

European Tax Law

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European Tax Law: Secondary Law – The Merger Directive



“THE MERGER DIRECTIVE” 90/434/EEC; 2005/19/EC; 2009/133/EC

The objective of the directive

- Reorganizations generally triggers no capital gains taxation **at domestic level** as taxation on Assets, Losses and Hidden Reserves or Provisions is typically deferred until late disposal or possibility to use them.
- Cross-border Reorganizations in the Internal Market require not to be jeopardised by restrictions, distortions or disadvantages arising from the tax provision of different MS
- Simply extending domestic rules to cross borders situations could not solve the differences between MS
- Common Tax System for Mergers, Divisions, Transfer of Assets and Exchange of Shares was adopted in 1990
- **AIM:** no taxation of Income or Capital Gains in the 4 possible transactions above and in the transfer of SE or SCE later among MS, protection of MS taxing rights in case of a transferring or acquired company.



“THE MERGER DIRECTIVE”

Historical Developments

- In 1969, proposal on a common tax treatment of EU cross-border Merger (and demerger/divisions, transfer of assets, exchange of shares)
- It took 20 years for final proposal adopted by the Council 1990
- In 2003 proposal to amend Directive broadening the personal and objective scope with the view to extend the list of companies including SE and SCE, including the transfer of registered office and partial divisions”.
- Amendments were codified in 2009



“THE MERGER DIRECTIVE”

Personal Scope

- Art. 3(a):
 - **Company from a MS:** 3 requirements, one of the legal forms, tax resident within EU, subject to one of the tax of the annex without the possibility of an option.
 - Conditions above may be met in 2 different MS. However all conditions have to be met cumulatively
 - Cross Reference to ATAD 1 due to these transactions
 - Example with PEs



“THE MERGER DIRECTIVE”

Objective Scope

- Art. 1, requires a “company from a MS” to be involved in any of the operations/transactions covered in art. 2
 - Art. 2 the list of Transactions is exhaustive:
 - MERGER
 - DIVISIONS, PARTIAL DIVISIONS
 - TRANSFER OF ASSETS
 - EXCHANGE OF SHARES
 - TRANSFER OF REGISTERED OFFICE of an SE or SCE
- NO OTHER TRANSACTIONS OR REORGANIZATION TYPES COVERED



“THE MERGER DIRECTIVE”

Objective Scope

- **MERGER:**
- Art 2 (a) defines Merger: an operation where one or more companies transfer all of their assets and liabilities to another company (dissolving without liquidation). The **Transferring Company** cease to exist.
- The **Receiving Company** is the legal successor of the assets and liabilities. In return for the assets and liabilities received it **issues shares** to the shareholders of the Transferring company. An additional cash payment is allowed, not exceeding 10% of nominal/accounting value.
- **3 Different subtypes of Mergers are defined:**
 - (1) one or more existing Co.s merge into another existing Co
 - (2) two or more Co.s merge into a NewCo
 - (3) wholly owned Subsidiary merge with its parent Co. (UPSTREAM MERGER)



“THE MERGER DIRECTIVE”

Objective Scope

- DIVISIONS and PARTIAL DIVISIONS:
- Art 2 (b) and (C) defines the above: Division is an operation where one Company transfer all of its assets and liabilities (dissolving without liquidation). The **Transferring Company** cease to exist.
- The **Receiving Company/ies** is the legal successor of the assets and liabilities. In return for the assets and liabilities received it/they **issues shares** to the shareholders of the Transferring company. An additional **cash payment** is allowed, not exceeding **10%** of nominal/accounting value.
- **Since 2005, Partial Division is also covered**, no dissolution, one or more branches of activity to one or more existing Co.s (split-off).
- Definition of **Branch of activity (2j)**. An Independent business capable of functioning by its own means. Transfer of a single asset is not covered.



“THE MERGER DIRECTIVE”

Objective Scope

- TRANSFER OF ASSETS:
- Art 2 (d) defines the above: an operation where one Company transfer, one or more branches of its activity. The **Transferring Company does not** cease to exist.
- The **Receiving Company/ies issues shares** to the Transferring company.
- No additional cash payment is allowed.
- Definition of **Branch of activity (2j)**. An Independent business capable of functioning by its own means. Transfer of a single asset is not covered.



“THE MERGER DIRECTIVE”

Objective Scope

- **EXCHANGE OF SHARES:**
- Art 2 (e) defines the above: an operation whereby the Acquiring Company pays for the shares in the Acquired Company by issuing shares of its own capital to the former shareholders of the acquired company. Acquired company becomes a Subsidiary.
- No cash payment exceeding 10% of the nominal/accounting value of the shares.
- **TRANSFER OF REGISTERED OFFICE (SE and SCE) art. 1(b)**



“THE MERGER DIRECTIVE”

PROVISIONS ON TAX CONSEQUENCES

- Essence of the Directive is the **Deferral of Capital Gains Tax** for all operations covered. Art. 4(1) and 4(2)(a)
- **Roll Over Basis** (carrying over the value for tax purposes of the assets, liabilities and shares involved) Art. 4(4)
- MS shall refrain from taxing any cap. gain potentially triggered, i.e. **NEUTRALITY**
- Book-keeping of the same tax values at Receiving Co level/ shareholders level
- **Remaining Permanent Establishment Requirement** Art. 4(2)(b) safeguarding of tax rights for MS of the Transferring Company



“THE MERGER DIRECTIVE”

PROVISIONS ON TAX CONSEQUENCES

- Art . 5 Carry Over of Tax Free Provisions and Reserves – Roll over to PE
- Art. 6 Take Over of Losses – ECJ decisions Marks & Spencer (final losses)

- NO taxation of the SHAREHOLDERS involved

Art. 10 (1) Transfer of a foreign PE – triangular case

Hybrids Entities included in 2005, artt. 4(3), 8(3) and 11.



THE INTEREST & ROYALTIES DIRECTIVE

ABUSE

Art. 15 Anti- Abuse Clause

- MS may refuse to apply the benefits of the Directive where it appears that the reorganization has as its principal or one of its principle objective tax evasion or tax avoidance.
- Lack of a definition of Tax evasion or taks avoidance.
- NOW ART. 6 OF ATAD 1 – arrangements or series of arrangements (include reorganizations)

MS are free to impose domestic legislation to regulate this aspect within the limits of primary law.

- Leur Bloem C-28/95 and Kofoed C-321/05 ECJ and Zwijnenburg C-352/08 cases