

Proposed new tax regulations for the corporate sector

Sweden: April 2018

In Brief

On 21 March 2018, the Swedish government put forward proposals for new corporate tax regulations. The key suggestion is to limit the deduction for net interest expenses in the corporate sector. The right of deduction will be based on a so-called EBITDA-rule and will be accompanied by a decrease in the corporate tax rate.

The proposal in brief

Right of deduction

A new general limitation on the right of deduction has been proposed for net interest expenses in the corporate sector. This includes interest costs to external lenders as well as on interest costs on intra-group debt and is thus a change compared to prior legislation which limited the deduction of intra-group interest costs only.

The right of deduction will be based on a so-called EBITDA- (Earnings Before Interest, Tax, Depreciations and Amortizations) model. This means that net interest expenses are deductible up to a certain level of the taxable EBITDA-result (not the same as the EBITDA according to the accounts). The current proposal is 30 percent of the taxable EBITDA-result.

An allowance of SEK5m is proposed, which implies that net interest expenses up to that amount will not be covered by the proposed EBITDA-rule. Should the company be part of a group, the entire group must not apply the same rule, but if one company in the group uses the allowance rule, the total deduction of the entire group may not exceed SEK5m.

Net interest costs which are disallowed under this EBITDA-rule can be carried forward for a period of up to six years. Any such net interest costs can however only be utilized against future net interest income.

Net interest profit in one company can be offset against net interest costs in another group company. There are however no other specific relief or consolidation possibilities in order to apportion the EBITDA-allowance between group companies. Instead, general tax consolidation rules by way of group contribution, which are subject to limitations, must be applied to apportion profit between companies within a group. The latter can potentially create a situation where it would have been more favourable to carry out all business within one company, which is very uncommon in the real estate industry. Effectively consolidation within a group will in any case become more burdensome than before as a result of these new restriction rules and due to the fact that no efficient rules are proposed to apportion the EBITDA-allowance within a group.

Corporate tax rate

The corporate tax rate is proposed to be reduced in two stages. From the current 22 percent to 21.4 percent in 2019 and to 20.6 percent in 2021.

Intra-group interest costs

The government proposes that the current interest deduction limitation rules will be narrowed in scope. Interest expenses on loans from related companies are now proposed to be deductible (subject to the limitation under the EBITDA-rule) if the company which is the beneficial owner of the corresponding interest income:

- is resident in the European Economic Area, or
- is resident in a country with which Sweden has a full double tax treaty and the company is resident in that country under the treaty, or
- is taxed at a rate of at least 10 percent on the interest income (or would be if the interest income had been the only income for the company).

A deduction would however still not be available if the debt relationship exclusively, or almost exclusively, arose in order to create a substantial tax benefit for the group. The expression “exclusively or almost exclusively” means 90-95 percent.

Further, if the debt has arisen due to an intra-group acquisition of assets (e.g. in a debt push down situation), a deduction will only be available where the principal motivation for the acquisition is commercial reasons

Other proposed regulations

It is proposed that a so-called basic deduction will be introduced for rental properties for the costs incurred in new construction, in making additions to existing buildings and in the reconstruction of buildings. The basic deduction implies an accelerated depreciation rate of 2 percent for the first six years after the construction, thus enabling a 12 percent deduction of the capitalized expenditures over the period.

Rules against so-called hybrid mismatching are to be introduced to prevent international tax planning.

Leasing rules are to be introduced addressing only the interest portion and not the right of depreciation.

Details

The new regulations are proposed to come into effect on 1 January 2019.

The proposed limitation on interest expense deduction implements the EU Directive against tax avoidance and OECD’s recommendation against base erosion and profit shifting (BEPS) into Swedish law.

Our view

As the main proposal is a direct effect of the EU Directive, changes are, and have been, expected. Comparing the new proposal to the prior proposal issued during the summer of 2017, there are a few welcome changes.

First of all, it can be noted that the Government has taken into account arguments and analysis made by stakeholders. Instead of proposing an EBIT-model, which the prior proposal considered as the most reasonable limitation, an EBITDA-model is instead proposed. Further, the limit (in percent) has been increased from the prior 25 percent to 30 percent. In addition to this, the safe harbour rule is substantially higher (SEK5m) compared to the prior proposal (SEK100k).

Although, further limitation into interest deductibility increases the complexity of the corporate tax system and the administrative burden for tax payers, it is encouraging to see that the new proposal is more in line with the de minimis rules in the EU Directive. Suggesting well-known rules that are similar to those proposed by other membership countries minimizes the risk of harmful effects on the corporate sector in Sweden.

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