objective grounds if the subjective requisite is met.⁴⁵ The rule was introduced in 1987, albeit

⁴² See Proposition (Prop.) 2013/14:1 p. 517 (Swed.).

⁴³ See Prop. 2013/14:1 p. 225.

⁴⁴ See Prop. 2013/14:1 p. 227.

⁴⁵ See above at Section 5.8.

with a somewhat different wording and scope.⁴⁶ It is clear from the preparatory works that the burden of proof rests on the taxpayer who, in order to deduct such a loss, must prove that a "bad deal" was in fact made.⁴⁷

In addition to the current provision implying that the subjective prerequisite is to be assessed on objective grounds, it is emphasized that the scope for deductions for losses is exceptionally low on sales to related parties. Consequently, in such cases there is a strong presumption that the transaction cannot result in a deductible loss.

6 Conclusion

In this article, I have discussed possible meanings of subjective prerequisites in the Swedish Income Tax Act. Conclusions have been presented continuously and will therefore only be summarized here.

The starting point of the survey has been formulations in the ITA referring to intention and purpose. An inventory shows several hundred hits. On closer examination, however, it appears that only a small number of places where the current terms are found may, in fact, contain subjective prerequisites. There appears to be no change over time in the designs of laws.

Of the formulations that have been subjected to closer analysis, the majority can be categorized as elements of tax avoidance rules. The investigation confirms the prevailing perception, namely that the existence of a certain intention of the taxpayer in income taxation should normally be assessed on the basis of objectively observable circumstances.

A closer analysis of a number of subjective prerequisites shows that most of them also have a scope allowing for assessments based on credible data from the taxpayer regarding the purpose of certain transactions. However, if such data were to be used as the basis for the assessment, it is usually necessary that other circumstances do not contradict them. Indeed, the survey provides support for the conclusion that objectively observable circumstances generally create a presumption. Consequently, if the taxpayer claims that individual intent differed from what was suggested by other circumstances based on normal behavior, there are strong reasons for ignoring the taxpayer's claims.

As a legislative technique, the use of subjective prerequisites represents a *de facto* shift of power from the legislature to the courts and tax administration. This technique should not be overdramatized, however. It always increases with increasing vagueness, and must be considered necessary to some extent in the extensive tax legislation. On the other hand, the legislator can choose to identify objective criteria in the legislation without going by way of subjective prerequisites, the fulfilment of which is still primarily meant to be established on objective grounds. This technique has the principal advantages of transparency, uniformity, and predictability. The disadvantage in relation to regulation with subjective prerequisites is that with subjective prerequisites, it is possible to take individual aspects into consideration.

From the point of view of legality and equal treatment, it is important that the introduction and interpretation of vague references to intention and purpose be carefully considered. The terminology is so indefinite that foreseeability is hampered if one does not strive to give such references a fundamentally sustainable meaning.

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⁴⁶ See Proposition (Prop.) 1987/88:62, Bet. (Parliamentary Committee) 1987/8:SkU15, Svensk Författningssamling (SFS) 1987:1203.

⁴⁷ See Prop. 1989/90:110 p. 711.

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Appendix

References to purpose (Swed. *syfte*)⁴⁸

- Ch. 7 Sec. 10: This article refers to the transparency requirement for non-profit associations. The purpose of the association may affect the right to refuse membership. See also Ch. 7 Sec. 11.
- Ch. 7 Sec. 15: Healthcare facilities, which are run without profit, are taxable only for income types that fall under Ch. 13 Sec. 1.
- Ch. 16 Sec. 24: The purpose of rehabilitation measures, including preventive treatment carried out by an employer, is of importance in determining the right to deduct the expenses.
- Ch. 25 a Sec. 14: The purpose of the taxpayer's acquisition of assets is relevant to whether the assets are considered to be liquid (shell company's regime for legal entities).
- Ch. 27 Sec. 16: A final sale conducted within a land/plot enterprise, which essentially aims at a tax benefit, disqualifies the taxpayer

from the use of capital gain rules.

- Ch. 33 Sec. 8: Capital contribution not made for the purpose of long-term increase of capital reduces the capital base for interest distribution (sole trader).
- Ch. 33 Sec. 19: Capital contribution not made for the purpose of long-term increase of capital reduces the capital base for interest distribution (partnership).
- Ch. 34 Sec. 7: Capital contribution not made for the purpose of long-term increase of capital reduces the capital base for an expansion fund (sole trader).
- Ch. 34 Sec. 13: Capital contribution not made for the purpose of long-term increase of capital reduces the capital base for an expansion fund (partnership).
- Ch. 39 Sec. 6: Non-life insurance companies shall deduct fees and contributions relating to another subject's activities aimed at preventing certain injuries.
- Ch. 49 a Sec. 7: The purpose of the taxpayer's acquisition of assets is relevant to whether the assets are considered liquid (shell companies regime for natural persons).
- Ch. 57 Sec. 12: When calculating the basis for the threshold amount, no allowance is made for capital contributions made for any purpose other than the permanent provision of capital to the company.

References to purpose (Swed. *ändamål*)

- Ch. 3 Sec. 10: Short breaks for certain purposes are included in the six months according to the so-called six-month rule.
- Ch. 7 Sec. 4: This article defines the purpose requirement for foundations, non-profit organizations, and religious communities. See also Ch. 7 Sec. 3, which determines the extent of tax liability in view of the purpose requirement.
- Ch. 7 Sec. 5: Foundations, non-profit associations, and religious communities shall, in their activities, promote public interest (the activity requirement).
- Ch. 7 Sec. 6: Trusts, non-profit associations, and religious communities shall use their income in pursuit of public interest (the fulfillment requirement).
- Ch. 7 Sec. 16: Limited tax liability applies to "student nations" (student association) in Lund and Uppsala, and for certain foundations, for the purpose of administering certain tasks provided by statutory law.
- Ch. 7 Sec. 17: Limited tax liability applies according to the "Catalog" for the subjects *Jernkontoret och Sveriges Standardiseringsförbund*, as long as profits are used for public purposes.
- Ch. 7 Sec. 18: There is a presumption of public interest when the fulfillment requirement is applied to certain foundations.
- Ch. 7 Sec. 21: There is a tax exemption for certain properties used for purposes provided in Ch. 3 Sec. 4 of the Property Taxation Act.
- Ch. 8 Sec. 5: There is a tax exemption for scholarships with a purpose other than the recipient's education, if not a reimbursement for specific work and not distributed periodically.
- Ch. 16 Sec. 2: This article describes deductions for entertainment and similar purposes.

⁴⁸ For information in English on Swedish tax law in general and with regard to a number of the specific rules that are included in the inventory, see Påhlsson, Robert. *Business Taxation in Sweden*. Uppsala 2014.

- Ch. 19 Sec. 10: Expenditure on construction equipment is not included in the acquisition value of a building intended for purposes other than housing,
- Ch. 27 Sec. 14: This article outlines the limitation of the concept of a single land/plot enterprise in respect of transfers to employees.
- Ch. 30 Sec. 14: Acquisition of tax allocation reserve is accepted upon transfer of mutual life insurance companies' insurance policies to companies formed for this purpose.

References to intention (Sw. *avsikt*)

- Ch. 2 Sec. 8: The term *private residence* also encompasses housing that the owner is not currently using, but intends to use in the future as a dwelling for himself or for close relatives.
- Ch. 2 Sec. 13: The concept of residential property also includes land if the intention is to build a private residence on it.
- Ch. 7 Sec. 7: When assessing whether the fulfilment requirement for certain tax-exempted associations is met, account shall be taken of revenue consisting of beneficial support only if the intention is direct use for the association's activities.
- Ch. 11 Sec. 17: Tax exemption for the benefit that consists of the employer paying for an employee's education, at a time when the employer is undergoing restructuring, applies if the taxpayer intends to receive other employment with the employer.
- Ch. 44 Sec. 24: When selling under market value, capital losses are deemed to arise only if the seller did not intend to increase the buyer's wealth.