

Government proposal on tax treatment of reorganizations

The Norwegian government released a proposal for legislative amendments that would significantly increase the opportunities for cross border reorganizations. The legislative proposal broadly follows the suggested amendments from a discussion paper released 18 January 2010. Given the current composition of the Norwegian parliament, the proposal is likely to be adopted without any significant changes.

General observations

The general impression of the proposal is that it entails a liberalization and simplification of the rules governing cross border reorganizations. Furthermore, if adopted, the proposed changes will contribute in bringing the Norwegian tax law further in line with Norway's obligations under the EEA agreement. The Government states that the EU merger directive has been a general policy guideline when drafting the proposals.

Current rules for reorganizations

Under Norwegian tax law, a merger or demerger is as a main rule treated as a disposal of the shares and underlying assets, which can lead to capital gains taxation, recapture of depreciation and restrictions on the loss carry-forwards. However, under certain conditions, mergers and demergers can be done tax-free on a roll over basis. A tax free merger or demerger implies that the tax positions connected to the transferred assets or business are transferred to the acquiring company. The rules on tax free mergers and demergers only apply if all the companies involved are resident in Norway.

The main condition for a tax-free merger or demerger is that the merger is executed in accordance with Norwegian corporate law and Norwegian GAAP.

Cross border share for share exchanges

Norwegian tax law currently does not contain any rules for tax free share for share reorganizations. However, since 2004, corporate shareholders have been able to rely on the participation exemption method to enter into such transactions. The participation exemption method has limited applicability for shares in companies resident outside the EEA.

The Government now proposes that Norwegian shareholders – both corporate and individual – may exchange their shares in a limited liability company for shares in a limited liability company on a roll-over basis. The deferred tax is contingent on the following criteria:

- Any cash or consideration other than shares in the transferee company cannot exceed 20% of the total consideration received,
- At least 90% of the shares in the transferor company must be exchanged,
- Neither the transferee or the transferor company may be resident in a low tax jurisdiction outside the EEA. If either is resident in a low tax jurisdiction within the EEA, that company must be actually established and conduct genuine economic activity in its state of residence in order to qualify the share swap for roll-over treatment,
- At least one of the participating companies must be resident outside Norway.

Cross border mergers and demergers

The EU company merger directive was implemented in Norwegian company law in 2007. The Ministry of Finance now proposes that the following transactions may take place on a tax neutral basis (i.e. without immediate taxation at neither the company nor the shareholder level):

- One or more Norwegian limited liability companies should be able to merge with one or more companies with limited liability resident in a jurisdiction within the EEA. If the Norwegian company is the transferor company any Norwegian business operations must be continued in a Norwegian branch.
- A demerger of a Norwegian limited liability company where the surviving companies subsequently are subject to the laws of at least two different jurisdictions within the EEA. The deferral is subject to the condition that any business operations in Norway must be continued through a Norwegian branch.
- Companies resident in other jurisdictions may merge or demerge without any Norwegian tax consequences. Any assets employed in a Norwegian branch will get a carry over tax basis. The tax deferral is contingent on assets not being transferred out of Norwegian taxing jurisdiction. The deferral only applies with respect to companies resident outside the EEA as long as they are not resident in low tax jurisdictions. If any of the companies are resident within a low tax jurisdiction within the EEA, the deferral is contingent on the company being actually established and conducting genuine economic activity within the EEA.

Tax deferral on transfer of branch assets

The government also proposes roll-over treatment when

- Assets in foreign branches of Norwegian companies are transferred to newly formed foreign limited liability companies in exchange for shares in the limited liability company. The foreign company must be resident in a jurisdiction which has entered into a tax information exchange agreement with Norway.
- When a company resident in a treaty jurisdiction transfers its Norwegian branch to a related company resident in Norway, or to another group company's branch in Norway.

Exit tax

Under current legislation, a Norwegian company transferring its tax residency out of Norway is taxed as it was liquidated on the day before the transfer, entailing a full taxation at both the level of the company and its shareholders. In a recent reasoned opinion from the EFTA Surveillance Agency (the EEA equivalent to the European Commission) it was argued that these rules violate the freedom of establishment under the EEA Agreement.

The government now proposes an exemption to the exit charge when companies are moved to another jurisdiction within the EEA. In the event the company is transferred to a low tax jurisdiction within the EEA, the exemption is contingent on the company being actually established and conducting genuine economic activity in the new resident state after the transfer. To the extent any assets or liabilities are transferred out of Norwegian taxing jurisdiction, these will be subject to a gain or loss recognition under the general exit tax regime.

Other proposals

The proposal also contains several proposed changes that affect domestic and cross border reorganizations alike. The most significant amongst them is abolishing the general clause that conditions the tax deferral of mergers and demergers on the transaction being executed in accordance with Norwegian company law and GAAP. This requirement has been strictly enforced by the tax authorities and has been heavily criticized by both tax practitioners and scholars.

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