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A: Sharing and shifting of corporate losses – The new profit shifting?

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Summary and conclusions

Austrian corporate tax law does not provide for a definition of losses. Rather, losses simply result from an excess of deductible expenses over income received by a corporate taxpayer, leading to a taxable base below zero. Although corporations are subject to CIT from the time they become legal entities until their legal demise, the Austrian CITA divides the tax life of a corporation into fiscal years. In principle, this means that profits and losses can be balanced with each other within the same fiscal year without any limits. However, from a cross-period perspective, the periodical perspective would lead to undesirable effects: While positive income is always taxed, there is no tax credit in the case of losses. For this reason, Austrian CIT law provides for a very generous loss carry-forward regime without time limits, that still has a compensatory function today and mitigates the effects of the periodicity principle. However, losses can only be offset in the amount of 75% of profits of the taxable year (so that at least 25% of profits remain taxable), with the unused remainder being available for carry-forward. In contrast, a corresponding carry-back of losses is not possible and was only temporarily permitted as a COVID-19-related tax benefit. The Austrian law therefore inherently assumes, through the unlimited carry-forward of losses, that the losses can be used at some point anyway. This approach fails, of course, when the life of a corporation comes to an end. For this reason, when a company is liquidated, the CITA allows the tax period to be extended to up to five years, allowing for a de facto loss carry-back.

However, the unrestricted ability to carry forward losses also enables tax planning. As early as the mid-1990s, the Austrian tax legislator took note of the fact that pending loss carry-forwards could become a tradable asset: Profitable businesses could simply buy loss-making shell entities to deduct losses suffered from former business activities to set up a new business. In 1992, Austria, thus, decided to restrict the loss deduction in economically unjustifiable cases, when the ownership structure as well as the economic and organizational identity of an entity is significantly changed. During the same period, however, it was also recognized that the strict separate entity approach taken by the CITA may be unsatisfactory, especially in cases of legitimate economic reorganization: It should be possible to carry out changes of legal form without major tax consequences and to carry over losses to the acquiring legal entity. Thus, also in 1992, the so-called Reorganisation Tax Act (RTA) was enacted, containing a robust framework for the transfer of losses in reorganisation transactions that aims to prevent artificial loss shifting as far as possible. Finally, in 2005, Austria introduced an optional group taxation regime, enabling the consolidation of profits and losses among controlled entities. It also allows the deduction

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of losses of foreign entities controlled by Austrian resident group members, but requires recapture when the foreign losses are or could be used, e.g., to offset foreign profits.

Since Austria applies a worldwide taxation regime, foreign losses are, in principle, taken into account in the Austrian tax base as well. However, if corporate losses are allocated to a foreign PE by way of a tax treaty and the exemption method is applied to the respective loss, the respective loss would be excluded from the Austrian tax base. Since Austrian tax policy for corporate income shows a strong preference for the exemption method, a regulation for such cases became necessary very early on. Thus, Austria adopted a '*deduction/reincorporation system*', allowing for a deduction of foreign exempt losses, but requiring their recapture when the respective loss can be deducted in the other state. On the one hand, this is intended to take account of the ability-to-pay concept, while on the other hand the recapture shall avoid that the same loss is deducted twice. If the credit method is applied, foreign losses are included in the Austrian tax base anyway, making recapture unnecessary.

Due to the fact that Austria applies a separate entity approach, there is no direct loss offset with respect to losses of foreign subsidiaries, apart from Austria's group taxation regime. Indirect deduction of losses from a foreign subsidiary by way of impairments is very limited according to Austrian law: The Austrian participation exemption regime exempts changes in value and capital gains or losses relating to substantial holdings in foreign corporations. Losses and impairments of qualified participations (above 10%) may not be deducted, unless the corporation has opted against tax neutrality, when it acquired the respective participation. In the latter case and with an ownership interest below 10 %, any losses and impairments are only deductible over seven years.

Austrian corporate tax law is very developed and provides for a very progressive and abuse-proof legal framework which, on the one hand, enables tax-neutral reorganisations, but, on the other hand, also prevents artificial shifting of losses to a large extent. Various amendments to the ITA, CITA and RTA as well as a body of existing case law on corporate and reorganisation tax issues over the past decades have contributed to the fact that mass dissemination of loss shifting-schemes is hardly possible. Both the CITA and RTA provide for numerous SAARs addressing losses. In addition, the Austrian Fiscal Code provides for a GAAR, necessarily also covering loss schemes, which are, for these reasons, a rare phenomenon in Austria. Also COVID specific legislation did not change anything in this respect.

There is no doubt that the OECD BEPS project has been a major development also heavily impacting Austrian tax policy. In particular the EU's ATAD and the adoption of CbCR as well as mandatory disclosure rules by way of amendments to the EU's Directive on Administrative Cooperation have led to major amendments to domestic corporate tax law. Nevertheless, in Austria, many provisions to prevent the abusive use of losses for tax planning purposes were already in place before the OECD's BEPS project was even started. Austria, as an OECD and EU member state, has always closely followed international tax trends. For this reason, BEPS only had a very limited impact on Austrian rules on corporate loss utilization.

Part One: General aspects of corporate tax losses

1.1. General overview

Austria does apply the book-tax conformity principle (Maßgeblichkeitsprinzip). This means that for the determination of profits of corporations, the accounting principles are decisive also for tax law, unless mandatory provisions under tax law provide for deviating regulations.

Corporate losses in Austria are not specifically defined in law, neither in corporate law nor in tax law. The term can be derived from the definition of income and profit.[3] Corporate losses are a negative result of the comparison of the business assets on a reporting date with the business assets on the reporting date of the previous year. In other words, from a profit and loss statement perspective, corporate losses are a negative result of the balance of business income and business expenses (negative income).

Losses are generally allocated to the respective seven income schedules of the Austrian ITA, which are also relevant for the Austrian CITA. As all income of corporations must be attributed to a single type of income – income from business activities (*Gewerblichkeitsfiktion*) – for corporations that are all obliged to mandatory accounting (*Rechnungslegungspflicht*)[4] a loss compensation across various income schedules (vertical loss compensation) is excluded. However, a compensation across one single income schedule (horizontal loss compensation) within the meaning of the ITA is also not carried out for these corporations, because the determination of profits is carried out uniformly even in the case of several activities, each of which would fulfil the characteristics of a separate source of income. The horizontal loss offset thus already occurs at the level of the determination of profits and has the effect of an internal loss offset. However, it should not be disregarded that even within the framework of the uniform determination of profits, intra-company or activity-related loss offset restrictions can also come into effect (see in detail section 1.2.7).

While companies have unlimited access to the loss carry-forward,[5] the loss carry-back was only temporarily available as a response to the COVID-19 crisis. Hence, a total loss which would arise where profitable periods (and corresponding tax payments) are succeeded by loss periods and eventual liquidation, is not considered.

Following a worldwide taxation regime, foreign losses are taken into account in the Austrian tax base. However, Austria applies the exemption method in its overall tax treaty policy. Consequently, Austrian domestic law also allows the deduction of losses even if the respective losses would be exempt according to a tax treaty. To protect the domestic tax base and to prevent multiple deduction of the same losses, section 2 paragraph 8 ITA – which is applicable for corporations underlying the CITA as well – requires repatriation of the foreign losses deducted in Austria, when the foreign exempt losses can finally be deducted in the source state.

3 See, e.g., Raab/Renner, in Lachmayer/Strimitzer/Vock (eds.) Die Körperschaftsteuer (2019) § 8 m.no. 1344.

4 S. 7 para. 3 CITA.

5 S. 18 para. 6 ITA.

1.2. Types of tax policies for domestic losses

1.2.1. Pre-operating losses

Austrian tax law does not contain special rules concerning the carry-over of start-up or pre-operating losses. This is coherent because Austria provides the carry-forward of losses without any time limitations. In addition, corporations are already liable to tax from the time when the legal basis, such as articles of association, partnership agreement or deed of foundation, is established and they first become visible to the public.[6] Therefore, the CIT subjectivity starts even before the corporation exists under corporate law. Formation costs in this period are explicitly deductible.[7] There is no special scheme necessary.

Even if corporations suffer losses, they must pay a minimum tax for revenue-raising reasons.[8] This also applies at the beginning of the tax liability, however, the minimum tax levied is credited against the CIT liability in later years. For limited liability companies (small corporations) with unlimited tax liability, however, there is a reduced minimum tax in the first ten years from the start of unlimited tax liability. According to the legislative materials, this provision is intended to "create a general tax privilege for the formation of limited liability companies".[9] This measure can therefore also be understood as a tax policy measure to mitigate start-up loss situations.

1.2.2. Loss carry-back

Generally, Austrian tax law does not provide for a permanent loss carry-back, neither in income tax law nor in corporate tax law. This has changed for a short term due to the Covid-19 pandemic. In reaction to the economic crisis caused by the COVID-19 crisis, a temporary loss carry-back was introduced in Austria.[10] The loss carry-back was available for both individuals and corporations.[11] The aim of the loss carry-back was to quickly strengthen the liquidity of companies through the earlier offsetting of losses over different periods compared to the offsetting through the loss carry-forward only for which future profits are needed.[12]

In the case of a loss carry-back, business losses suffered in the assessment period 2020 up to an amount of EUR 5 million can be carried back to the assessment period 2019 in order to be set off against profits generated in that year. If such a compensation is not possible in the 2019 assessment, the loss carry-back is extended to the year 2018, up to a maximum of EUR 2 million, with any remaining losses being eligible for an ordinary loss carry-forward afterwards. In total, the maximum amount of EUR 5 million may not be exceeded in 2019 and 2018. In contrast to the loss carry-forward for corporations, there is no 75% offset limit for the loss carry-back.[13]

6 S. 4 para. 1 CITA.
7 S. 11 para. 1 CITA.
8 S. 24 para. 4 CITA.
9 Explanatory Memorandum 24 BlgNR 25 GP 15.
10 See, e.g., Klokar, Der Verlustrücktrag nach dem Konjunkturstärkungsgesetz 2020, AVR 2020, 117 (117 et seq).
11 S. 124b no. 355 ITA in conjunction with s. 26c no. 76 CITA (BGBl I 2020/96) in conjunction with COVID-19-Verlustberücksichtigungsverordnung (BGBl II 2020/405).
12 See Explanatory Memorandum 287 BlgNR 27. GP, 8.
13 See the next chapter for this 75% offset limit.

The amount of the loss carry-back is variable within the limits because the loss carry-back, in contrast to the loss carry-forward, is designed *per se* as an option that is subject to the taxpayer's application.[14] This right of application also excludes the loss carry-back from being a special expense in the narrower sense, unlike the loss carry-forward. If the application for a loss carry-back is filed, the loss carry-back takes precedence over the loss carry-forward. Losses carried back are not included in the loss carry forward.[15] If a taxpayer incurs a loss in both 2020 and 2019, it is still possible to carry back the loss from the 2020 assessment year to the 2018 assessment period, taking into account the EUR 2 million limit.[16]

For the transfer of the loss carry-back to another taxpayer, the principles for the loss carry-forward apply.[17] In contrast to loss carry-forwards, a transfer of the loss carry-back to the legal predecessor in the case of reorganisations is not permitted.[18] Losses not carried back may, however, be carried forward under the regular loss carry-forward regime.[19]

If a deviating financial year ends in the calendar year 2020, the regulations on the loss carry-back can alternatively be applied for the years 2019/20 or 2020/21.[20] The option to carry back the loss from the 2020 assessment or from the 2021 assessment indicates a certain advantage for companies with a deviating financial year: Depending on the advantage, taxpayers can choose for which business year they apply the loss carry-back.

In the case of group taxation, the loss carry-back can only be taken into account by the group parent in respect of the consolidated group income.[21] This should prevent all group members' 2019 or 2018 assessments from having to be rolled up again.[22] The maximum amount results from the number of group members with unlimited and limited tax liability plus the group parent.[23]

Liquidation losses determined in accordance with section 19 CITA are excluded from the carry-back of losses in order to meet the objective of strengthening companies in crisis.[24] Income which is subject to CFC legislation (section 10a CITA) must be taken into account when calculating the loss carry-back.[25]

The introduction of a temporary loss carry-back was the most significant reactive measure of the tax legislator to the COVID-19 crisis in terms of tax policy. The loss carry-back can lead to positive liquidity effects in a very short time and is to be welcomed from a tax policy perspective. However, the legal anchoring in the transitional provisions of the ITA

[14] See, e.g., Klokar/Postlmayr, Zweifelsfragen zum Verlustrücktrag und zur COVID-19-Rücklage, SWK 2021, 394 (395 et seq).

[15] See e.g., m.no. 4507a of the guidelines on the ITA of the ministry of finance (hereinafter referred to as EStR 2000).

[16] See, e.g., Geweßler/Uedl, Verlustrücktrag iSd KonStG 2020, ÖStZ 2020, 537 (542).

[17] S. 18 para. 6 ITA in conjunction with s. 8 para. 4 no. 2 CITA.

[18] Critically on this question Klokar/Loibl, Verlustvortrag und Verlustrücktrag im Erbfall, AVR 2021, 123 (128 et seq).

[19] S. 18 para. 6 ITA in conjunction with s. 8 para. 4 no. 2 CITA.

[20] S. 124b no. 355 lit b ITA and s. 3 COVID-19-VerlustberücksichtigungsVO.

[21] Further special rules for group taxation can be found in s. 26c no. 76 CITA. For further details see also Knesl/Knesl/Uedl, Der KStR-Wartungserlass 2021: Ausgewählte Änderungen der KSt-Richtlinien (Teil 1), ÖStZ 2022, 88 (90 et seq).

[22] Explanatory Memorandum ErlRV 287 BlgNR 27. GP, 9.

[23] See, e.g., V. Bendlinger/Klokar, COVID-19-bedingte Maßnahmen im Unternehmenssteuerrecht, ecolex 2021, 390 (394).

[24] See m.no. 475an of the guidelines on the CITA of the ministry of finance (hereinafter referred to as KStR 2013).

[25] See KStR 2013, m.no. 475ap in conjunction with m.no. 475af.

and CITA made it clear from the beginning that the loss carry-back would only temporarily remain within the Austrian direct tax legislation. A permanent possibility to carry back losses would be desirable, especially as a measure to balance out the difficulties of assessing the tax for each period independently.[26] In certain cases, the lack of a carry-back possibility can in fact lead to the disappearance of losses that have not been offset.

1.2.3. *Loss carry-forward*

The Austrian CITA provides for an unlimited loss carry-forward for corporations in an overall loss-making situation. The design of the loss carry-forward for corporations is primarily derived from section 18 paragraph 6 of the ITA. Losses incurred in the previous calendar year are deductible as special expenses *sui generis* under the conditions specified therein: The ability to carry forward losses is limited to business income.[27] In addition, the ability to carry forward losses requires a determination of profits based on proper profit determination.[28] The loss carry-forward can be carried forward for an unlimited period of time.[29] It differs from the other special expenses in that there are no "expenses", which is why it is also separated from the other special expenses in terms of the legal system.[30]

The loss carry-forward is to be carried out *ex officio* in the year in which the total amount of income after deduction of special expenses shows a positive value for the first time.[31] Existing loss carry-forwards must be offset as soon as possible.[32] Unlike the loss carry-back, the loss carry-forward does not allow the taxpayer to choose when to make use of it.[33] If the loss carry-forward has not been realised despite offsetable positive income, the loss carried forward is reduced by the amount by which it could have been offset against positive income.[34]

Historically, the loss carry-forward is based on the goal of taxation of a multi-year average income.[35] The loss carry-forward still has this compensatory function today and mitigates – also as an expression of the ability-to-pay principle in personal income tax law – the effects of the periodicity principle. It serves as a necessary supplement to the determination of profits for the realisation of the objective net principle and is considered to break through the principle of sectional taxation.[36] In the literature and case law, the

[26] See with more arguments e.g., Renelt, Der Verlustrücktrag – Ein dauerhaftes Instrument auch für die Zukunft! ÖStZ 2021, 350 (350 et seq).

[27] VwGH 22 April 2004, 2004/15/0043.

[28] On constitutionality VfGH 3. March 1987, VfSlg 11.260; 10 December 1992, B 227/91, VfSlg 13.295; 26 February 1996, B 370/95, VfSlg 14.406.

[29] See, e.g., Kirchmayr, in Achatz/Kirchmayr (eds.) KStG (2011) § 8 m.no. 535.

[30] See, e.g., Raab/Renner, in Lachmayer/Strimitzer/Vock (eds.) Die Körperschaftsteuer (2019) § 8 m.no. 1348.

[31] VwGH 27 June 2018, Ra 2016/15/0072; 20 September 1977, 937/77.

[32] See, e.g., Ressler/Rohm, in Kofler/Lang/Rust/Schuch/Spies/Staringer (eds.) KStG, 3rd edition (2022) sec. 8 m.no. 240.

[33] See, e.g., BFG 26 May 2020, RV/2101092/2019.

[34] VwGH 27 June 2018, Ra 2016/15/0072; 19 September 2013, 2012/15/0014; 20 September 1977, 931/77; see also BFG 23 December 2016, RV/6100138/2015; 25 July 2018, RV/5101244/2014.

[35] For more on the history of the loss-carry forward see Taucher, Erbschaften und Ertragsteuern (1991) 138 et seq. with further references; see also Schimetschek, Ist der Verlust nach § 10 Abs. 1 Z. 5 EStG vererblich? ÖStZ 1966, 37 (38).

[36] See Hohenwarter, Verlustverwertung im Konzern (2010) 158 et seq.

loss carry-forward is thus also seen as a tool to come closer to the idea of the total income period and to overcome the narrow limits of calendar year taxation.[37] In principle, it can only be claimed by the (legal) person who actually generated the loss (*Personenidentität*).[38] Exceptions to the entitlement to carry forward losses exist in the area of the Reorganisation Tax Act (UmgrStG) as well as in the context of inheritance (also applies to corporations), if the legal successor has taken over the business causing the loss at book values.[39]

For corporations, the overall amount of deductible losses carried forward is, however, limited to 75% of the corporation's total amount of income.[40] This leads to a "minimum amount" of 25% of the generated income subject to tax in the year the income is realized. Losses that cannot be compensated in a given year can, however, be carried forward to future years.[41] While this limitation was abolished for the taxation of natural persons with the AbgÄG 2014, it remained in force for corporations, which can probably only be explained by budgetary considerations.[42] However, the offsetting limit does not apply to certain preferentially treated profits (e.g., liquidation profits or profits from the sale or termination of businesses).[43]

As the loss carry-forward is designed without any monetary or time limitation, there were also no changes in response to the Covid-19 crisis. However, there was the aforementioned introduction of the temporary loss carry-back as a supplement to the loss carry-forward.

1.2.4. *Losses after the end of a business*

When a corporation has reached its end of life (for whatever reason), the legal consequences of liquidation taxation pursuant to section 19 CITA take effect. This provision is strongly characterised by the idea of final taxation.[44] The liquidation or winding up of a corporation is regularly the last possibility for capturing the hidden reserves in the assets of a corporation. A liquidation profit is the profit realised in the period of liquidation resulting from the comparison of the liquidation final assets and the liquidation initial assets.[45] For this taxation regime, a special extended taxation period is provided (generally up to three years or in insolvency cases up to five years) to replace the ordinary taxation period (one year).[46] Hence, positive and negative results of the individual financial years are aggregated during the extended taxation period. The aggregation of the results of several financial years can therefore lead to a *de-facto* loss carry-back during the extended taxation period, because

[37] See Stoll, Rentenbesteuerung (1979) 476; Hohenwarter-Mayr, Rechtsnachfolge im Unternehmenssteuerrecht (2019) 871; VwGH 15 September 2016, Ra 2015/15/0003.

[38] See Raab/Renner, in Lachmayer/Strimitzer/Vock (eds.) Die Körperschaftsteuer (2019) § 8 m.no. 1351; VwGH 9 January 1959, 802/55; see also VwGH 4 December 1978, 1496/77, 3171/78.

[39] See for this in detail Klokar/Loibl, AVR 2021, 123 (123 et seq.); see also VwGH 25 April 2013, 2010/15/0131, 2011/15/0143; 15 September 2016, Ra 2015/15/0003.

[40] S. 8 para. 4 no. 2 CITA in conjunction with s. 18 para. 6 ITA.

[41] S. 8 para. 4 no. 2 (c) CITA; see also VwGH 25 November 2009, 2007/15/0252.

[42] Critically on that, e.g., Raab/Renner, in Lachmayer/Strimitzer/Vock (eds.) Die Körperschaftsteuer (2019) § 8 m.no. 1361.

[43] See, e.g., Ressler/Rohm, in Kofler/Lang/Rust/Schuch/Spies/Staringer (eds.) KStG, 3rd edition (2022) sec. 8 m.no. 241b.

[44] See, e.g., Hristov, Die Liquidation im Ertragsteuerrecht (2011) 3.

[45] S. 19 para. 2 CITA.

[46] S. 19 para. 3 CITA.

negative results from later financial years can be aggregated with positive results from earlier financial years.[47] Otherwise, as already mentioned above, a loss carry-back is not available in Austrian law beside COVID specific legislation.

Losses incurred during the liquidation procedure at the level of the liquidated corporation cannot be offset against capital gains at the level of the shareholders.[48] Also, existing loss deductions of the disappearing corporation cannot be transferred to the shareholder due to the personal nature of the loss deduction.[49]

In a loss situation after the end of business, there are no specific carry-back provisions besides the general liquidation taxation regime. It may happen that losses remain disregarded as a loss carry-forward will no longer be possible in the subsequent tax period. In these cases, where the lack of a carry-back option leads to the loss of unrealised losses there should be a – at least limited – carry-back option. So far there have been no indications (not even in the context of the crisis) to change this.

1.2.5. *Transfer of losses in reorganization schemes*

With the introduction of the Reorganization Tax Act (RTA) in 1991 which came into force in 1992 to allow tax-free reorganizations, the treatment of losses in reorganization schemes was also regulated ("change of corporate identity").[50] Depending on the reorganization scheme there are several legal provisions concerning the treatment of losses, but basically, they always refer to the main regulation in section 4 RTA, which deals with the transfer (by the transferor) and the preservation (by the transferee) of loss-carry forwards in corporate mergers. The following explanations are limited to the basic principles.

In principle, the loss carry-forward is linked to the economic identity of the taxable entity suffering the loss in the Austrian CITA. However, in the case of mergers following the RTA, generally, a loss carried forward of the transferring corporation can be transferred to the acquiring corporation.[51] The succession of losses is linked to the transfer of the book value of the loss-producing source of income (Grundsatz des objektbezogenen Verlustvortragsübergangs; 'principle of the object-related transfer of losses carried forward'). Fundamentally, this is also true in the case of conversions, transfers of assets and divisions.[52] Nevertheless, the law also provides for a number of restrictions to this "transition of loss deduction" (e.g., to avoid multiple deduction of the same losses).[53] The RTA also contains an extension of the change of control rules in the context of mergers, conversions, transfers of assets and divisions (see section 1.2.7). For the purpose of the RTA, a harmful change of control also exists if the significant changes to the financial, organizational and economic

[47] See Gaier, Der Verlustrücktrag' im österreichischen Steuerrecht, SWK 1979, 87 (87 et seq.); Peyerl, Körperschaft in Liquidation kann nicht Gruppenträger sein, RdW 2015, 327 (329); Komarek, Liquidations- und Sanierungsgewinnbesteuerung (2016) 115 et seq.

[48] VwGH 22 September 1992, 89/14/0112; UFS 22. September 2003, RV/1404-W/03.

[49] See Hristov, in Kofler/Lang/Rust/Schuch/Spies/Staringer (eds.) KStG, 3rd edition (2022) sec. 19 m.no. 19.

[50] See in detail Hohenwarter-Mayr, Verlustnutzung und Missbrauchsabwehr bei Umgründungen aus österreichischer Sicht, in Hennrichs (ed.) Umstrukturierungen im Steuerrecht (2020) 421 (440 et seq.).

[51] S. 4 Reorganization Tax Act (RTA).

[52] See sec. 10 RTA (conversion), sec. 21 RTA (transfer of assets) or sec. 35 (division).

[53] See sec. 4 no. 1 (a)-(d) and no. 2 RTA.

structure are carried out in part by the transferring entity and in part by the acquiring entity.[54] The aim of the regulation is to prevent the pooling of losses with the profit potential from other economic activities that new shareholders shift to the shell company.

If a merger or any other reorganization is executed outside the applicability of the RTA, and the corporate reorganization is therefore treated as a taxable exchange, losses that can be carried forward will not be transferred to the acquiring corporation, according to the tax authorities.[55]

1.2.6. Group loss compensation (tax consolidation vs. group loss transfer)

The optional group taxation regime allows members of a group to consolidate profits and losses at the level of the group parent.[56] As a result, the group parent is solely liable to pay the tax on the overall income of the group. Accordingly, in an overall loss-making situation, the losses can also only be carried forward to subsequent taxable years at the level of the group parent. The core benefit of the group taxation scheme is obviously the liquidity advantage achieved by the immediate offsetting of profits and losses among several corporate entities that would otherwise be taxed separately.

With respect to resident group members, profits and losses are generally fully attributable under the group taxation regime, regardless of the degree of participation. Regarding losses, there are two limitations: Firstly, losses that a group member accrued before it became part of the group ("pre-group losses") or that were accrued outside the group and transferred to a group member in the course of a reorganization ("extra-group losses"), can solely be offset against the individual profits generated by that group member on a stand-alone basis.[57] Secondly, in order to avoid a double deduction of losses within a group, depreciations of participations in group members and losses from an alienation of such participations are tax neutral.[58]

With respect to a non-resident group member's income, several limitations apply to its calculation, attribution and deduction.[59] Generally, only losses are attributable to the resident parent entity. Such losses are calculated on the basis of both the Austrian tax accounting rules and the rules of the state where the non-resident group member resides. Only the lower of the amounts is attributable in proportion to the holding in the non-resident group member. Moreover, the deduction of losses from foreign group members is limited

[54] See, e.g., Hohenwarter-Mayr, Verlustnutzung und Missbrauchsabwehr bei Umgründungen aus österreichischer Sicht, in Hennrichs (ed.) Umstrukturierungen im Steuerrecht (2020) 421 (449 et seq.).

[55] See m.no. 399 of the guidelines on the RTA of the ministry of finance (hereinafter referred to as UmgrStR 2002); see also VwGH 20 January 2021, Ra 2020/15/0076. See critically on this e.g. with further references Kofler/Six, in Kofler (ed.) UmgrStG, 11th edition (2022) § 4 m.no. 2.

[56] See in detail, e.g., Hohenwarter-Mayr/Zolles, Austrian branch report – Subject 1 – Group approach and separate entity approach in domestic and international tax law, cahiers de droit fiscal international, volume 106, IFA 2022.

[57] S. 9 para. 6 no. 4 CITA.

[58] S. 9 para. 7 CITA.

[59] S. 9 para. 6 no. 6 CITA. A group membership of a non-resident entity requires that more than 50% is held by another group member that is subject to unlimited tax liability in Austria (Sec. 9 para. 2 limb 4 CITA). Losses of subsidiaries of foreign subsidiaries may, thus, not be deducted under the Austrian group taxation regime, except if only Austrian resident corporations directly or indirectly own more than 50 % of ownership interests in the respective sub-subsidiaries (so-called '*second tier limitation*').

to 75% of the total income of all resident group members and the group parent, with the remainder being carried forward at the level of the group parent. The double utilization of such foreign losses is prevented through a recapture system:[60] If the (previously deducted) losses of the non-resident group member can be offset with foreign profits abroad, the amount previously deducted will be added to the group income. This recapture system is supplemented by a "final" recapture in case the foreign group member (economically) leaves the group taxation regime or the group as such is terminated.[61]

The Austrian group taxation regime has also been influenced by case law of the CJEU. Of particular relevance for Austria is the *Papillon* case,[62] where the court has stated that a domestic subsidiary may not be excluded from the tax group solely because it is held by a non-resident group member (so-called 'sandwich situation'). Although the Austrian legislator has not adopted the wording of section 9 of the CITA yet, it is well known that the provision needs to be interpreted in line with this case law. Moreover, pending proceedings before Austrian courts[63] are currently clarifying whether CJEU case law[64] requires the formation of horizontal groups in situations where two or more resident entities are only affiliated by foreign parent entities.[65] Besides the latter case of horizontal group formation, the Austrian group taxation regime goes beyond the requirements of the CJEU by allowing the immediate deduction of foreign losses.

1.2.7. The role of anti-abuse provision (GAARs and/or SAARs) in the context of losses

Besides the GAARs in section 22 FFC[66] and section 44 RTA, there is one SAAR in the CITA in the context of losses: the deduction of losses stemming from previous periods is prohibited, if a qualified and substantial change in the shareholder structure of the company occurs (*Mantelkauf*; change of control rules in case of shell-entities).[67]

This limitation only applies, if (i) a non-gratuitous transfer of a substantial holding in the target company (usually assumed for a change of 75% or more) is accompanied by (ii) changes in the business purpose and (iii) the organizational (as a paraphrase for the management and administration) structure of that company.[68] The changes in these three criteria – that must be fulfilled cumulatively – have to be intrinsically linked.[69] Indirect

[60] S. 9 para. 6 no. 7 CITA.
[61] For further details and in the context of the Marks&Spencer-doctrine of the CJEU see Knotzer/Pinetz, in Kofler/Lang/Rust/Schuch/Spies/Staringer (eds.) KStG, 3rd edition (2022) sec. 9 m.nos. 247 et seq and m.nos. 280 et seq.
[62] CJEU 17 November 2008, C-418/07, *Société Papillon*, ECLI:EU:C:2008:659.
[63] See BFG 31 March 2022, RV/7104573/2020 and the pending procedure at the Supreme Administrative Court (VwGH).
[64] CJEU 14 May 2020, C-749/18, *B and Others*, ECLI:EU:C:2020:370.
[65] See, e.g., Knotzer/Lawson, Die horizontale Unternehmensgruppe im Spannungsverhältnis zwischen nationaler Rechtsgrundlage und Niederlassungsfreiheit, ecolex 2022, pp. 650 et.seq.
[66] AT: Bundesgesetz über allgemeine Bestimmungen und das Verfahren für die von den Abgabenbehörden des Bundes, der Länder und Gemeinden verwalteten Abgaben (Bundesabgabenordnung, BAO) [Federal Fiscal Code].
[67] S. 8 para. 4 no. 2 (c) CITA.
[68] See e.g., Ressler/Rohm, in Kofler/Lang/Rust/Schuch/Spies/Staringer (eds.) KStG, 3rd edition (2022) sec. 8 m.nos. 242 et seq. with further references.
[69] VwGH 26 July 2005, 2001/14/0135.

changes in ownership (in a multi-tier structure) are not covered, as the rule does not provide for a cross-entity perspective.[70] In the case of business restructurings aimed at securing a substantial part of the respective company's existing jobs, the consequences of the change of control rules – disallowance of loss carry-forwards – do not apply ("escape clause").[71]

1.3. Key principles of tax treaty law relevant in case of losses

1.3.1. Profit allocation of PE's (Articles 5 and 7 of the Models)

In the Austrian constitutional system, tax treaties are on the same level as domestic laws and are not considered superior to domestic law. Nevertheless, in the case of normative conflicts between both legal spheres, tax treaty provisions regularly prevail since the tax treaty provisions are generally considered as the more specific ones (*lex specialis*). With respect to losses, it is important to note that neither the OECD MC nor any tax treaty of Austria defines the term 'income' or 'loss' as such. Tax treaties in general do not deal with the determination of 'income' or 'loss'. Thus, tax base determination is a matter of domestic law. However, the 'income' to which a tax treaty applies is defined by the sum of all distributive rules; and since article 21 OECD MC refers to 'Other income', tax treaties cover every source of 'income' that is taxable under a tax covered[72] by the respective treaty. Although the distributive rules do not explicitly refer to deductions, costs, expenses and losses, it has always been undisputed in case law[73] and literature[74] that the distributive rules also apply to deductions.

Austrian corporate tax law is based on a separate entity approach.[75] Each individual legal entity which is registered[76] or has its place of effective management (POEM) in Austria[77] is therefore considered as an individual taxable subject, irrespective of whether it is affiliated with other entities. However, PEs are not considered as separate taxpayers under the CITA. Austrian unlimited tax liability covers the worldwide income of the respective entity, necessarily including foreign PE income. If, however, a tax treaty assigns the right to tax foreign PE income to another state, the method article obliges Austria as the residence state to eliminate double taxation of the income attributable to PE. Austria's strong preference for the exemption method for business income and the CJEU's case law on PE losses have shaped the development of the rules on loss consideration: Under the exemption method any losses attributable to the PE could not be deducted, because the respective loss would have to be exempt under domestic law. Section 2 paragraph 8 number 3 of the ITA, however, allows deducting "losses that could not have been taken into account abroad". However, the losses of the PE must be determined according to Austrian law and, moreover, are limited by the amount of losses determined under foreign tax law. Consequently, only the lower amount

[70] VwGH 13 September 2017, Ro 2015/13/0007; 15 December 2021, Ro 2019/13/0008.
[71] S. 8 para. 4 no. 2 (c) sentence 2 CITA.
[72] Art. 2 OECD-MC.
[73] See explicitly BFH 16.3.1994, BStBl. 1994 II 801.
[74] Lang, Die Zuordnung von Finanzierungsaufwendungen im DBA-Recht, SWI 1995, pp. 289 et.seq.
[75] In detail see Hohenwarter-Mayr/Zolles, Austrian branch report – Subject 1 – Group approach and separate entity approach in domestic and international tax law, IFA 2022.
[76] S. 26 para. 1 FFC.
[77] S. 1 para. 2 CITA.

of the losses determined under Austrian law and under foreign law may be deducted. Furthermore, foreign losses recognized need to be recaptured in the calendar year in which the respective losses are or could be recognized abroad.[78] Recognized losses from a country with which Austria has not agreed on comprehensive administrative assistance need to be recaptured no later than in the third year after their recognition. By applying this so-called "asymmetrical deduction/reincorporation method" also at issue in the CJEU's *Wannsee*[79] case, it seems that this scheme is in line with the fundamental freedoms, also because no "final recapture" takes place in cases where the foreign permanent establishment is sold or closed.

The same rules apply with respect to the credit method. If the credit method is applied, foreign PE losses are included in the Austrian tax base according to section 2 paragraph 8 number 3 of the ITA. However, a recapture of the losses is obsolete, because the amount of creditable foreign tax decreases anyway when the losses are deducted abroad, eliminating the risk that any losses are deducted twice.[80] Nevertheless, the credit method gives rise to problems in situations where the main entity suffers a loss, because no credit can be granted for foreign taxes attributable to foreign PE income. Finally, the maximum tax credit would amount to zero and Austrian law does not provide for a credit carry-forward.[81]

The taxation of non-resident legal entities (neither registered nor with their POEM in Austria) is governed by section 1 paragraph 3 the CITA defining which legal entities are subject to limited CIT liability. The scope of limited CIT liability is determined by section 21 CITA, again referring to section 98 ITA. Section 98 ITA ties the nexus of limited tax liability for independent services and business income to the existence of a PE.[82] Austrian tax law specifically defines the term PE in section 29 FFC, which only slightly deviates from article 5 of the Models.

With regard to the allocation of profits between the main entity and the PE, domestic Austrian law does not provide for specific rules. Rather, the legal basis for the allocation of profits or losses to the PE are the treaty provisions themselves as provided for in article 7 of the Models. In this respect it is important to note that Austria made a reservation with regard to the AOA "to use the previous version of article 7"[83] which was included in the Model immediately before the 2010 update. Austria endorses neither the AOA nor the changes made in the Commentary in the course of the 2008 update to the OECD-MC. To date, none of Austria's (more than 90) tax treaties contain the AOA and, thus, it has not been implemented in domestic tax laws. Furthermore, Austria's recently concluded treaties, e.g., Japan[84] and UK[85], which were concluded in 2018 and 2019, do not provide for the AOA either.[86] The practical impact of not applying the AOA with respect to loss utilisation is –

78 Sec. 2 para. 8 no. 4 ITA.

79 CJEU 23 Oktober 2010, C-157/07, *Krankenheim Ruhesitz am Wannsee-Seniorenheimstatt*, ECLI:EU:C:2008:588.

80 Nevertheless, there is an interesting situation that might lead to a double deduction of the same loss: Austrian law does not require recapture if a foreign PE that suffered losses is sold before it returned to being profitable again. In this situation, Austria would allow the deduction of the relevant losses, but there would be a recapture, even if the losses could be deducted once in the future in the country where the permanent establishment is located.

81 However, many authors have claimed to introduce such a credit carry-forward, see i.a. S. Bendlinger, DBA als Rechtsgrundlage für den Anrechnungsvortrag, SWI 2015, 168 et.seq.

82 S. 98 para. 1 no. 2 and no. 3 ITA.

83 OECD-MC on art. 7, para. 96.

84 Federal Law Gazette (BGBl III) 2018/167.

85 Federal Law Gazette (BGBl III) 2019/32.

86 In detail on Austria's position on the AOA, see Bendlinger, Die Betriebsstätte – 4th edition (2020) p. 439.

above all – the fact that a loss in the main entity prevents that profits are attributable to a PE of the same entity. Since the AOA presumes the PE to be a separate entity, a PE might be attributed a profit, even though the total income of the main entity is negative.

By closely following the OECD practice before the 2010 update, Austria sticks to the principles of profit allocation as laid down in article 7 paragraph 2 and 3 OECD MC 2008. According to article 7 paragraph 2 OECD MC 2008 the profits are to be allocated to a PE as "if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment". Finally, complementary to paragraph 2, the third paragraph of article 7 OECD MC 2008 is of particular relevance for the allocation of losses and expenses: "In determining the profits of a permanent establishment, there shall be allowed as deductions expenses which are incurred for the purposes of the permanent establishment, including executive and general administrative expenses so incurred, whether in the State in which the permanent establishment is situated or elsewhere". Austria, thus, allows to allocate expenses to a PE, irrespective of whether the expenses occurred in the head-office, the PE itself or in a third state PE. This also applies to so-called "*overheads*" (these are "*executive and general administrative expenses*" as stated in article 7 paragraph 3 OECD MC 2008). However, it is important to note that article 7 OECD MC 2008 does not limit contracting states to apply domestic deduction limitations. Whether a specific expense or loss is deductible, finally depends on domestic (Austrian) rules of base determination.[87]

Austria's policy of respecting international law, as well as its membership in the EU, has meant that Austria has always strived for non-discriminatory tax legislation. The latter, in particular, has shaped the principles governing the taxation of PEs: Section 21 paragraph 1 numbers 2 and 3 CITA provides for specific rules for PEs of non-resident corporations clarifying that, with regard to the determination of income and losses, the same rules as for resident corporations apply. Thus, also with respect to losses, the CITA does not treat PEs worse than resident corporations in principle.

For this reason, section 102 of the ITA also allows the carry-forward of losses attributable to PEs of non-resident corporations, as is the case for resident corporations. However, to avoid multiple deduction of the same loss, the loss carry-forward for the PEs is limited pursuant to section 102 paragraph 2 number 2 of the ITA in three respects:

- (1) the deduction is only allowed with respect to the domestic PE;
- (2) the PE losses are to be primarily offset against foreign profits of the non-resident corporation, and
- (3) the deduction according to the last sentence of section 102 paragraph 2 number 2 of the ITA requires that the domestic loss exceeds the non-resident corporation's total profits.[88]

Although Austria's tax policy is geared towards avoiding discrimination, section 102 paragraph 2 number 2 of the ITA has given rise to interesting questions in connection with the fundamental freedoms and the PE non-discrimination prohibition in article 24 paragraph 3 of the Models. In particular the last limitation (3) has been subject to intense

87 Comprehensively, see Bendlinger, Die Betriebsstätte – 4th edition (2020) pp. 368-369.

88 Marschner in Kanduth-Kristen/Marschner/Peyerl/Ebner/Ehgartner, Einkommensteuergesetz Kommentar – 15th edition (2022) s. 102 para. 13.

and convincing criticism in literature. In light of the CJEU's case law,[89] it was assumed that the freedom of establishment – if applicable – "suppresses" the effects of the last sentence of section 102 paragraph 2 number 2 of the ITA.[90] Recent case law has clarified that this limitation also violates treaty-based PE non-discrimination provisions.[91] The third limitation can, thus, also be ignored with respect to non-EU resident corporate taxpayers, if the respective treaty with a third country includes a PE non-discrimination prohibition. With respect to the other two limitations, tensions with non-discrimination seem to be more subtle. Only the first limitation (1) might very well give rise to discrimination issues, due to the fact that the Austrian tax administration seems to deny the deduction of losses among PEs of the same entity.[92] This question has, however, as far as can be seen, not been addressed by courts yet.[93] Furthermore, it has been argued that the limitation to domestic losses might be discriminatory in cases where domestic law denies the existence of a PE whereas a PE exists under the treaty.[94] Only the second (2) limitation seems to clearly be non-discriminatory, because domestic corporations are also obliged to deduct losses as soon as possible (see section 1.2.3).

1.3.2. *Profit/loss recognition in relation to foreign subsidiaries (Art 7 and 13 of the Models)*

Since Austria follows a separate entity approach, there is no possibility to offset losses of corporate subsidiaries directly, besides the immensely important exception with regard to Austria's tax group consolidation addressed in section 1.2.6. Only losses of foreign entities treated as a disregarded entity, partnership or other flow-through entity can be recognized, because they are considered as fiscally transparent under Austrian tax laws. Nevertheless, losses of corporate subsidiaries are reflected in impairments, which can be written off within seven years according to section 12 paragraph 3 of the CITA, provided the impairment is not caused by a distribution made to the parent entity. The same applies if a participation in a subsidiary is sold with losses. The indirect deduction of losses is only prohibited within tax groups.[95]

However, this does not apply to participations in non-resident corporations where more than 10% ownership interest is held for more than ten years: According to section 10 paragraph 3 of the CITA any profits or losses from the sale of such qualified participations or from their impairments are tax neutral. Any changes in value or profits or losses from the sale of a participation are, thus, ignored for tax purposes. For this reason, as a rule, Austrian

[89] In particular CJEU 23 Oktober 2010, C-157/07, Krankenheim Ruhesitz am Wannsee-Seniorenheimstatt, ECLI:EU:C:2008:588.

[90] For comprehensive reference to literature, e.g., Moldaschl in Kofler/Lang/Rust/Schuch/Spies/Staringer (eds.), Körperschafsteuergesetz Kommentar – 3rd edition (2022) s. 21 para. 119.

[91] VwGH 16 February 2006, 2005/14/0036 and VwGH 28 November 2007, 2007/14/0048.

[92] See the information provided by the Austrian Ministry of Finance (so called "Express Answer Service"), where the Austrian authorities state that it is not permissible to offset losses against profits received in a different Austrian PEs (in these cases construction sites) of the same foreign corporation, see Austrian Ministry of Finance, Deutsche Unternehmen mit verlust- und gewinnbringenden Inlandsbaustellen (17. 07. 2000), EAS 1690, GZ. P 8/13-IV/4/00; and Austrian Ministry of Finance, Verlustvortragsproblematik bei sukzessiven Baubetriebsstätten (23 July 2001), EAS 1880, GZ. K 892/1-IV/4/01.

[93] Oberrader, Der Verlustabzug und das Betriebsstättendiskriminierungsverbot, SWI 2021, pp. 73 et.seq.

[94] Haslehner, Betriebsstättendiskriminierungsverbot (2009) pp. 325 et.seq.

[95] S. 9 para. 7 CITA.

law does not provide for an indirect deduction of losses from foreign subsidiaries. However, section 10 paragraph 3 of the CITA allows opting against tax neutrality of changes in value and capital gains to enable the indirect recognition of foreign subsidiaries' losses. In this case section 12 paragraph 3 CITA applies, which in turn requires the losses deduction to be spread over seven years. The option is only available in the year the acquisition of the participation has been made; it can neither be made nor revoked at a later date and, thus, contains a speculative element.

The case law of the CJEU did indeed impact Austrian rules on cross-border losses of subsidiaries, but mainly with regard to group taxation as addressed in section 1.2.6.

Part Two: Utilization of losses for tax planning

2.1. General overview

Austrian corporate tax law is very developed and, with the RTA already in force in 1992, contains a very progressive and abuse-proof legal framework which, on the one hand, enables tax-neutral reorganisations, but, on the other hand, also prevents artificial shifting of losses to a large extent. Various amendments to the ITA, CITA and RTA as well as existing case law on corporate tax and reorganisation tax law over the past decades have contributed to the fact that mass dissemination of loss shifting schemes is hardly possible. Both the CITA and RTA provide for numerous SAARs addressing losses.[96] The most important SAAR with respect to losses is laid down in section 8 paragraph 4 number 2 letter c CITA, denying loss deduction, when the ownership structure as well as the economic and organizational identity of a corporate taxpayer are changed significantly (see in detail section 2.4). The RTA regularly refers to this provision and states that it has to be applied also in the course of reorganisations.[97] In addition, section 22 FFC as well as section 44 RTA provide the tax administration with GAARs which – if the SAARs are not applicable in a particular case – may render a particular undertaking harmless from a fiscal perspective. The ambit of GAARs is, however, very indeterminate. For convincing reasons, the literature fears that the Austrian GAAR is in tension with the constitutional rule of law (also see section 3.8).[98]

Besides GAARs and SAARs, Austrian tax law follows the principle of 'substance over form', which is vaguely phrased in section 21 et. seq. of the FFC. As a consequence, the lack of economic substance cannot be hidden by means of financial instruments construed to deliberately shift losses to different taxpayers. However, firstly, the substance over form principle is a very undetermined principle and secondly, it is undisputed that no tax legislation, no matter how far developed, can eliminate tax planning completely. Rather, it is a legitimate interest of corporations to make use of the leeway granted to them by the tax laws, as long as the law is not violated. Nevertheless, as will be seen, such schemes seem to be a rare phenomenon in Austria due to comprehensive deduction limitations and extensive anti-abuse legislation. Even COVID specific tax regimes did not change anything in this respect.

[96] See, e.g., s. 8 para 4 no. 2 letter c CITA.

[97] S. 4, 10, 21, 35 RTA.

[98] Laying the foundation for extensive Austrian literature, see Gassner, Der Gestaltungsmißbrauch im Steuerrecht – Änderung der Rechtsprechung? ÖStZ 1981, pp. 262 et.seq.

2.2. Schemes shifting profits to a loss-making party

In Austria schemes to shift profits to loss-making parties are difficult to implement, due to the fact that, as a rule, the transfer of assets leads to a realisation of hidden reserves. It is only possible to shift assets among different corporate taxpayers without being obliged to realise gains, if the RTA can be applied. Furthermore, Austrian corporate tax law is highly sensible with regard to transactions between related parties: According to section 8 paragraph 2 CITA every monetary value that is distributed to an entities' shareholders, irrespective of whether it is an open or concealed distribution, does not lower the CIT base. This is a consequence of the CITA's separate entity approach and requires compliance with the arm's length principle for every transaction between related entities. Corporate taxpayers, thus, cannot simply shift income streams among them. Rather, the Austrian CITA even prohibits the deduction of losses within a single corporate taxpayer, if its identity changes due to a modification of the ownership and organizational structure of the respective entity.[99] Furthermore, section 12 CITA contains numerous deduction limitations, in particular with regard to interest and royalty payments, which limit the applicability of such schemes.[100] Additionally, section 12a CITA contains a deduction limitation for interest payments ("interest barrier" – see already section 3.1).

2.3. Schemes circumventing time restriction on the carry-over of losses

Austrian corporate tax law allows the carry-over losses without any time limit. Thus, there is no need to circumvent any time restrictions.

2.4. Schemes circumventing change of ownership/activity restrictions on the carry-over of losses

As has already been discussed in section 1.2.3, the CITA allows the deduction of losses of an entity without further requirements and time limits. Of course, these generous rules also allow for tax planning arrangements and enable deducting losses, even in situations that lack economic substance. Starting in the early 1990s the Austrian legislator took notice of schemes, where empty shell entities were sold to new shareholders that changed the business but could still use the losses which were aggregated by the entity over previous years or sometimes even decades. Due to the fact that the respective entities had not transferred any assets and did really suffer the respective losses, the CITA 1988 did not initially impose any limitations on the loss reduction in this respect. However, in 1992 the Austrian tax legislator introduced section 8 paragraph 4 number 2 letter c CITA to restrict the loss deduction outside economically justifiable cases when the ownership structure as well as the economic and organizational identity of an entity are changed (in detail on the provision, see section 1.2.7). The CITA thus prevents accumulated losses and loss carry-forwards from becoming tradable assets.[101]

[99] S. 8 para. 4 no. 2 letter c CITA.

[100] See in particular s. 12 para 1 nos. 9 and 10 CITA.

[101] Ressler/Rohm in Kofler/Lang/Rust/Schuch/Spies/Staringer (eds.), Körperschafsteuergesetz Kommentar – 3rd edition (2022) s. 8 para. 242.

2.5. Incorrect application of transfer pricing rules

Transfer pricing has already been identified as a major point of concern with regard to shifting losses in the course of the OECD's report on losses published in 2010.[102] In this respect, it is important to note that Austrian law does not provide for any specific rules specifying the arm's length principle. Rather, only the Austrian tax administration publishes the non-legally-binding so-called Austrian Transfer Pricing Guidelines ('Verrechnungspreisrichtlinien'), which were subject to a major revision in 2021 (see in detail section 3.2) and closely follow the OECD-TPG 2017. Thus, Austrian tax practice strongly commits to the templates provided by the OECD, also regarding transfer pricing. In addition, the correct application of international transfer pricing rules has long been an important focus of tax audits in Austria. Above all, the Austrian Transfer Pricing Documentation Act ('Verrechnungspreis-dokumentationsgesetz' in short VPDG)[103] requires comprehensive transfer pricing documentation as part of Country-by-Country Reporting (CbC-Reporting, in detail see sections 3.1 and 3.7) for companies with an annual turnover of more than EUR 750 million. The information gained in the course of the CbC-Report is to be shared with other EU tax administrations.[104] For this reason, standardized transfer pricing schemes to shift losses do not exist.

2.6. Schemes planning around rules on the recognition or treatment of losses

The Austrian rules on the recognition of losses, whether within the standard rules of the CITA or the group taxation regime provided in section 9 CITA, are quite generous and only provide for very few limitations. Thus, standard schemes to plan around rules on the recognition or treatment of losses rarely occur. There are only specific limitations to the use of losses with regard to pre-group losses[105] and with regard to the use of losses suffered by foreign subsidiaries within Austria's group taxation regime (see section 1.2.6). However, the rules are very straightforward and do not provide for much tax planning leeway. There is indeed a scheme to deliberately avoid the 'second tier limitation' on the realisation of losses of foreign group entities.[106] Section 9 CITA only allows inclusion of foreign subsidiary losses into the group taxation if a resident group member holds more than 50 % of the ownership interests. The scheme addressed above includes two foreign group members holding 50 % each in a sub-subsidiary. In this case, the second-tier limitation would not apply to the sub-subsidiary, simply due to the fact that none of the foreign group members hold more than 50 % in the sub-subsidiary. Nevertheless, this is in line with the purpose of section 9 CITA and has been found harmful by neither administrative practice nor the courts so far.

[102] OECD, Guidance on the transfer pricing implications of the COVID-19 pandemic (2020).
[103] Federal Law Gazette (BGBl I) 77/2016.
[104] S. 11 Transfer Pricing Documentation Act (VPDG).
[105] S. 9 para. 6 no. 4 CITA.
[106] On this scheme, see *Mayr/Bodis/Lachmayer* in *Doralt/Ruppe*, Steuerrecht – Band I (2019) para. 944.

2.7. Schemes creating artificial losses

Artificial losses occur if a taxpayer succeeds in generating deductible expenses with no economic loss incurred. The OECD has investigated the phenomenon of artificial losses, and, in particular, identified schemes where (i) expenses were generated in connection with tax exempt income by way of financial instruments, where (ii) intra-group sales of shares were financed by loans granted by and to related parties and where (iii) artificial goodwill write-offs were created by means of reorganizations.[107] All of these schemes cannot be implemented without violating Austrian law: The CITA denies deduction for any expenses related to tax exempt income, capital gains or derivates.[108] However, there is one exception to the latter rule: Interest paid for financing costs of participation is deductible, even if the dividends arising from the participation are tax exempt.[109] However, even in this case, deduction of interest might be prevented by the Austrian "interest barrier" in section 12a CITA, due to the fact that exempted dividend income is not included within the tax EBITDA and, thus, reduces the amount of deductible interest.

Furthermore, there is a specific prohibition for the deduction of interest payments to finance intra-group sales of shares.[110] The artificial creation of goodwill is also not an issue, because, if the RTA is applied, goodwill cannot occur due to the obligation to assess transferred assets at their carrying values. If the RTA is not applied, goodwill could be generated, however, it would need to be realised and taxed at the standard rate.[111]

Finally, an artificial loss might occur if a company relocates to Austria: Section 6 paragraph 6 ITA provides for a "step-up" to the market value with respect to assets and liabilities that are allocated to Austria. If, e.g., an asset is reallocated to Austria, and has a higher book value than market value, an artificial (unrealized) loss arises. Nevertheless, this is not problematic: Again section 8 paragraph 4 number 2 letter c CITA prevents loss utilisation, if the ownership structure as well as the economic and organizational identity of an entity are changed. The transferred losses can, thus, only be used if the relocation does not change the overall identity of the corporate taxpayer.

2.8. Schemes involving the dual/multiple use of the same loss

The CITA, as well as the RTA, contains various mechanisms to prevent multiple loss deduction. In section 14 CITA the hybrid mismatch rules of articles 9 and 9a ATAD are implemented. Among other things, the provision specifically addresses situations in which the same deductions could be made more than once ('double-dip'). In these situations, section 14 paragraph 7 CITA denies the deduction of such expenses. This includes, for example, schemes involving dual-resident companies, PEs and double-dip leases. With regard to reorganizations, the RTA specifically addresses situations in which the same loss is deducted twice, e.g. by deducting losses of previous subsidiaries indirectly via impairments and additionally deducting them directly after an upstream merger. In this case, the RTA

[107] See the Chapter on "Schemes creating artificial losses" in OECD, Corporate Loss Utilisation through Aggressive Tax Planning (2010), pp. 55-56.

[108] S. 12 para. 2 CITA.

[109] S. 11 para. 1 no. 4 CITA.

[110] S. 12 para. 1 no. 9 CITA.

[111] Sec. 6 no. 14 ITA and sec. 20 CITA.

requires that any carried forward losses are reduced by the impairments made by the parent entity.[112]

Since double consolidation of the foreign group member leads to subsequent taxation (or non-recovery) of the foreign loss, Austrian law also explicitly tackles potential double or multiple loss deduction in the course of its group taxation regime. However, interestingly, there is no rule against double consolidation of the group parent in Austria and abroad. Section 14 paragraph 7 CITA does not cover this situation either.[113] Thus, if an Austrian group parent is consolidated within a group taxation regime abroad, Austrian law does not exclude loss deduction, even if the losses could potentially be deducted in a different state as well.

Since Austrian corporate law allows the creation of partnerships that provide for limited liability under civil law for the partners but are, nevertheless, considered fiscally transparent under Austrian tax laws (so-called 'Kommanditgesellschaften' – 'Limited Partnerships' or 'Stille Gesellschaften' – 'Silent partnerships'), there had been schemes involving such partnerships to shift losses to profit making corporate taxpayers (so-called 'Verlustbeteiligungsmodell' – in English 'loss participation schemes'). Finally, so-called "loss-participation" regimes occurred, where certain taxpayers bought participations in loss making partnerships – still enjoying limited liability under civil law – but could reduce their ITA burden by offsetting losses of the loss making partnership. However, the Austrian tax legislator soon recognised that such schemes involving partnerships are undesirable from a tax policy perspective and introduced comprehensive rules to limit the use of partnership losses.[114] According to section 23a and section 27 paragraph 8 number 2 ITA any losses incurred by partners may neither be deducted from other income schedules nor be carried forward. Rather, the respective loss can only be deducted in subsequent profits gained from the same participation. The partners, thus, can only use the losses, if the same participation finally leads to a profit in future years.

Part Three: Impacts of BEPS on the treatment of losses

3.1. General overview

The implementation of BEPS recommendations in Austria was carried out primarily through the implementation of the European Anti-Tax Avoidance Directive (ATAD)[115] and the Directive on Administrative Cooperation (DAC).[116] The ATAD aims at tackling aggressive tax planning and avoidance in the context of a common internal market and contains five anti-avoidance measures that Austria, as an EU member state, had to introduce into domestic laws, namely, an interest limitation rule (article 4 ATAD; section 12a CITA), exit taxation (article 5 ATAD), a general anti-abuse rule (article 6 ATAD; section 22 FFC), CFC rules (articles

[112] Sec. 4 no. 1 letter d RTA.

[113] Contrary, section 14 paragraph 1 number 5 of the German CITA explicitly denies loss deduction at the level of the group parent, if the losses may be deducted in another state either by the group parent or a different taxpayer.

[114] See sec. 23a ITA and sec. 27 para. 8 no. 2 ITA.

[115] 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, L 193/1 of 19 July 2016.

[116] Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation and repealing Directive 77/799/EEC, L 64/1 of 11 March 2011.

7 and 8 ATAD; section 10a CITA) and an anti-hybrid rule (article 9 and 9a ATAD; section 14 CITA). Furthermore, the DAC regulates procedural and administrative issues with regard to tax matters and has regularly been amended in the course of the OECD BEPS Project. For example, the EU implemented both BEPS Action 12 on mandatory disclosure rules and Action 13 on Country-by-Country Reporting (CbC-Reporting) by way of the 3rd (DAC4)[117] and 5th (DAC6)[118] amendment of the DAC.

From the authors' perspective, possible schemes encouraging the shifting of losses in a cross-border context were neither primarily on the agenda of the European nor the Austrian legislator after the BEPS recommendations. In Austria, many provisions to prevent the abusive use of losses for tax planning purposes were already in place before the BEPS project (e.g., change of control rules).

3.2. Transfer pricing

3.2.1. BEPS Actions 8-10

Austria's transfer pricing practice is heavily influenced by its membership of the OECD. When the OECD first published the OECD-TPG in 1995, the tax administrations of Austria and Switzerland coordinated to publish a German translation. In the course of the 2010 update of the OECD-TPG, the Austrian administration decided to publish its own guidelines (so-called "Verrechnungspreisrichtlinien 2010 – VPR 2010[119]). When the Final Reports on BEPS Action 8-10 were published and incorporated into the OECD-TPG 2017, the Austrian tax administration decided to revise its guidelines and, in October 2021, published a recast to the Austrian Transfer Pricing Guidelines 'VPR 2021' replacing VPR 2010.[120] However, it seems that the VPR 2021 did not change Austrian tax practice with regard to losses.

3.2.2. Transfer Pricing implications of the Covid-19 pandemic in relation to losses

3.2.2.1. Comparability analysis

There is consensus in the Austrian literature that, even in times of crisis, the arm's length principle should be used as a benchmark for comparability analysis.[121] However, as the OECD-TPG 2017 note, "an independent enterprise would not continue loss-generating activities unless it had reasonable expectations of future periods".[122] For this reason, the Austrian Transfer Pricing Guidelines 2010 (widely following the OECD TPG) tended to assume that

117 Council Directive (EU) 2016/881 of 25 May 2016 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation, L 146/8 of 3 June 2016.

118 Council Directive (EU) 2018/822 of 25 May 2018 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements, L 139/1 of 5 June 2018.

119 Austrian Ministry of Finance, VPR 2010, Verrechnungspreisrichtlinien 2010, GZ BMF-010221/2522-IV/4/2010 (28 October 2010).

120 *Ibid*, pp. 1-2.

121 Rosenberger, COVID-19 Fitness für Verrechnungspreissysteme, SWI 2021, p. 232.

122 OECD TPG 2017, Chapter III para. 3.64.

a stable profit share should at least be allocated for routine activities and did not seem to allow for 'loss comparables'; in particular due to the fact, that a diligent businessman will regularly assume that the business will earn profits from an ex-ante perspective. This might, however, be different in a global crisis where many enterprises, also in a predictive analysis, have to accept temporary losses. However, many authors already pointed out at the beginning of the pandemic that, due to COVID, it might be appropriate to assume that also routine activities might give rise to the allocation of losses in certain situations.[123]

3.2.2.2. *Allocation of losses and costs associated with Covid-19*

The Austrian tax administration did not provide for any specific guidance with respect to transfer prices in the course of the COVID-19 pandemic. No COVID specifics have landed in the courts yet either. However, it is reasonable to assume that the OECD's suggestions in the course of the OECD COVID-19 Pandemic Guidance do have a significant impact on Austrian transfer pricing policy: The strong commitment to OECD tax policy indicates that the Austrian tax administration might very well accept the measures proposed by the OECD, if they are reasonably applied. For this reason, losses might be allocated to affiliate entities, if the enterprises can bring reasonable evidence for their transfer pricing policy. The same will be true for COVID-caused renegotiations of contracts or the consideration of force majeure impacts. In any case, it is important that the result does not evidently contravene the arm's length principle. Furthermore, literature is unanimous that, regarding the consideration of Covid-caused special situations, proper documentation of transfer prices is key to bringing evidence in subsequent tax audits.[124]

3.3. Anti-mismatch recommendations

As already pointed out in section 2.8, Austria implemented article 9 and 9a ATAD within section 14 CITA, which specifically addresses double deduction of the same costs and expenses. The rules of section 14 paragraph 2 number 2 and section 14 number 7 CITA apply to all situations where the same loss could be deducted twice. As section 14 only came into force on 1 January 2020, there is no specific case law on the new hybrid mismatch provisions yet.

3.4. CFC recommendations

Austria rejected a CFC regime in the past. The existing instruments in the Austrian tax law were found to be sufficient to counter the tax policy problems of CFC situations.[125] Indeed, even before the implementation of the ATAD, there had been some provisions in

[123] Comprehensively Hahn/Rasslagg, Berücksichtigung von Loss Comparables' bei TNMM-Datenbankstudien – ein (No-) Go? TPI 2019, pp. 351 et.seq.

[124] See S. Bendlinger, Ergebnisabgrenzung bei Betriebsstätten in der Krise, TPI 2021, p. 137.

[125] See, e.g., Gassner, Neun und noch mehr Gründe gegen ein österreichisches Außensteuergesetz, SWI 2001, 295, 295 et seq.

the Austrian tax law that have consequences similar to CFC legislation:[126] in particular the special provisions within the Investment Funds Act[127] (InvFG), namely, sections 186-188; the so-called switch-over method in section 10a paragraph 7 CITA (section 10a paragraphs 4-6 CITA old version) introduced in 1994 (at the time: section 10 para. 3 CITA) and the Austrian general anti-abuse rule (section 22 FFC). In the course of the Annual Tax Act 2018,[128] Austria introduced CFC rules for the first time with the implementation of articles 7 and 8 ATAD. According to section 10a CITA, low-taxed passive income earned via a controlled entity is attributed to the controlling Austrian company, where it is taxed.[129]

Regarding loss situations, section 10a CITA and the CFC Regulation[130] contain limited rules. In practice, however, losses of a CFC company can be of great importance. In these cases in particular, there is considerable legal uncertainty due to the lack of requirements by law and administrative regulations. In particular, questions arise in connection with the calculation of the effective average tax rate ("low taxation"), the *de minimis* limit, the determination and attribution of passive income:[131] It is unclear how facts from previous financial years, such as a possible loss deduction at the CFC or the inclusion of a group member, can influence the assessment of low taxation in a specific financial year. In such a case, there is a strong argument for taking over the loss carry-forwards available under foreign tax law without conversion.[132] The passive income to be included is established in accordance with the Austrian provisions on the determination of profits.[133] This is the same as the procedure for determining income for the purpose of assessing low taxation. When calculating income, positive and negative passive income must be balanced out, but active income cannot be offset against passive income.[134] Therefore, this is a loss compensation within the passive income.[135] No inclusion is made if the determination of passive income in accordance with Austrian rules results in a total loss.[136] The regulation provides a so-called "waiting deferral provision" ("*Wartetastenregelung*") for a surplus of negative passive income.[137] If the negative passive income exceeds the positive passive income, the excess amount can be carried forward and taken into account in subsequent tax periods. However, the loss offset is limited to the passive income of the same controlled entity. The passive income

[126] See, e.g., Auer/Langer, Chapter 4: Austria, in Lang/Owens/Pistone/Rust/Schuch/Staringer (eds) Implementing Key BEPS Actions: Where Do We Stand? (2019) 97, 101.

[127] Bundesgesetz über Investmentfonds (Investmentfondsgesetz 2011 – InvFG 2011) – Federal Law Gazette (BGBl I) 77/2011.

[128] Jahressteuergesetz 2018 (JStG 2018) – Federal Law Gazette (BGBl I) 62/2018.

[129] For a more detailed description see e.g., Klokar/Riedl, Controlled Foreign Company Legislation in Austria, in Kofler/Krever/Lang/Owens/Pistone/Rust/Schuch/Spies/Staringer (eds.) Controlled Foreign Company Legislation (2020) 59-88.

[130] The national regulation (*VO-Passiveinkünfte niedrigbesteuerter Körperschaften*, BGBl II 2019/21) on CFC legislation specifies certain legal provisions of s. 10a CITA in more detail.

[131] For further details see Jann/Mayer, Verluste im Regime des § 10a KStG, in Kirchmayr/Mayr/Schlager/Zöchling (eds.) Handbuch Hinzurechnungsbesteuerung (2020) 63 (63 et seq.).

[132] See, e.g., Klokar, in Kofler/Lang/Rust/Schuch/Spies/Staringer (eds.) KStG, 3rd edition (2022) sec. 10a m.no. 110.

[133] S. 10a para. 5 no. 3 first sentence CITA. This corresponds to the specifications from art. 8 para. 1 first sentence ATAD.

[134] S. 5 no. 2 VO.

[135] See, e.g., Schilcher/Knesl, Die § 10a KStG-VO zur Hinzurechnungsbesteuerung und zum Methodenwechsel im Überblick, RdW 2019, 54, 59.

[136] S. 10a para. 5 no. 3 second sentence CITA; see also Materials on Annual Tax Act 2018, Explanatory Notes to Government Proposal No. 36 26th Legislative Period, 26.

[137] S. 5 no. 2 second sentence VO.

needs to be recorded by the controlling corporation as income from commercial activities as defined in section 23 ITA.[138]

3.5. Limitation of interest deductibility

In 2021, Austria implemented article 4 ATAD and introduced a limitation to the deduction of interest ('interest barrier'). According to section 12a CITA an entity may only deduct interest payments as long as the excess of interest payments over interest income exceeds 30 % of the entities' EBITDA. However, the excess interest that cannot be deducted within a fiscal year may be carried forward without any time limit. Also, the non-used part of the EBITDA (excess amount of 30 % of the EBITDA over the excess interest payments) may be carried forward for a maximum of five years. Furthermore, up to an amount of excess interest payments, an amount of EUR 3 Mio is deductible in any case ('free allowance'). The amount of EUR 3 Mio is, thus, also deductible if the EBITDA is zero or negative, e.g., due to a loss.[139]

Consequently, the impact of losses on the Austrian interest barrier is evident: The higher the taxable loss, the lower the amount of deductible interest. However, due to the fact that the EBITDA is the taxable profits increased by tax effective deduction of assets as well as deductible interest payments,[140] for purposes of section 12a CITA, an overall loss does not necessarily mean that the EBITDA is negative and no interest payments can be deducted; and even if the EBITDA is negative, interest payments are still deductible if, e.g., an entity has carried-forward amounts of non-used EBITDA of previous years.

3.6. Patent boxes

Austria does not provide for a patent box regime. In general, not a single tax incentive of Austria has been listed in the BEPS Action 5 report.

3.7. Mandatory disclosure rules and CbCR

When adopting the DAC6 to implement BEPS Action 12, the EU legislator was very much guided by the hallmarks proposed by the OECD in the Final Report. Consequently, the hallmark on arrangements related to losses mentioned therein is also to be found in Annex IV Part II B 1 of DAC6. According to this hallmark, a disclosure is mandatory if the so-called main benefit test is fulfilled for "[a]n arrangement whereby a participant in the arrangement takes […] steps which consist in acquiring a loss-making company, discontinuing the main activity of such company and using its losses in order to reduce its tax liability, including through a transfer of those losses to another jurisdiction or by the acceleration of the use of those losses". The Austrian legislator has implemented the DAC6 by way of the so-called

138 S. 5 no. 3 VO.

139 Mayer in Kofler/Lang/Rust/Schuch/Spies/Staringer (eds.) KStG, 3rd edition (2022) sec. 12a m.no. 38.

140 S. 12a para. 4 CITA and s. 1 EBITDA-Determination Regulation (as enacted by the austrian tax administration – in german EBITDA-Ermittlungsverordnung, Federal Law Gazette [BGBl II] 390/2021).

EU-Mandatory Disclosure Act ('EU-Meldepflichtgesetz')[141] in which the hallmark addressing losses can be found in section 6 number 4.

The Austrian legislator has implemented the DAC4 adopting BEPS Action 13 by enacting the VPDG (see already in section 2.5) which is very much based on the wording of the directive and obliges MNE Groups to prepare a CbC-Report if their yearly turnover exceeds EUR 750 Mio. According to sections 5 and 6 VPDG in-scope MNE Groups are obliged to prepare a so-called master file including information on the organisational structure of the Group, its business model, its intellectual property, its financial activities and its financial position. Furthermore, a local file, including information on domestic activities, needs to be prepared. Considering the set of information to be reported, there is no doubt that the CbC-Report is quite suitable for identifying the schemes targeted at shifting of losses as described in section 2 of this report. Finally, the CbC-Report could be an additional source of information for local tax authorities to filter harmful tax practices with respect to loss utilisation. Both the master file and the local file include specific information with respect to the business activity of the reporting MNE Group. The master file on the one hand, e.g., shows the organisational structure of a MNE Group and contains – among other information – details with respect to group internal financial activities including identification of business units with significant financial functions within the MNE Group.[142] This information might be a source to identify artificial loss creating schemes, because tax authorities can analyse how losses had been shifted within the different members of the MNE Group. On the other hand, there is the local file where an MNE Group, e.g., has to report paid and received group-internal interest or licence fees and has to disclose copies of group-internal contracts (including for example certain loss-sharing agreements).[143] A focused analysis of the CbC-Report by tax authorities could therefore very well shed light on how losses flowed and were used within a MNE Group. The potential of the CbC-Report to identify loss shifting schemes, however, should not be overestimated, as clever tax planning is not necessarily visible in the sheer volume of the CbC-Report.

3.8. BEPS Action 6 and Principal Purpose Test (PPT)

As an OECD member state, Austria has always been engaged in the development of the OECD Model and the MLI, which Austria heavily supported and already signed in 2017. In the course of the implementation of the MLI several treaties within Austria's tax treaty network have been amended by way of implementing a Principle Purpose Test – short PPT (article 7 MLI).[144] Furthermore, it can be assumed that future Austrian treaties will contain a provision corresponding to article 29 paragraph 9 OECD-MC.

However, the introduction of the PPT is not likely to change much in Austrian tax practice. The Austrian tax administration has held for decades that tax treaties do not prevent the

[141] Federal Law Gazette (BGBl I) 91/2019.

[142] Sec. 5 letter 2 VPDG.

[143] See Sec. 9 letter 2 and 4 VPDG.

[144] On the changes adopted in the course of the MLI, see S. Bendlinger, Das Multilaterale Instrument – eine ernüchternde Bilanz, SWI 2020, pp. 2 et.seq.

application of the domestic GAAR enshrined in article 22 FFC.[145] Furthermore, the latter provision has been subject to extensive debate in literature whereby the prevailing view is, for good reasons, fundamentally sceptical of GAARs.[146] In recent times, Austrian courts, including the Supreme Administrative Court having jurisdiction in tax matters, tended to avoid reference to the vague concepts of GAARs but rather, solved potentially "abusive" cases through interpretation of the tax provisions at issue.[147] Finally, as the said decision of the Supreme Administrative Court shows, many potential cases of abuse can already be solved by addressing the question of income allocation. In any case, the Austrian corporate tax and reorganization tax laws provide for a whole canon of mechanisms to avoid misuse of corporate tax legislation regarding loss utilisation.

145 See in the literature close to the Austrian tax administration, claiming that the question whether a treaty is invoked abusively is solely a question of domestic law, Loukota, Das zweite Treaty-Shopping Erkenntnis des VwGH, SWI 2000, pp. 420 et.seq.

146 Comprehensively, see Gassner, Interpretation und Anwendung der Steuergesetze (1972).

147 VwGH 28 January 2022, Ra 2019/15/0162.

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