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Study on Effects of Tax Systems on the Retention of Earnings and the Increase of Own Equity

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- ANNEX 23 -
- SWEDEN -
- COUNTRY REPORT -

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SWEDEN

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INTRODUCTION

Key summary of findings:

A basic principle within the Swedish legal system is that similar cases shall be judged in a similar way. In the legislative work regarding tax legislation this principle means that similar cases should be taxed in the same way. Another principle is the neutrality principle meaning that the tax rules shall be neutral when the taxpayer chooses between different alternatives. Taxes should not affect the taxpayer's choice. Situations when the taxpayers choice should not be affected by taxes are amongst else the following.

- Choice between different alternatives for private investments; shares, interest bearing investments etc.
- Choice of business form; sole proprietorship, partnership or limited liability Company.

The reason for answering most questions below with a no or there is no difference is mainly due to the principles above.

Looking at the business owner there should be no difference if he makes private investments or investments in his business (if the tax of the shareholders corporation is not considered). Off course the taxation is not completely alike, but there is a possibility for the owner of shares in a closely held company to have dividend and capital gain when selling the shares partly taxed as capital income. An individual conducting business through a sole proprietorship or partnership can also receive part of the income from the business as capital income. Capital income means that the income will be taxed with a tax rate of 30%. In some cases the income is quotated for tax purposes, leading to a taxation of capital income with for example 20 or 25 %.

The Swedish participation exemption makes it advantageous from a tax perspective to retain the earnings in a company. On the other hand these earnings may be included in the value of assets in the hands of the business owner for net-wealth tax purposes. Please note that there are proposals on abolishing net-wealth taxation in Sweden completely.

PART 1 – GENERAL QUESTIONS

1. **What are the main characteristics of the tax systems applicable on enterprises and business owners in your Country (corporate income tax, income tax, capital gains tax, other profit based taxes, capital based taxes, other taxes)?**

Business owners (sole proprietorship and partner in partnership):
Individuals are subject to state and municipal income taxes on business income. State income tax is levided only if the taxalbe income exceeds a certain threshold. Business income of an individual includes income from all types of business activities.

Shareholders in closely held companies :
There are special tax regulations for dividend income and capital gain income recevied by an individual shareholder in a closely held company.

A close company is defined as a company in which a small number of individuals direclty or indirecly own shares representing more than 50 % of the voting rights (ITA 56:2)

Enterprises :
Companies are subject to the national income tax and certain payroll taxes and social security contributions. VAT is also imposed. No local income taxes are levied on corporate profits. No net worth tax is levied on companies.

Taxation of corporate profits follows the classical system. Double taxation may be eliminated or modified, in the case of corporate shareholders, by the participation exemption.

The tax rules governing taxation of enterprises and business owner are included in the Income Tax Act (ITA).

1.1. Corporate

1.1.1 What are the general principles for the computation of taxable profits?

Swedish business taxation is based on the entity's financial statements prepared in accordance with generally accepted Swedish accounting principles and with adjustments as provided by law. Resident companies are taxable on their world wide income. All income of a company, including capital gains, is categorized as business income. Company tax is levied at 28 % on the net income (the tax base). However, the effective tax rate would be slightly lower since companies are allowed to create a tax allocation reserve. The allocation can be up to 25 % of the net profit. The reserve must be dissolved (added to income) at the latest in the sixth year after the allocation has been made.

The corporate, i.e. the employer, is liable to pay social contributions relating to the wages and benefits paid to their employees. The social security fee is levied at 32.48% (year of assessment 2007). There is no special corporate capital gains tax. Dividends received by a Swedish company are according to the Swedish participation exemption rules usually tax exempt, provided the shares are fixed capital assets and held for business reasons. Capital gains deriving from the sale of shares held for business reasons are, under the same conditions as for dividends, tax exempt.

1.1.2 What are the main differences between the tax balance sheet and commercial balance sheet?

There is no tax balance sheet, only taxable adjustments of the commercial balance sheet.

1.1.3 What are the most important adjustments for the computation of taxable profits/taxable gains on the base of accounting profits?

The most important adjustments are non deductible costs, non taxable income, group contributions and difference in calculating capital gain in respect of sale of shares and real estate, difference in calculating income from partnership and difference in calculating depreciation on immovable property.

1.2. Income

1.2.1. What are the general principles of income taxation of business owners on business income, wages, distributed earnings, interest on loans and capital gain (sale of shares)?

Sole proprietorship and income from partnership:
The tax base for a business owner is calculated as the aggregate of the separate categories of income as business income and income from employment. The personal income tax rate (state and municipal income taxes) ranges between 28-57 %, due to progressive calculation. See under wages below. National income tax on earned income (employment income and business income) is imposed with the same rates.

Capital income and capital gains at the sale of private property (not business property) is taxed at a rate of 30 %. Sale of shares and real estate is taxed as the sale of private property.

A special regime applies to business income derived by individuals including an expansions reserve (chap. 34 ITA) and an interest allocation (chap. 33 ITA).

Under this regime, income retained in an expansion reserve is subject to tax at the rate of 28% (equal to the corporate income tax rate), instead of the national and local income taxes. When the reserve is reversed, it must be reported as taxable income; the 28% tax that was paid will be credited. In addition, there are rules providing for a part of business income to be deemed to be interest, thus being taxed as capital income at the rate of 30%.

Business income:
Business income of an individual includes income from all types of business activities, professions and agriculture. It also includes income from immovable business property and income and capital gains from movable property pertaining to a business. Furthermore, the income of a CFC is taxed in the hands of its shareholders under certain conditions.

The computation of taxable income is made separately for each category of income. Within the business income category, the net result is computed separately for income from all sources, i.e. (a) income from a partnership, (b) income from a business carried on abroad and (c) income from any other business. The net positive results of all sources are aggregated to arrive at the total taxable business income.

Wages:
All taxable income not considered business income or capital income is *employment income*. Wages are taxed with municipal and state tax. The municpal tax range approximately between 28-32 %.

National income tax on *earned income* (employment and business income) is imposed at the following rates (for 2007):

Taxable income (SEK)	Rate for bracket (%)
Up to 316,700	0
316,700 – 476,700	20
476,700 and over	25

The combined tax rate on income from wages is therefore 28-58 %.

Distributed earnings and interest on loans:
Dividends and interest are generally taxable as capital income. However, part of the dividends from closely held companies may be taxed as employment income in the hands of a shareholder who actively works or who has actively worked for the company to a significant degree during the last 5 years, rather than (more leniently taxed) capital income.

Capital gains (sale of shares):
Capital gains from the sale of shares are generally taxable as capital income. However, part of the capital gain from sale of shares in closely held companies may be taxed as employment income in the hands of a shareholder who is active in the company (se above under distributed earning and interest on loans).

1.2.2. Is there a different tax treatment for income from different income sources?

Yes, there is a difference in treatment of income. There are three categories of income of individuals which are employment income, business income and capital income. Employment income and capital income are each deemed to form only one source. Income from different types of business carried on by an individual taxpayer in Sweden also forms one source of income. However, income from a business carried on abroad and income from a partnership are always treated as separate sources.

1.3. Capital

1.3.1. Is there a different tax treatment between distributions of earnings and capital gains realised by the sale of the business or the shares in the undertaking?

Yes. Sale of business is treated as business income. Sale of shares is treated as capital income.

1.3.2. Are there different tax treatments for long-term capital gains and short-term capital gains?

No, the same rule applies.

1.3.3. Are there different tax treatments for capital gain from SME business stock and capital gain from larger companies' business stock?

No there is no different tax treatment applicable in respect of the size of the company.

There is only a difference in tax treatment of the sale of shares in a closely held company where the owner is active (chap. 57 ITA). Part of the capital gain from sale of shares in closely held companies may be taxed as employment income in the hands of a shareholder who actively works or who has actively worked for the company to a significant degree during the last 5 years, rather than (more leniently taxed) capital income.

Country … (Sweden)	**RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES FOR CORPORATIONS (distinguish specific tax rates for SMEs)**		
			2006

Corporate tax			
1. Tax rate			
Standard			28 %
Reduced			N/A
Minimum Tax			N/A
Special Rates			N/A
Non profit tax (local tax on corporations, energy tax…)			There are no local taxes imposed on companies.
2. Tax accounting rules			The profit and loss statement is the staring point for determining taxable business income. Tax law then provides for the necessary adjustments.
3. Depreciation			
Basis			Right to depreciation is limited to owner of assets (chap 18 ITA).
Methods			Depreciation of equipment and other assets is given at the rates indicated below. They are available equally to Swedish resident companies and to Swedish branches of non resident companies. **Short life items:** Equipment and machinery with a value of less than SEK 5,000 (SEK 20,000 for large companies) or with an expected economic life of three years or less may be depreciated in the year of acquisition (ITA 18:4). **Machinery and equipment:** There are three methods of depreciating machinery/equipment. Two of them are linked to the financial accounts. See ITA 18:13-17. (a) The most common method is depreciation as recorded in the books. Depreciation can be made with 30% per annum of the book value at the end of the year. (b) The alternative rule allows a straight line depreciation of 20% per annum where the assets are categorised by yeas of acquisition. (c) The third method is only relevant for tax purposes and is independent of the depreciation made in the financial accounts. This method allows annual depreciation of 25% on the residual net tax value.

			Buildings: Yearly depreciation is calculated by applying a percentage, 2-5%, to the acquisition cost of the building on a straight line basis. This method is independent of the depreciation made in the financial accounting. See chap 19 ITA. **Land improvements:** Annual depreciation of 5% based on the total costs for improvements. See ITA 20:5 **Stock/inventory:** Stock and work in progress is valued at the lower of acquisition cost or market value on a first in first out (FIFO) basis. Alternatively, stock may be valued at 97% of aggregate value, excluding real property, debt claims and securities held as current assets. See ITA 17:3-4.
Rates			See (3. Depreciation) above.
Accounting			Based on economic life.
Intangibles			Intangible assets such as patents, goodwill, trade marks and similar rights with a limited economic life are depreciable according to the same rules as apply to machinery and equipment – see (3. Depreciation) above.
Non depreciable assets			Land, work of art
4. Provisions			Profit periodization reserve. Corporate tax is levied at 28% on the net income (the tax base). However, the effective tax rate would be slightly lower since companies are allowed to create a tax allocation reserve. The allocation can be up to 25% of the net profit. The reserve must be dissolved (added to income) at the latest in the sixth year after the allocation has been made. See chap. 30 ITA
Risks and futures expenses			It is possible to create a reserve for future expenses in respect of guarantee obligations. ITA 16:3-5
Bad debts			N/A
Pensions			Pensions may be provided for in various ways, e.g. by direct payment of pensions to former employees and their relatives, by contributions to a personnel or pension fund, by the payment of the necessary premiums to an insurance company and by the creation of a reserve on the liabilities side of the balance sheet. The creation of such a reserve is allowed, subject to certain legal requirements. For example, the actual pensions to be paid are subject to maximum amounts, chap. 28 ITA.

Repairs			Yes for guarantees obligations.
5. Losses			
Carry forward			Losses can be carried forward indefinitely, provided there is continuity of ownership, chap 40 ITA. Capital losses on the sale of shares are deductible only for shares in listed companies if the holding is less than 10% of the voting power of the shares in the company (portfolio investments). Deductible capital losses on the sale of shares can be carried forward by companies and in some cases company groups. A loss may only be set off against capital gains on portfolio shares. Losses on sale of real estate may only be set off against capital gains on real estate. See chap 25 ITA.
Carry back			N/A
Transfer of losses			Sweden has rules regarding group contribution meaning that profits may bee transferred between companies within a group. The group contribution is deductible for the giving company and taxable for the receiving company, chap 35 ITA.
5. Inventories			
Valuation rules			Inventory (stock-in-trade) is defined as goods held by the taxpayer for the purpose of sale or consumption in his business. Generally speaking, the value adopted in the commercial accounts is accepted for tax purposes, subject to rules laid down in the law. Under the main rule, inventory may not be valued below cost or market value at the date of the balance sheet. The market value is the sales value less connected costs or, in certain cases, the replacement value after deduction of unsalable goods. In determining the value, the FIFO method should be used. Alternatively, inventory (excluding immovable property and securities) may be valued at not lower than 97% of the inventory's total acquisition value; this provision results in a standard deduction for obsolescence of 3%. See chap 17 ITA
Allocation methods			
Personal Income tax			Not applicable for corporations

Interest Income			Treated as business income
Dividends			When participation exemption applies dividends are tax free for corporations, cap 24 ITA. Dividends received by a Swedish company are according to the Swedish participation exemption rules usually tax exempt, provided the shares are fixed capital assets and held for business reasons. Unquoted shares are always considered as held for business reason. Quoted shares that have been owned, at the time of the sale, for at least one year qualify as business related if they (1) represent at least 10% of the company's voting rights or (2) are otherwise considered necessary for the business conducted by the shareholding company or any of its affiliates. Shares in foreign companies will also normally qualify as shares held for business reasons. Capital gains deriving from the sale of shares held for business reasons are, under the same conditions as for dividends, tax exempt.
Employment income			Not applicable for corporations.
Capital gains tax			There is no capital gains tax for corporations. In general, capital gains derived by a company are included in its business income. Special rules apply to the computation of capital gains on immovable property. Gains on shares and other securities that do not qualify for the exemption for business-related holdings are taxable as ordinary business income.
Sale of fixed assets			Proceeds from the sale of property classified as inventory of the company are included in the taxable business profits and taxed accordingly. In the same manner, proceeds from the sale of fixed business assets are included in the computation of taxable business profits, except in the case of immovable property (see below). In principle, the proceeds received from the sale or other disposal or loss of machinery and equipment are included in taxable business profits. However, an equal amount is deducted from the aggregated depreciable base. This means, in effect, that actual tax liability is

			postponed, in whole or in part, through reduced depreciation allowances in subsequent years. If assets in this category are sold or destroyed in the year of acquisition, their cost is fully deductible in that year and any proceeds from sale or insurance indemnity received are included in taxable business profits. Sales proceeds on goodwill are taxable as business profits in the same manner as machinery and equipment, regardless of whether they are disposed of in connection with the business.
Timing rules			
Accounting rules			
Inflation			
Rates			
Exemptions			
Sale of shares			If shares and other securities are classified as inventory of the seller, any proceeds from their disposal are included in business profits. Gains from the sale of shares or other securities not classified as inventory are either taxable under the special capital gains rules or are not subject to tax if they constitute a business-related holding (see below). Participation exemption: Capital gains derived from the sale of shares and other securities in resident or non-resident companies are not subject to tax (and consequently losses are not deductible), provided that they constitute a business-related holding. The exemption does not apply to gains on shares or securities held as inventory. Unquoted shares are always deemed to be business-related holdings if they constitute fixed business assets. Quoted shares that constitute fixed business assets and have been owned, at the time of the sale, for at least 1 year qualify as business related if they (1) represent at least 10% of the company's voting rights or (2) are otherwise considered necessary for the business conducted by the shareholding company or any of its affiliates
Capital loss			
Fixed assets			
Shares			Not deductible if business-related holding.

			Losses incurred on the alienation of shares and other securities not related to the company's business (e.g. portfolio investment) may only be set off against gains on the same type of asset; any surplus of such losses may be carried forward indefinitely to be set off against gains on the same type of asset.
Wages			
Average cost to the Undertaking			Social security contributions: Social security fees for the employer is 32,42 Average charges: Including payment for vacation taken in cash and social security fees the average cost for charges for salaries is 57,7 % for workers and 69 % for white-collar workers.
Average cost to the employee			
Overall tax on distributed earnings or Dividends			The total tax on distributed earnings to owners of closely-held companies are between 42-50 %
Timing			Dividends can only be payable after the end year closing.
Tax credit structure			N/A
Excluding non profit tax			N/A
Including non profit tax			N/A
Deduction of expenses			
General rule			Expenses that are directly associated with a business income may be deductible.
Non-deductibility of expenses			Some costs are not deductible, including bribes under criminal law and other illicit payments, fines and entertainment expenses in excess of certain limits. Direct taxes, other than payroll taxes and social security contributions, are not deductible. Dividends paid are not deductible.
Thin capitalization			Sweden does not have thin capitalization rules.
Overall corporate tax on Retained earnings			The corporate tax rate is 28 %. There is no specific tax rate on retained earnings.
Excluding non profit			N/A

tax			
Including non profit tax			N/A
Debt financing			
Interest deductibility			Yes
Limits on interest deductibility			Interestcost is deductible but, as a rule, a company must adhere to market prices in conducting business with related parties.
Interest deductibility on business owner loan to Undertaking			Yes

Country …. (Sweden)	**RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES FOR PARTNERSHIPS (distinguish specific rates for SMES)**		
	2002	2003	2006
Tax applicable to partnerships			
1. Tax rate			A Swedish partnership is generally defined as a relationship between two or more persons to attain a joint purpose with joint endeavours or means. The major distinction between a partnership and a corporation in Sweden is that each partner of a partnership is personally taxable on his share in the profits and capital of the partnership. Hence, partnerships are not taxable at the national or municipal levels, the partnership profits are taxed just once and at the individual tax rate of each partner. As a main rule, all income derived by a partnership constitutes business income. If the partner is a corporation: 28 % If the partner is an individual: 28-57 %.
Standard			N/A
Reduced			N/A
Minimum Tax			N/A
Special Rates			N/A
Non profit tax (local tax on corporations, energy tax…)			N/A

2. Tax accounting rules			The partnership must create a profit and loss statement on a yearly basis and, normally also a balance sheet. The profit and loss statement is the starting point for determining the taxable business income. Tax law then provides for the necessary adjustments. After the income is determined according to this general pattern, the result is allocated to the partners. The income is therefore computed and classified at the partnership level. Some deductions and adjustments are however maid at the level of the partners. This is true, for example, for interest allocation (chap. 33 ITA) and expansions reserves (chap. 34 ITA) when the partner is an individual.
3. Depreciation			
Basis			See answers under corporation above.
Methods			
Rates			
Accounting			
Intangibles			
Non depreciable assets			
4. Provisions			See answers under corporation above
Risks and futures expenses			
Bad debts			
Pensions			
Repairs			
5. Losses			
Carry forward			Losses can be carried forward if possible at the level of the partners. Corporate partners: Losses are deductible except for limited partners. Individual partners: Since each partnership interest constitutes a separate source, losses cannot be offset from one partnership interest against the income from another partnership interest or against the income from the individual's sole proprietorship. Instead the loss is carried forward.
Carry back			
Transfer of losses			The legislation of group contribution is not applicably on partnership.
5. Inventories			
Valuation rules			See answer under corporation above.

Allocation methods			
Personal Income tax			
Interest Income			
Dividends			
Employment income			
Capital gains tax			As a main rule, all income derived by a partnership constitutes business income. Capital gains on real estate and condominiums, however, are an exception. They are taxed as capital income in the hands of a partner who is an individual. See ITA 13:4
Sale of fixed assets			
Timing rules			
Accounting rules			
Inflation			
Rates			
Exemptions			
Sale of shares			A partnership cannot hold business-related shares. The sale of shares is therefore taxable.
Capital loss			
Fixed assets			
Shares			
Wages			See under corporations. The remuneration received by a partner for services rendered to the partnership is however not considered to be employment income
Average cost to the Undertaking			
Average cost to the employee			
Dividends			Dividend income is fully taxable
Timing			
Tax credit structure			
Deduction of expenses			See under corporations
General rule			
Non-deductibility of expenses			
Thin capitalization			
Retained earnings			N/A

Debt financing			
Interest deductibility			Yes, see under corporations
Limits on interest deductibility			See under corporations
Interest deductibility on business owner loan to Undertaking			No the partners cannot lend money to the partnership. The question is treated within the system when distributing taxable profit.

2. What are the main types of business entities and the main differences in (corporate) income taxation for sole traders, general partnerships, limited partnerships and corporation and other business entities if relevant?

Business entities:

- Public and private companies
- General and limited partnership

Business may also be conducted by an individual as a sole proprietorship.

For difference in taxation see part 1.

2.1. Are partnerships treated transparent for tax purposes?

Yes

2.2. Can partnerships opt for corporate income tax?

No

2.3. Once they have opted for a regime is it easy to switch back?

2.4. Is there a difference in this respect between general and limited partnerships?

No

2.5. Can corporations opt to be treated tax transparent?

No

2.6. Once they have opted for a regime is it easy to switch back?

2.7. Are their differences in this respect between the different types of corporations?

No

and in a table form:

	INCLUDE RELEVANT TAX PROVISIONS IN 2002 AND SUBSEQUENT CHANGES UP TO 2007			
Country ….. **(Sweden)**	General Partnership	Limited Partnership	Corporation	Sole Trader
Corporate tax	Taxed in the hands of the partners	Taxed in the hands of the partners	28 %	N/A
Income tax				28-57 %
Capital gains tax			N/A	N/A
…				
Option for Transparent treatment	No	No		
…				

3. Are there any special tax regimes for SMEs for (corporate) income tax purposes?

NO – N/A

Explanation

If YES to 3 (if yes please answer, if the answer was "no", please add "not applicable)

3.1. What are the conditions to be fulfilled in order to benefit from these special tax regimes?
3.2. Are there limits on the length of time during which these special tax regimes are available, or other limits?

4. Are there any special tax incentives, such as (re-)investment reserves or provisions, special depreciations/capital allowances deductible for (corporate) income tax purposes?

YES

Explanation: Companies are allowed to create a tax allocation reserve. The allocation can be up to 25 % of the net profit. The reserve must be dissolved (added to income) at the latest in the sixth year after the allocation has been made. See chap. 30 ITA9

And answering sub-questions including but not limited to:

4.1. Do these elements of internal financing represent an important alternative to the financing by retained earnings?

NO

Explanation

4.2. Are there any compulsory measures in relation to the retention of earnings (e.g. legal constraints for the distribution of profits and dividend policy)?

NO

Explanation and description of such measures and how they work – case study

5. Are there any differences in the tax treatment of stock and cash dividends[1]?

NO

Explanation

6. Have there been any changes in the tax regulation in recent years - since 2002 – that have had an important effect on the retention of earnings, the distribution earnings or the reinvestment of profits for a particular purpose?

NO

Explanation and comment of table under Question 1

7. Are there any current plans for tax reforms that have as their object to have an impact on the retention of earnings?

NO

Explanation and description of what the object is precisely and how it is justified (case study)

PART 2 – TAX ASPECTS OF RETAINED EARNINGS VERSUS DISTRIBUTED PROFITS AND WAGES

[1] For the Undertaking stock dividend means increased own equity. For the shareholder it means additional shares in the Undertaking which may be untaxed until sold, unlike a cash dividend.

8. What is the tax treatment of retained earnings compared to distribution of earnings on the level of the Undertaking and at a combined level of Undertaking (corporate) and business owner (individual)?

At the level of the undertaking there is no difference. The tax rate is 28 %. At the level of the individual shareholder a dividend will be taxed with 20-57 % of tax. Henceforth the dividend income earned by the business owner will be double taxed (economic double taxation).

8.1. Is there an economic double taxation of distribution of earnings (taxation of Undertaking income and then taxation on the distribution of earnings at the Undertaking level or at the business owner level)?

YES – If the shareholder is an individual or a partnership. See above under 22. A corporation which receives dividend can avoid double taxation through the participation exemption.

Explanation through case study

Sweden has a dual income tax system, with a view to reduce the tax burden on capital income. The main feature of the system is that a person's entire income is divided into income derived from capital and income derived from labour (business and wages). Income from business is split in two parts when it is derived by a sole trader or from a closely held company with active shareholders. Although labour income is taxed at a progressive tax rate, all income from capital is subject to a uniform proportional tax rate.

The flat rate at which capital is taxes (30 %) is almost equal to the corporate tax (28 %). The lower rate on labour income is fixed at this same level (approximately 30% municipal tax).

Dividend income and income from the sale of shares in a closely held company is in the hand of an active owner only taxable with 2/3 up to a certain level. This means that the tax rate below is described as 20 %. The same income for a non-active shareholder is taxed with 5/6 i.e. 25 %. Part of the income for an active shareholder is also taxed as wage income. Therefore the active owner will be taxed on distributed earnings with a tax rate that range between 20-57 %.

The *combined tax costs* (both corporate and individual tax) for the distribution of earnings as dividend could be the following. The dividend is 100 SEK, meaning that 72 SEK can be distributed after deduction of corporate tax.

Dividend to an active owner (within the limit of capital taxation)	42 SEK
Dividend both capital and labour tax (max progressive rate)	69 SEK

Depending on how much of the dividend that can be taxed as capital income the tax cost will vary between 42 SEK up to 69 SEK for both the company and the shareholder (the economic double taxation).

and in a table form:

	INCLUDE RELEVANT TAX PROVISIONS IN 2002 AND SUBSEQUENT CHANGES UP TO 2007	
Country ……	**Undertaking**	**Individual Business owner**
Corporate tax	28 %	N/A
Income tax		Salary income
Dividend tax	Tax free on business related holdings	20-57 %
Dividend credit	N/A	N/A
Capital gains tax	Capital gain on business related holdings are tax free	20-57 %
If option for Transparent treatment chosen	N/A	N/A

9. Please described the differences in the tax treatment of distribution of earnings realised as a capital gain in the context of a sale of the shares or of the business compared to that (i) of retained earnings, (ii) of wages salaries paid to the business owner and (iii) of a loan granted by the Undertaking to the business owner?

Explanation and description of special treatment if any (case study)

The sale of shares is in principle taxed in the same way as dividend income, meaning that part of the income will be taxed as wage and part as capital income (see above under 22).

If the earnings are retained in the company there is no extra tax payable beside the corporate income tax paid when the income is earned by the company.

Regarding wages paid to the business owner the following can be said. If a shareholder receives dividend income his gross profit is 72 SEK (100 SEK gross profit for the company). The gross dividend income will be tax with 20-57 % in the hands of the shareholder. If a shareholder receives salary income his gross profit is 75,5 SEK (100 gross profit for the company). The cost of social security fees for the company is included in the calculation for gross salary. The gross salary income will be taxed with 28-57 % in the hands of the shareholder.

It is forbidden for a shareholder to take a loan from the company in which he holds shares.

A sale of the business will be treated as business income in the hands of the corporation. For the shareholder to be able to get hold of the profit from the sale he must take out a dividend, sell the shares or liquidate the company.

and in a table form:

	INCLUDE RELEVANT TAX PROVISIONS IN 2002 AND SUBSEQUENT CHANGES UP TO 2007			
Country … (Sweden)	**Distributed profits Capital gain**	**Retained Profit**	**Wages/Salaries to business owner**	**Loan to business owner**
Sale of shares	20-57 %		28-57 % in wages tax plus social security fees 32,42 %	Not permitted
Sale of business	Taxed as business income			
…				
….				

10. Is the combination of wages (paid to the business owner by the Undertaking), profit distributions and retained earnings a tax planning issue that is anticipated and addressed by business owners in view of minimising the overall tax burden of the business owner and the Undertaking?

YES – If combined the different thresholds can lead to favourable taxation. Please see the effect of tax costs in the examples above under 22 and 23. It is not possible in a short and general manner describe the different thresholds and tax planning opportunities. The Swedish system of taxation of shareholders in closely held companies is extremely complex. Of course the aim is to get as much income as possible taxed as capital income, since the tax rate can be reduced to 20 % for the shareholder.

11. In respect to the previous question, is the business owner more interested in minimising his/her tax burden and then the Undertaking's or both equally?

Explanation: The business owner is interested in the total tax burden both his own and the undertaking's

12. Are there instances in which minimising the tax burden of the business owner would mean dramatically increasing the tax burden of the Undertaking?

NO

13. For corporate income tax or capital gains tax purposes, are there any incentives/disincentives to retain earnings rather than distribute them or pay wages?

YES – If the earnings are retained in a company, due to the participation exemption taxation can be avoided. Dividend to an individual shareholder will be taxed but not to a corporate shareholder.

13.1. Are there any limitations or ceilings for these incentives?

NO

Description

13.2. Is there a risk that these incentives can be used more than one time by the business owners by splitting up the business activities into different legal entities?

NO

Description via case study

14. What is the tax treatment of declared loans granted by the Undertaking to the business owner?

Such a loan is not permitted. The loan will be taxed as salary income for the business owner. The business owner may be sentenced to imprisonment or a fine according to the criminal code.

Description and case study (unless already provided under Question 10) and answering sub-questions including but not limited to:

14.1. Is there a minimum interest rate to be charged for tax purposes?
14.2. How is the interest rate treated for tax purposes for the Undertaking?
14.3. How is the interest rate treated for tax purposes for the business owner?
14.4. What are the combined tax effects of such a loan compared to a distribution of earnings equivalent in amount?

15. Are there any other taxes (e.g. net worth tax) which are imposed or based on the net equity of the Undertaking?

YES – Yes net worth tax is payable on the value of the shares if part of the assets in the company is not business assets.

Description via case study

16. Are there any other tax incentives for either the retention of earnings or their distribution of profits?

NO

Description via case study

PART 3 – TAX ASPECTS OF RETAINED EARNINGS FINANCING VS DEBT FINANCING

17. In debt financing, what is the tax treatment of interest expenses paid or accrued by the Undertaking?

Interest expenses are deductible.

Explanation and description of special treatment if any (case study)

And answering sub-questions including but not limited to:

17.1. Is there a different tax treatment to deductions on interest paid when the lender is a resident or a non-resident for tax purposes?

Transfer pricing regulations are applicable at transactions between related parties on cross-border transactions.

17.2. Is there a different tax treatment on interest on long-term debt and interest on short-term debt?

NO

18. Are there any tax benefits that are actionable based on specific amounts of equity (e.g. notional interest expense based on the increase of own equity or the total amount of equity)?

NO

Explanation and case study

And answering sub-questions including but not limited to:

18.1. What is the exact calculation method used to implement this incentive and to evaluate the benefits once this incentive is implemented?
18.2. Are there any other tax provisions favouring increases in own equity?

19. Is debt financing of an enterprise by the business owner himself of his/her family recognised for tax purposes (ie. If the business owner or his/her family lends money to the Undertaking are they treated differently than other lenders for tax purposes)?

NO

Explanation

And answering sub-questions including but not limited to:

19.1. If so, are there any incentives for the business owners to debt-finance their enterprise instead of retained earnings financing or equity financing?

20. Is there a general discrimination between retained earnings financing and debt financing from a tax point of view?

NO

Explanation

20.1. Is there a general discrimination between retained earnings financing and equity financing from a tax point of view?

NO

Explanation

20.2. Is there a general discrimination between equity financing and debt financing from a tax point of view?

NO

Explanation

21. Are there any debt to equity ratios limiting the deductibility of interest expenses for tax purposes?

NO

Explanation, description of the ratio and case study

And answering sub-questions including but not limited to:

21.1. If so, does the limitation apply to loans granted by the business owner and affiliated persons or does it include loans granted by third parties?

NO

Explanation, description of the ratio and case study

21.2. What are the consequences if the debt to equity ratio is not respected?

Explanation, description of the ratio and case study

22. Are there any tax provisions likely to impact the conversion of retained earnings into share paid in capital (For example share buy-back)?

NO

Explanation

And answering sub-questions including but not limited to:

23. Are there any other taxes that have as their object to affect or impact on either Undertaking debt financing or retained earnings financing?

NO

Explanation and case study

PART 4 – TAX ASPECTS OF BUSINESS INCOME VERSUS PRIVATE INCOME

24. In respect to individual business owners, what is the general tax treatment for private (ie: interest on passive investment) income compared to business income (ie: income generated from your business activity)?

Description and case study

and in a table form:

	INCLUDE RELEVANT TAX PROVISIONS IN 2002 AND SUBSEQUENT CHANGES UP TO 2007	
Country … (please fill in)	Private Investment Income	Business Income
…	25-30 %	28 % for the corporation 20-57 % for the shareholder
…		
…		
…		
…		

and answering sub-questions including but not limited to:

24.1. Are there different allowances or special treatments for private investment income and business income?

Private investments are taxed at a lower tax cost since the investor does not need to consider the tax cost of the company he is investing in. If the investment is maid in a quoted company the tax rate for the shareholder on the sale of shares or dividend income is 30 %. If the company is a closely held company and the investor is not active the tax rate on sale of shares or dividend income is 25 %.

Shareholders in closely held companies must consider the tax cost of the company and his own tax costs which range between 20-57 %.

Explanation and case study

25. Is there a different tax treatment for interest income received in a private investors capacity (ie: business owner investment return in another Undertaking) and interest income earned through business activity (ie: business owner investment return from the Undertaking)?

NO

Explanation

26. Does the tax system encourage business owners to invest in private assets, which are subsequently rented or leased to their enterprises?

NO

Explanation

27. Does the tax system encourage that assets be acquired by the Undertaking and rented or leased to the business owner?

NO

Explanation

28. Are capital gains from private assets taxed in the same way as capital gains realised within the context of a business activity?

NO

Explanation and case study

and answering sub-questions including but not limited to:

28.1. If capital gains from private assets are taxed lower, does this represent an important incentive for the business not to invest in their own Undertaking?

YES

Explanation

29. Are interest expenses incurred on private debts deductible for tax purposes?

YES

Explanation

30. Is there a tax advantage for the Undertaking in transferring debts from the business owner to the Undertaking?

NO

Explanation and case study

31. Is there a tax advantage for the business owner in transferring debts from the business owner to the Undertaking?

YES – the net worth tax of the business owner might be lowered since there will be higher debts in the company. This will lower the value of the shares.

Explanation and case study

32. Are there other taxes such as inheritance tax which have an important impact on own equity and retention of earnings decisions?

NO – there is not inheritance tax in Sweden.

Note: It can be read from our key summary of findings that our conclusion was that there is no difference in Sweden between different alternatives for investments due to the fact that similar cases should be taxed in the same way. Since there is no major difference between different investments many answers are no. Regarding case law there is no case law on the issues dealt with in the country report since there is no issue in Sweden.