

Austria an attractive place for Holding Companies

1. Introduction

Austrian law does not recognise a specific holding company status: a holding company is therefore taxed as any other Austrian company. Nevertheless, the following features of the tax system make Austria a favourable jurisdiction for international holding companies:

- A competitive tax rate of 25% with effect from January 1st 2005;
- Attractive group taxation regime with effect from January 1st 2005;
- No thin capitalization legislation;
- No withholding tax on interest paid to non-residents;
- International participation exemption for dividends and capital gains received from foreign subsidiaries;
- No C.F.C. legislation
- No withholding tax on dividends paid to E.C. resident parent companies;
- More than 60 double tax treaties, most of which follow the OECD treaty model reducing the general withholding tax of 25% on dividends.

2. Establishing and Funding of an Austrian Company

There are two legal forms available for setting up an Austrian holding company: The “GmbH” (*Gesellschaft mit beschränkter Haftung*, limited liability company) and the “AG” (*Aktiengesellschaft*, joint stock company). The GmbH is characterized by a lower minimum capitalization requirement (GmbH: € 35,000; AG: € 70,000) and by less strict company law provisions. Incorporation for both companies is carried out by notarial deed; registration is filed at the public Companies Register at the relevant Commercial Court. For tax purposes, both the GmbH and the AG are non-transparent entities.

Equity contributions to an Austrian company are subject to Capital Duty of 1%. In case of larger equity contributions such capital duty burden might possibly be reduced by application of specific structures available through exemption rules in the Capital Duty Act and the Austrian Reorganisation Act. However, expert advice will have to be sought for each individual case.

Austria does not impose statutory thin capitalization rules. Loan arrangements between an Austrian company and one of its shareholders are generally recognised for tax purposes provided the terms of the loan meet the conditions of an arm's length test. In specific cases, debt/equity ratios of 85:15 have been accepted by the tax authorities.

3. Income Taxation of Austrian Companies

3.1 Residency and Taxable Income

A company is resident in Austria for tax purposes if it has its legal seat or its effective place of management in Austria. Resident companies are subject to corporate income tax on their worldwide income at a flat rate 25% (rate effective as of 1st January 2005; previously rate of 34%).

There is a minimum annual corporate income tax of € 1,750 for a GmbH and € 3,500 for an AG, such tax payable in advance in equal quarterly instalments. This minimum tax is payable even in case of no taxable income in Austria.

3.2 Participation Exemption

The Austrian Corporate Income Tax Act (CITA) distinguishes between domestic participation exemption for participations in Austrian resident companies and the international participation exemption for shareholdings in non-resident companies.

3.2.1 Domestic Participation Exemption

Any income received by a resident company from another resident company is exempt from corporate income tax, regardless of extent of shareholding or holding period (sec. 10/1 CITA).

Capital gains from the sale of the participation in an Austrian company, however, do not fall under the domestic participation exemption and are fully taxable. Gains realised upon the liquidation of the subsidiary are treated as capital gains and not as dividends.

3.2.2 International Participation Exemption

Under Section 10/2 CITA, dividends and other distributions of profits received by an Austrian company from a foreign company are tax free subject to the following conditions:

- The Austrian Company holds at least 10% of the share capital of the foreign company;
- The shares have been held for a minimum period of one year; and
- The foreign company is comparable to an Austrian corporate entity or meets the requirements of Article 2 of the EU Parent/Subsidiary Directive.

If the holding period of one year is fulfilled, the international participation exemption applies even retrospectively to dividends paid during the first year. Inter-company dividends paid from profits earned by the subsidiary prior to the acquisition of the shares by the holding company are also covered from this tax exemption.

Under the international participation exemption, capital gains (or losses) from the alienation of shares and from the liquidation of a subsidiary are, in principle, tax neutral and not included in the tax base. Similarly, no tax deduction for a write down of the value of the participation may be claimed.

However, the Austrian Holding company may elect to include capital gains and losses from an international participation in its tax base. This irrevocable election must be made when filing the tax return for the business year during which the foreign participation has been acquired and also extends to any further quotas in the participation within the foreign company the Austrian parent may acquire at a later point in time. Opting for such taxable treatment may be sensible in cases of expected losses and write-downs of the foreign participation.

The international participation exemption is not available in case:

- The subsidiary's main business consists of, directly or indirectly, deriving passive income, i.e. interest income, rental income (excluding rents from immovable property) or income from royalties or the alienation of participations. However, dividend income derived (directly or indirectly) from operating companies is not considered as passive income; and
- The subsidiary is subject to a tax system that is not comparable to the Austrian system. According to the relevant Directive of the Minister of Finance, a foreign tax system is comparable to the Austrian system if an average tax burden on the subsidiary's income as computed in accordance with the Austrian tax law principles exceeds 15%.

If both of these circumstances apply, the “exemption method” switches over to the “credit method”. This means that

- Dividends and capital gains from the alienation of shares in the foreign company become taxable at the level of the Austrian holding company; and
- Foreign corporation tax on the profits of and withholding tax on the dividends from the foreign company are credited against the Austrian tax liability on the foreign source income.

The application of participation exemption may also be denied under the abuse-of-legal-rights-concept.

3.2.3 Deduction of financing costs

As a general principle, costs relating to tax-exempt income are not tax deductible in Austria. However, since 1st January 2005 financing costs for the acquisition of participations qualifying to national and international participation exemption are also deductible.

3.3 Carry forward of Losses

Since 1991, it has been possible to carry forward losses indefinitely. However, only 75% of a year’s taxable income may be offset by losses carried forward. A carry back of losses is not permitted.

3.4 Losses incurred by foreign permanent establishments

In 2001, the Supreme Administrative Court held that losses generated in a foreign permanent establishment, which are not deductible abroad, can be deducted in Austria even though income derived from the foreign establishment would be tax exempt under an applicable tax treaty. Conversely, if in the following years the loss can be deducted abroad – wholly or partly- from foreign taxable profits, the tax base of the Austrian tax payer will be increased by an amount corresponding to the deduction. The 2005 Tax Reform Act incorporates that practice applied by the tax authorities into the Austrian Income Tax Act and the CITA.

3.5 Group Taxation

As of January 1, 2005, a new group taxation regime has been introduced to replace the existing “*Organschaft*” (ie. national group taxation) concept that was widely seen as outdated. Under the new rules all taxable profits and losses of group members are attributed to the group parent. However, group taxation is optional; the option can be exercised separately by each company that is a potential group member.

The group parent must be either an Austrian company or an Austrian-registered branch of a foreign company in such legal form that is either listed in the Art 2 of the EU Parent/Subsidiary Directive or comparable to an Austrian corporation and that has its effective place of management in a member state of the European Economic Area. Several companies may jointly act as a group parent provided that certain minimum holding requirements are met.

Participating group members may be both Austrian and foreign companies in such legal form that is comparable to an Austrian corporation, and which is held by Austrian resident group members or the group parent.

To qualify as a tax group, financial integration is required. The group parent must hold - directly or indirectly – a participation of more than 50% in the share capital as well as a majority of the voting rights of each Austrian or foreign subsidiary that is to be a member of the tax group. This financial integration requirement must be met during the entire business year of the participating subsidiary. The group members must also file a written application with the revenue office which is binding for at least three years.

If the conditions for group taxation are fulfilled, 100% of taxable profits and losses of the Austrian group members are attributed for tax purposes to the group parent even if the parent does not hold all shares in a group member. In such cases it is necessary to reach agreements on compensation payments. Such compensation payments are treated as tax neutral in Austria.

Regarding foreign group members, only losses (not profits) will be taken into account. The loss that is attributed to the group parent has to be calculated in accordance with Austrian tax law. If, in the years that follow, the foreign member obtains a credit for the foreign loss against foreign profits (e.g. by using a loss carry forward provision) in accordance with the rules of the foreign tax laws in questions, recapture rules apply in Austria with the result that the tax base of the group parent will be increased by the amount of such losses used abroad. Should the foreign member cease to be a member of the tax group for any reason other than voluntary liquidation or insolvency, the tax base in Austria will also be increased by an amount corresponding to the losses previously offset in Austria but not yet used abroad.

The new taxation regime also sets out new rules for writing off acquisition cost of shares in Austrian group members. However, whereas in the past goodwill could be amortised only in case of an asset deal, goodwill acquired by the purchase of shares in an Austrian resident company from a seller outside the group may now be amortised, if the target company operates an active business and becomes a group member.

The amortisable goodwill is calculated as the difference between the acquisition cost and the equity book value, increased by hidden reserves attributable to non-depreciable assets. Amortisable goodwill is capped at 50% of the acquisition cost. Goodwill is amortised over 15 years from the date of acquisition, but is tax deductible only when the target company is integrated into the tax group.

4. Austrian Withholding Taxes

4.1 Dividends

Generally, dividends paid by an Austrian company to non-resident shareholders are subject to withholding tax at a rate 25%, unless a reduced rate applies under a tax treaty (e.g. DTT with Argentina and Brazil reduced rate of 15%).

Under the provisions that implement the EC Parent Subsidiary Directive in Austria, dividend distributions by resident subsidiaries to EU parent companies are exempt from any withholding tax under the following conditions:

- The parent has a legal form listed in the Directive;
- The parent holds directly a participation in the Austrian subsidiary of at least 10% (subject to reciprocity; otherwise 25%); and
- The participation is held for at least one year; dividend payments made prior to completion of the minimum holding period are subject to withholding tax, however such tax can be reclaimed retrospectively on application once the minimum holding has elapsed.

4.2 Interest

Interest payments to non-Austrian residents are generally not subject to withholding tax at source in Austria. The same notion applies for income from debt-claims that carry a right to participate in the Austrian debtor's profits unless the contractual relationship is qualified as silent partnership. Only interest income from debt-claims secured by Austrian real estate is subject to withholding tax at a rate of 25%. However, interest payments to EU companies and permanent establishments within the EU are exempted if the requirements of the Interest and Royalties Directive are met (see below, 4.3).

In case of shareholder loans, special attention must be given to the general anti-avoidance principle. If the terms of loan do not meet the arm's length test, interest payments are not tax deductible for the subsidiary and subject to withholding tax as a hidden distribution of profits.

Nevertheless, given the fact that Austrian tax law does not provide for statutory thin capitalisation rules, debt financing may be an attractive method for repatriation of profits from an Austrian holding company to its foreign parent company.

4.3 Royalties

Royalties paid by an Austrian company to non-residents are generally subject to withholding tax at a rate of 25%. However, under most tax treaties the withholding tax is reduced or eliminated altogether (e.g. Germany, Poland, Hungary, Croatia).

As per 1 January 2004, Austria adopted the EU Interest and Royalties Directive. The new Section 99a of the Austrian Income Tax Act applies to interest and royalty payments made after 31 December 2003 to associated companies of a type listed in the Annex to the Interest and Royalties Directive or their permanent establishments that are located in an EU member state, subject to the recipient qualifying as the beneficial owner of such payments.

Companies qualifying as parent, subsidiary or sister companies are deemed to be "associated" for the purpose of the directive. In any event, the parent company must directly hold at least 25% of the capital of the subsidiary for an uninterrupted period of one year.

Furthermore, all companies involved in the structure of the corporate body must be resident within the European Union.

If at the time of the payment the holding requirement has not been met or the Austrian debtor company has not had the required documentary evidence, the withholding tax can be retrospectively refunded upon request as soon as these conditions are met. However, the Austrian tax authorities are free to deny an exemption, if a corporate group structure was established with a view to tax avoidance (in which case the Austrian company will be held liable for withholding tax if it applied the exemption).

4.4 Other Income

A 20% withholding tax is levied on fees for technical and commercial consulting services rendered by a non-resident. However, Austria waives its taxing rights under most tax treaties.

5. **Other Tax Issues**

5.1 Wealth Tax

Austria does not impose a general wealth tax. Wealth tax is only levied on real estate. The annual tax amounts to 1% of a specially assessed value ("*Einheitswert*") which is approximately 10% of the market value.

5.2 Anti-Avoidance Legislation

There are only a few specific statutory anti-avoidance provisions in Austrian tax law, the most noteworthy being the aforementioned provisions relating to the international participation exemption. Austria does not have C.F.C legislation or statutory thin capitalisation legislation. Transfer pricing issues are dealt with in accordance with the general anti-avoidance principle, in particular the arms length principle.