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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 5 -
- AUSTRIA -
- COUNTRY REPORT -

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AUSTRIA

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INTRODUCTION

In Austria a tax reform came into force on January 1st, 2005, covering particularly the income tax on individuals and the corporation tax. Tax rates were reduced for lower as well as for higher income, whereas at the same time a number of tax allowances and deductions were abolished or essentially reduced. For example, the corporate tax rate on income of individuals was lowered from 34 % to 25.[1]

The considerable changes of the taxation of corporations make it now much more attractive to do business in the legal form of a company. It can be assumed, that especially the number of private limited companies ("GmbH") will increase in the future.

[1] Austrian Tax Reform Act 2005 („Abgabenänderungsgesetz" 2005), passed the Austrian parliament on May 6, 2004, and became mainly effective from January 1, 2005. The rate of corporate income tax was cut off to 25% for profits derived after December 31, 2004. In case of deviating business years, profits derived in 2004/2005 were partly taxed at 34%, partly at 25%.

Furthermore, the 2005 tax reform enables a purchaser to benefit from a step-up in basis; formerly, only an asset deal qualified the purchaser to amortise goodwill and deduct hidden reserves. Due to the 2005 tax reform, a part of the acquisition costs of shares in a corporation (provided that the corporation in question is eligible for group membership) will be treated as goodwill. The amount of goodwill is limited to 50% of the acquisition costs of the shares and may be amortised within a period of 15 years. As a matter of evidence, this part of the 2005 tax reform will increase the attractiveness of share deals.

A new modern “group taxation” system was introduced by the 2005 tax reform. This new “group taxation” system does not require economic and operational control (as it was previously the case) or a profit and loss transfer agreement.[2]

[2] Taxation of branch offices of foreign corporations is based on a 25% income tax rate for its profits. The permanent establishment is to be attributed such profits as it could have earned if it has exercised the same or similar activity under the same or similar conditions as an independent company.

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)?**

1.1. Corporate Income

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

Valuation methods used for commercial law purposes may also be applied for tax purposes, unless the tax law provides otherwise. The profit or loss shown in the financial statements is adjusted to take account of any differences between the requirements of tax and commercial law. Depreciation for tax purposes is generally in line with depreciation in financial statements. If the depreciation charges required for financial statement purposes exceed the amounts acceptable under tax law those allowed under tax law take precedence, resulting in a difference between taxable and financial statement income. There are certain restrictions with regard to accruals and provisions, particularly only 80% of long-term accruals and provisions are deductible.[3] Tax losses may be carried forward indefinitely and may be offset against both trading income and capital gains. Only 75% of current income may be offset against tax losses brought forward, thus 25% of current income is invariably subject to tax.[4] Excess tax losses can be carried forward. Loss carry-backs are not permitted[5].

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[3] Austrian Tax Reform Act 2001 („Budgetbegleitgesetz" 2001). Exemptions are provisions for personnel benefits, ie severance payments pensions, vacations and anniversary awards.
[4] Austrian Tax Reform Act 2001, since January 2001. With the tax reforms of 2000, BGBl I 2000/71, the deductibility of losses from loss investment were restricted so that these losses are neither be set off nor carried forward and was further restricted by the Austrian Tax Reform Act 2001 in the above sense.
[5] Losses may only be set off against later profits referring to the same investment.

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

Corporations must prepare the balance sheet in accounts format in the classification prescribed in the Commercial Code ("Unternehmens-gesetzbuch")[6]. Receivables and liabilities exceeding a term of one year are shown separately or disclosed in notes. The working capital and other ratios can be computed. Capital not yet paid in is deducted from the nominal capital. Share capital called up is reported separately under other receivables. Reserves are divided into capital reserves and revenue reserves, including revenue reserves under statutory provisions or under a company's by-laws. Stock corporations and larger limited liability companies have to appropriate 5% of the annual profit after taxes as long as this reserve does not exceed 10% of the statutory share capital.

The income statement prepared by stock corporations and limited liability companies must be in report form ("Staffelform")[7] using either the total-cost format ("Gesamtkostenverfahren")[8] or the cost-of sales format ("Umsatzkostenverfahren")[9].

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

Even if no income is generated a limited company triggers a minimum corporation tax of EUR 1.750 whereas EUR 3.500 are due in case of stock corporations.[10]

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[6] Austrian Commercial Reform Act 2005 („Handelsrechts-Änderungsgesetz" 2005, BGBl I 2005/120). According to the Handelsrechts-Änderungsgesetz 2005 parts of former Austrian Business Law Act („Handelsgesetzbuch" – „HGB") were changed as well as the wording of the law to "Commercial Code" („Unternehmensgesetzbuch" – „UGB").

[7] § 231 subsection 1 UGB.

[8] Total cost format „Gesamtkostenverfahren", § 231 subsection 2 UGB.

[9] Cost of sales format „Umsatzkostenverfahren", § 231 subsection 3 UGB.

[10] § 24 subsection 4 Corporate Income Tax Act ("Körperschaftsteuergesetz" – „KStG"), BGBl I 1997/70, beginning with the second year of unlimited tax liability even if no income is generated on a 5% basis of the minimum share capital.

The abolition of some tax benefits for corporations (e.g. roll-over tax credit, deemed interest on equity increases) is expected to have only an insignificant impact on the tax basis.

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)?

Profits that are distributed are subject to final withholding tax at a rate of 25%.[11] However, refund is available in case the taxable person chooses to declare the dividends he received because average income tax is lower than 25%.[12] This withholding tax rate is regularly reduced under Austria's double tax treaties. Most tax treaties require the company to withhold the full rate and the recipient of the dividend to apply to the tax authorities for a refund. A resident individual's dividend income from the Austrian sources is not subject to further income tax if 25% has been withheld at source. The withholding tax is the final tax ("Endbesteuerung") for the individual shareholder.[13]

Losses incurred as of 1998 may be carried forward without time limit in the amount of 75 % of taxable income. However, losses may not be deducted if the ownership of a corporation changes materially and if the nature of the business carried out changes dramatically.

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[11] Since 1989. The recipient of the dividends is liable to income tax (half the corresponding average rate) but the dividends withholding tax is credited to his personal tax liability. Until the year 1988 from dividends paid to shareholders the withholding tax at the rate of 20% was deducted by the company.
[12] § 97 subsection 4 Personal Income Tax Act („Einkommensteuergesetz" – „EStG").
[13] § 1 subsection 1, numeral 2 Final Tax Act („Endbesteuerungsgesetz"), BGBl 1993/11, as capital yield tax.

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

In cases of capital gains from the disposal of shares in a foreign corporation which have been held for more than one year and interest from cash deposits in Austrian as well as foreign banks the income tax rate of a maximum of 50% is reduced to a flat rate of 25% and is withheld at source if the deposit is made with an Austrian bank or, if the deposit is with a foreign bank, the tax rate is reduced in the course of the tax assessment. The reduced tax rates are equally available to non-resident individuals.

1.3. Capital

The objective of the table is to obtain a brief summary of the relevant/applicable tax provision for the subjects mentioned (and amendments to the rules over the period indicated). Specific references to legal provisions, tax rules regulations and tax regulations should be provided if they are likely to impact the structure of companies or their use of profits (ie if a tax provision is voted that exempts from taxes a portion of profits kept as retained earnings, this should be noted). This table will be read in conjunction with the table on company equity structure. Changes in tax regulation may or may not impact the equity structure of companies.

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For CORPORATIONS (distinguish specific tax rates for SMEs)				
	2002	2003	2004	2005	2006
Corporate income tax					
1. Tax rate					
Standard	34%	34%	34%	25%	25%
Reduced	N.A.	N.A.	N.A.	N.A.	N.A.
Minimum Tax	N.A.	N.A.	N.A.	N.A.	N.A.
Special Rates	N.A.	N.A.	N.A.	N.A.	N.A.
Non profit tax (local tax on corporations, energy tax…)	Real estate tax from 0,4% to 0,84%; VAT 20%; Stamp Duties (lease and rental 1%, loans, overdraft 0,8% or 1,5%, assignments of rights 0,8%, surety ships 1%)				
2. Tax accounting rules	Commercial Accounting ("Maßgeblichkeitsgrundsatz")				
3. Depreciation					
Basis	Cost price or production cost. Assets are depreciated over their estimated useful lives. Goodwill is amortized over a period of 15 years	Cost price or production cost. Assets are depreciated over their estimated useful lives. Goodwill is amortized over a period of 15 years	Cost price or production cost. Assets are depreciated over their estimated useful lives. Goodwill is amortized over a period of 15 years	Cost price or production cost. Assets are depreciated over their estimated useful lives. Goodwill is amortized over a period of 15 years	Cost price or production cost. Assets are depreciated over their estimated useful lives. Goodwill is amortized over a period of 15 years
Methods	Straight-line basis	Straight-line basis	Straight-line basis	Straight-line basis	Straight-line basis

Austria	**RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For CORPORATIONS (distinguish specific tax rates for SMEs)**				
	2002	2003	2004	2005	2006
Rates	Annual or half of the annual in the last six months	Annual or half of the annual in the last six months	Annual or half of the annual in the last six months	Annual or half of the annual in the last six months	Annual or half of the annual in the last months
Accounting	N.A.	N.A.	N.A.	N.A.	N.A.
Intangibles	2-3%	2-3%	2-3%	2-3%	2-3%
Non depreciable assets	N.A.	N.A.	N.A.	N.A.	N.A.
4. Provisions					
Risks and futures expenses	YES As long-term accruals only 80% deductible	YES As long-term accruals only 80% deductible	YES As long-term accruals only 80% deductible	YES As long-term accruals only 80% deductible	YES As long-term accruals only 80% deductible
Bad debts	N.A.	N.A.	N.A.	N.A.	N.A.
Pensions	YES	YES	YES	YES	YES
Repairs	YES	YES	YES	YES	YES
5. Losses					
Carry forward	75% of current income may be offset against tax losses	75%	75%	75%	75%
Carry back	Not permitted	Not permitted	Not permitted	Not permitted	Not permitted

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For CORPORATIONS (distinguish specific tax rates for SMEs)				
	2002	2003	2004	2005	2006
Transfer of losses	Losses incurred from foreign permanent establish-ment may be offset against Austrian income	Losses incurred from foreign permanent establish-ment may be offset against Austrian income	Losses incurred from foreign permanent establish-ment may be offset against Austrian income	On the basis of the group taxation or from foreign permanent establish-ment	On the basis of the group taxation or from foreign permanent establish-ment
6. Inven-tories					
Valuation rules	Lower of cost or market value	Lower of cost or market value	Lower of cost or market value	Lower of cost or market value	Lower of cost or market value
Allocation methods	FIFO-method on cost price basis. LIFO in accordance with the tax-payer`s actual practice	FIFO-method on cost price basis. LIFO in accordance with the tax-payer`s actual practice	FIFO-method on cost price basis. LIFO in accordance with the tax-payer`s actual practice	FIFO-method on cost price basis. LIFO in accordance with the tax-payer`s actual practice	FIFO-method on cost price basis. LIFO in accordance with the tax-payer`s actual practice
Personal Income tax					
Interest Income	25%	25%	25%	25%	25%
Dividends	25%	25%	25%	25%	25%
Employment income	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For CORPORATIONS (distinguish specific tax rates for SMEs)				
	2002	2003	2004	2005	2006
Capital gains tax					
Sale of fixed assets	Immovable property is only taxable as speculative gains	Immovable property is only taxable as speculative gains	Immovable property is only taxable as speculative gains	Immovable property is only taxable as speculative gains	Immovable property is only taxable as speculative gains
Timing rules	Within 10 years after acquisition	Within 10 years after acquisition	Within 10 years after acquisition	Within 10 years after acquisition	Within 10 years after acquisition
Accounting rules	Distinction between business income and non-business income for computing income tax with different procedures for determining the amount of income tax				
Inflation	1,8%	1,3%	2,1%	2,3%	1,4%
Rates	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%
Exemptions	Corporation	Corporation	Corporation	Corporation	Corporation
Sale of shares	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%
Capital loss	Neither be set off against other sources of income nor be carried forward	Neither be set off against other sources of income nor be carried forward	Neither be set off against other sources of income nor be carried forward	Neither be set off against other sources of income nor be carried forward	Neither be set off against other sources of income nor be carried forward

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For CORPORATIONS (distinguish specific tax rates for SMEs)				
	2002	2003	2004	2005	2006
Fixed assets	Immovable property is only taxable as speculative gains	Immovable property is only taxable as speculative gains	Immovable property is only taxable as speculative gains	Immovable property is only taxable as speculative gains	Immovable property is only taxable as speculative gains
Shares	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%
Wages	For the first € 3.640 = 0% For the next € 3.630=21% For the next €14.530=31% For the next €29.070=41% For further income 50%	For the first € 3.640 = 0% For the next € 3.630=21% For the next €14.530=31% For the next €29.070=41% For further income 50%	For the first € 3.640 = 0% For the next € 3.630=21% For the next €14.530=31% For the next €29.070=41% For further income 50%	Up to T€ 10=0% At T€ 25, tax €5.750, tax rate 23% At T€ 51, tax €17.085, tax rate 33,5% Over T€ 51 = 50%[14]	Up to T€ 10=0% At T€ 25, tax €5.750, tax rate 23% At T€ 51, tax €17.085, tax rate 33,5% Over T€ 51 = 50%
Average cost to the Undertaking	20,45%	20,45%	20,65%	24,43%	24,43%
Average cost to the employee	16,65%	16,65%	16,95%	17%	17%

[14] § 33 subsection 1 Income Tax Act „EStG", BGBl I 2004/57, since 2005.

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For CORPORATIONS (distinguish specific tax rates for SMEs)				
	2002	2003	2004	2005	2006
Overall tax on distributed earnings or Dividends					
Timing	N.A.	N.A.	N.A.	N.A.	N.A.
Tax credit structure	25%	25%	25%	25%	25%
Excluding non profit tax	N.A.	N.A.	N.A.	N.A.	N.A.
Including non profit tax	N.A.	N.A.	N.A.	N.A.	N.A.
Deduction of expenses					
	Depreciable movable assets with a price not exceeding €˚400. Repair and mainte-nance pay-ments in the period incurred. Organization expenses. For personal tax purposes:	Depreciable movable assets with a price not exceeding €˚400. Repair and mainte-nance pay-ments in the period incurred. Organization expenses. For personal tax purposes.	Depreciable movable assets with a price not exceeding €˚400. Repair and mainte-nance pay-ments in the period incurred. Organization expenses. For personal tax purposes.	Depreciable movable assets with a price not exceeding €˚400. Repair and mainte-nance pay-ments in the period incurred. Organization expenses. For personal tax purposes.	Depreciable movable assets with a price not exceeding €˚400. Repair and mainte-nance pay-ments in the period incurred. Organization expenses. For personal tax purposes.

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For CORPORATIONS (distinguish specific tax rates for SMEs)				
	2002	2003	2004	2005	2006
General rule	Annual income exceeded € 36.400, special allowances up to an annual income of € 50.900	Annual income exceeded € 36.400, special allowances up to an annual income of € 50.900	Annual income exceeded € 36.400, special allowances up to an annual income of € 50.900	Phased out if income exceeds T€ 10 up to € 35.511 A general deduction of € 1.264 Deduction for employees of € 54 Deduction for sole earner in a family of € 364 Com-muter`s deduction for employees €˚291	Phased out if income exceeds T€ 10 up to € 35.511 A general deduction of € 1.264 Deduction for employees of € 54 Deduction for sole earner in a family of € 364 Com-muter`s deduction for employees €˚291

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For CORPORATIONS (distinguish specific tax rates for SMEs)				
	2002	2003	2004	2005	2006
Non-deductibility of expenses	Excessive expenses for passenger cars, 50% of business-related meal expenses, gifts to non-employees, donations for public benefit, half the benefits and compen-sations for members of the supervisory board	Excessive expenses for passenger cars, 50% of business-related meal expenses, gifts to non-employees, donations for public benefit, half the benefits and compen-sations for members of the supervisory board	Excessive expenses for passenger cars, 50% of business-related meal expenses, gifts to non-employees, donations for public benefit, half the benefits and compen-sations for members of the supervisory board	Excessive expenses for passenger cars, 50% of business-related meal expenses, gifts to non-employees, donations for public benefit, half the benefits and compen-sations for members of the supervisory board	Excessive expenses for passenger cars, 50% of business-related meal expenses, gifts to non-employees, donations for public benefit, half the benefits and compen-sations for members of the supervisory board
Thin capitalization	As hidden equity income appropria-tion are not tax-deductible	As hidden equity income appropria-tion are not tax-deductible	As hidden equity income appropria-tion are not tax-deductible	As hidden equity income appropria-tion are not tax-deductible	As hidden equity income appropria-tion are not tax-deductible

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For PARTNERSHIPS (distinguish specific rates for SMES)				
	2002	2003	2004	2005	2006
Overall corporate income tax on Retained earnings					
Excluding non profit tax	N.A.	N.A.	N.A.	N.A.	N.A.
Including non profit tax	N.A.	N.A.	N.A.	N.A.	N.A.
Debt financing					
Interest deductibility	YES	YES	YES	YES	YES
Limits on interest deductibility	NO	NO	NO	NO	NO
Interest deductibility on business owner loan to Undertaking	YES	YES	YES	YES	YES

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For PARTNERSHIPS (distinguish specific rates for SMES)				
	2002	2003	2004	2005	2006
Tax applicable to partnerships					
1. Tax rate					
Standard	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%
Reduced	N.A.	N.A.	N.A.	N.A.	N.A.
Minimum Tax	Progressive from 0% up to 50%				
Special Rates	25%	25%	25%	25%	25%
Non profit tax (local tax on corporations, energy tax…)	Real estate tax from 0,4% to 0,84%; VAT 20%; Stamp Duties (lease and rental 1%, loans, overdraft 0,8% or 1,5%, assignments of rights 0,8%, surety ships 1%)				
2. Tax accounting rules	Commer. Accounting	Commer. Accounting	Commer. Accounting	Commer. Accounting	Commer. Accounting
3. Depreciation					
Basis	Assets are depreciated over their estimated useful lives. Goodwill is amortized over a period of 15 years	Assets are depreciated over their estimated useful lives. Goodwill is amortized over a period of 15 years	Assets are depreciated over their estimated useful lives. Goodwill is amortized over a period of 15 years	Assets are depreciated over their estimated useful lives. Goodwill is amortized over a period of 15 years	Assets are depreciated over their estimated useful lives. Goodwill is amortized over a period of 15 years

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For PARTNERSHIPS (distinguish specific rates for SMES)				
	2002	2003	2004	2005	2006
Methods	Straight-line basis	Straight-line basis	Straight-line basis	Straight-line basis	Straight-line basis
Rates	Annual or half of annual in the last six month	Annual or half of annual in the last six months	Annual or half of annual in the last six months	Annual or half of annual in the last six months	Annual or half of annual in the last six months
Accounting	Carried at cost, less depreciation, or at their lower going concern value	Carried at cost, less depreciation, or at their lower going concern value	Carried at cost, less depreciation, or at their lower going concern value	Carried at cost, less deprecia-tion, or at their lower going concern value	Carried at cost, less depreciation, or at their lower going concern value
Intangibles	2-3%	2-3%	2-3%	2-3%	2-3%
Non depreciable assets	N.A.	N.A.	N.A.	N.A.	N.A.
4. Provisions					
Risks and futures expenses	YES As long-term accruals only 80% deductible	YES As long-term accruals only 80% deductible	YES As long-term accruals only 80% deductible	YES As long-term accruals only 80% deductible	YES As long-term accruals only 80% deductible
Bad debts	N.A.	N.A.	N.A.	N.A.	N.A.
Pensions	YES	YES	YES	YES	YES
Repairs	YES	YES	YES	YES	YES

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For PARTNERSHIPS (distinguish specific rates for SMES)				
	2002	2003	2004	2005	2006
5. Losses					
Carry forward	Only 75% of current income	Only 75% of current income	Only 75% of current income	Only 75% of current income	Only 75% of current income
Carry back	Not permitted	Not permitted	Not permitted	Not permitted	Not permitted
Transfer of losses	N.A.	N.A.	N.A.	On the basis of the group taxation	On the basis of the group taxation
6. Inventories					
Valuation rules	Lower of cost or market value	Lower of cost or market value	Lower of cost or market value	Lower of cost or market value	Lower of cost or market value
Allocation methods	FIFO-method on cost price basis. LIFO in accordance with the tax-payer`s actual practice	FIFO-method on cost price basis. LIFO in accordance with the tax-payer`s actual practice	FIFO-method on cost price basis. LIFO in accor-dance with the tax-payer`s actual practice	FIFO-method on cost price basis. LIFO in accordance with the tax-payer`s actual practice	FIFO-method on cost price basis. LIFO in accordance with the tax-payer`s actual practice
Personal Income tax	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%
Interest Income	25%	25%	25%	25%	25%
Dividends	25%	25%	25%	25%	25%
Employment income	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of a 50%

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For PARTNERSHIPS (distinguish specific rates for SMES)				
	2002	2003	2004	2005	2006
Capital gains tax	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%
Sale of fixed assets	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%
Timing rules	Within 10 years after acquisition	Within 10 years after acquisition	Within 10 years after acquisition	Within 10 years after acquisition	Within 10 years after acquisition
Accounting rules	Carried at cost, less depreciation, or at their lower going concern value	Carried at cost, less depreciation, or at their lower going concern value	Carried at cost, less depreciation, or at their lower going concern value	Carried at cost, less depreciation, or at their lower going concern value	Carried at cost, less depreciation, or at their lower going concern value
Inflation	1,8%	1,3%	2,1%	2,3%	1,4%
Rates	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%
Exemptions	Corporation	Corporation	Corporation	Corporation	Corporation
Sale of shares	25%	25%	25%	25%	25%
Capital loss	Neither be set off against other sources of income nor be carried forward	Neither be set off against other sources of income nor be carried forward	Neither be set off against other sources of income nor be carried forward	Neither be set off against other sources of income nor be carried forward	Neither be set off against other sources of income nor be carried forward

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For PARTNERSHIPS (distinguish specific rates for SMES)				
	2002	2003	2004	2005	2006
Fixed assets	Immovable assets is only taxable as speculative gains	Immovable assets only taxable as speculative gains	Immovable assets only taxable as speculative gains	Immovable assets only taxable as speculative gains	Immovable assets only taxable as speculative gains
Shares	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%
Wages					
Average cost to the Undertaking	20,45%	20,45%	20,65%	24,43%	24,43%
Average cost to the employee	16,65%	16,65%	16,95%	17%	17%
Dividends	25%	25%	25%	25%	25%
Timing	N.A.	N.A.	N.A.	N.A.	N.A.
Tax credit structure	25%	25%	25%	25%	25%
Deduction of expenses					

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For PARTNERSHIPS (distinguish specific rates for SMES)				
	2002	2003	2004	2005	2006
General rule	Depreciable movable assets with a price not exceeding € 400. Repair and mainte-nance pay-ments in the period incurred. Organization expenses. For personal tax purposes: Annual income exceeded € 36.400, special allowances up to an annual income of € 50.900	Depreciable movable assets with a price not exceeding € 400. Repair and mainte-nance pay-ments in the period incurred. Organization expenses. For personal tax purposes: Annual income exceeded € 36.400, special allowances up to an annual income of € 50.900	Depreciable movable assets with a price not exceeding € 400. Repair and mainte-nance pay-ments in the period incurred. Organization expenses. For personal tax purposes: Annual income exceeded € 36.400, special allowances up to an annual income of € 50.900	Depreciable movable assets with a price not exceeding € 400. Repair and mainte-nance pay-ments in the period incurred. Organization expenses. For personal tax purposes: Phased out if income exceeds T€ 10 up to € 35.511 A general deduction of € 1.264 Deduction for em-ployees of € 54	Depreciable movable assets with a price not exceeding € 400. Repair and mainte-nance pay-ments in the period incurred. Organization expenses. For personal tax purposes: Phased out if income exceeds T€ 10 up to € 35.511 A general deduction of € 1.264 Deduction for em-ployees of € 54

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For PARTNERSHIPS (distinguish specific rates for SMES)				
	2002	2003	2004	2005	2006
Non-deductibility of expenses	Excessive expenses for passenger cars, 50% of business-related meal expenses, gifts to non-employees, donations for public benefit.	Excessive expenses for passenger cars, 50% of business-related meal expenses, gifts to non-employees, donations for public benefit.	Excessive expenses for passenger cars, 50% of business-related meal expenses, gifts to non-employees, donations for public benefit.	Deduction for sole earner in a family of € 364 Com-muter`s deduction for employees €˚291 Excessive expenses for passenger cars, 50% of business-related meal expenses, gifts to non-employees, donations for public benefit.	Deduction for sole earner in a family of € 364 Com-muter`s deduction for employees €˚291 Excessive expenses for passenger cars, 50% of business-related meal expenses, gifts to non-employees, donations for public benefit.
Thin capitalization	As hidden equity income appropria-tion are not tax-deductible	As hidden equity income appropria-tion are not tax-deductible	As hidden equity income appropria-tion are not tax-deductible	As hidden equity income appropria-tion are not tax-deductible	As hidden equity income appropria-tion are not tax-deductible
Retained earnings	N.A.	N.A.	N.A.	N.A.	N.A.
Debt financing	YES	YES	YES	YES	YES

Austria	RELEVANT TAX PROVISIONS AND SUBSEQUENT CHANGES For PARTNERSHIPS (distinguish specific rates for SMES)				
	2002	2003	2004	2005	2006
Interest deductibility	YES	YES	YES	YES	YES
Limits on interest deductibility	NO	NO	NO	NO	NO
Interest deductibility on business owner loan to Undertaking	YES	YES	YES	YES	YES

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?

NO

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

NO

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

The progressive income tax rates up to a maximum of 50% apply to both resident and non-resident individuals. The income tax rate is reduced to half the normal rate in cases of capital gains from the disposal of a going concern or the disposal of a partnership interest after a minimum holding period of seven years if the disposal is made upon retirement. Otherwise, such capital gains are subject to the full income tax rate, but will be spread evenly over three years after holding period of seven years. The reduced tax rate also applies to capital gains from the disposal of shares in a limited liability company or in a stock corporation if the shareholding is 1% or more at any point of time within the last five years and shares are held for more than one year. The application of half of the average tax rate entails ultimately that a corporation's distributed earnings are taxed at a maximum of 43,75%.

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?

The following types of companies are the most common:

- Company with limited liability ("GmbH")[15]
- Stock Company ("AG)[16]
- General Partnership ("OG")[17]
- Limited Partnership ("KG")

The withholding tax for capital gains and dividends is the final tax ("Endbesteuerung") for partnerships, sole traders and for companies and is the same rate of corporated tax, both of 25%.

[15] Limited Liability Corporation Act („Gesetz über Gesellschaften mit beschränkter Haftung" – „GmbHG"), RGBl 1906/58; BGBl 1996/304; BGBl I 2006/103.

[16] Joint Stock Corporation Act („Bundesgesetz über Aktiengesellschaften" – „AktG"), BGBl 1965/98; BGBl I 2004/161; BGBl I 2006/103.

[17] According to the Austrian Commercial Reform Act 2005 („Handelsrechts-Änderungsgesetz" 2005), BGBl I 2005/120, the general partnership is now called „Offene Gesellschaft" – „OG" instead of „Offene Handelsgesellschaft" – „OHG".

Setting up a GmbH or AG a 1% capital tax (“Gesellschaftssteuer”) is to be paid, based on the paid-capital including a premium[18], and a registration fee of approximately EUR 360,00 for the commercial register, depending on the complexity of the registration.

A capital increase is subject to a 1% capital tax and a registration fee of approximately EUR 230,00.

Setting up a partnership a registration fee may to be paid.

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?

N.A.

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

NO

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[18] § 8 Capital Tax Law („Kapitalverkehrssteuergesetz“ „KVG“), DRGBl I 1934/1058; BGBl 1948/57; BGBl I 2000/29.

2.5. Can corporations opt to be treated tax transparent?

N0

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

N.A.

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

YES

In a table from:

Austria	**INCLUDE RELEVANT TAX PROVISIONS IN 2002 AND SUBSEQUENT CHANGES UP TO 2007**			
	General Partnership	Limited Partnership	Corporation	Sole Trader
Corporate income tax	N.A.	N.A.	25%	N.A.
Income tax	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%	Up to a maximum of 50%

Austria	INCLUDE RELEVANT TAX PROVISIONS IN 2002 AND SUBSEQUENT CHANGES UP TO 2007			
	General Partnership	Limited Partnership	Corporation	Sole Trader
Capital gains tax	Income tax is reduced to half the normal rate if the partnership interest has been held for a minimum period of seven years and the disposal is made upon retirement. Otherwise capital gains are subject to the full tax rate, but may be spread over three years after a holding period of seven years.	Income tax is reduced to half the normal rate if the partner-ship interest has been held for a mini-mum period of seven years and the disposal is made upon retirement. Otherwise capital gains are subject to the full tax rate, but may be spread over three years after a holding period of seven years.	25%	25%
Option for Transparent treatment	YES	YES	N.A.	N.A.

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

NO, in cases of a limited company or a share corporation the corporate income tax rate of 25% is applicable with the obligation to pay minimum corporate income tax at a quarterly rate of EUR 437,50 for limited liability companies and EUR 875,00 for stock corporations for corporations sustaining losses. In cases of partnerships or sole traders the tax rate will accrue to a maximum of 50%.

3.1. What are the conditions to be fulfilled in order to benefit from these special tax regimes?

According to the affiliation privilege (Schachtelprivileg) any dividends an Austrian company receives as a result of holding shares of another Austrian company are not subject to corporation tax in the receiving company. Furthermore such dividends are not subject to withholding tax, if the receiving company holds at least 25%[19]. As a special incentive for foreign investment dividends and capital gains earning an Austrian company from a foreign company of which the Austrian company holds a minimum of 10% interest for one year are not subject to taxation in Austria[20]

3.2.Are there limits on the length of time during which these special tax regimes are available, or other limits?

According to the national affiliation privilege dividends are exempt from withholding tax when the domestic corporate shareholder holds a minimum of

[19] § 10 subsection 1 KStG.
[20] EC Parent-Subsidiary Directive 2003/123/EC, December 22, 2003, ABl EC L 7/41; EC Directive 90/435, July 23, 1990, ABL EC L 255;§ 10 subsection 1 and 2 KStG.

25% interest in the company. Capital gains and winding-up profits are not exempt form the corporate income tax and are taxed on the progressive tariff.
Losses from the sale or liquidation of international participations and write-downs of the book value have to be spread over seven years in order to become tax effective.

According to the international affiliation privilege dividends and capital gains on the sale and the write-downs of the international participation are tax neutral, if the shareholder holds for a minimum period of 1 year at least a 10% interest on the subsidiary[21]; the parent company is an Austrian company or a comparable foreign company subject to unlimited corporate income taxation in Austria; the subsidiary is built in one of the legal forms listed in the annex to the EC Parent-Subsidiary Directive or is legally comparable to an Austrian company.;
Losses of the alienation of an international participation and write –downs of the participation are also tax neutral.[22]
The exercising of the option for tax deductibility of capital losses and write downs was modified. For “older” companies and their international participation in a foreign subsidiary, the option has to be exercised before January 1, 2006, for filing the Austrian corporate income tax return in 2006. For “new” companies and their international participation in a foreign subsidiary, the option has to be exercised before January 1, 2004, regarding the return for 2004.

[21] An indirect shareholding by way of a partnership bears also the tax exemption.
[22] Austrian Tax Reform Act 2003 („Budgetbegleitgesetz“ 2003 – „BBG “ 2003), BGBl I 2003,/71. The shareholding percentage reduction from 25% to 10% interest became tax effective for “old” companies in 2006 and for “new” companies in 2004.

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, tax incentives available under the Austrian tax law include additional allowance of up to 25%, in particular cases up to 35% of research and development expenses, alternatively a tax credit equal to 8% of certain research and development expenses, and an employee's training allowance of up to 20% of qualifying training costs, alternatively a tax credit equal of 6% of such costs, and a particular allowance of up to EUR 2.000,00 if apprentices are employed, alternatively a tax credit of EUR 1.000,00.

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

   YES, capital will be created for long term decisions.

   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)?***

   YES, larger limited liability companies and stock corporations have to appropriate 5% of the annual profit after taxes as long as this reserve does not exceed 10% of the statutory share capital.

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

NO, since January 1, 2005, the rate of corporate income tax has been cut to 25% from 34% for profits. In case of deviating business years, profits derived in 2004/2005 will partly be taxed at 34%, partly at 25%.

Dividends received by an Austrian corporation on domestic investments are exempted from corporate income tax, regardless of the extent of investment and duration of ownership. Any withholding taxes with investment extent of less than 25% are credited against corporate income tax.

Dividends received from another Austrian company are exempted from Austrian corporation tax under the domestic participation privilege. The domestic participation privilege does not require a minimum shareholding or a minimum period of shareholding.

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?**

YES - Explanation and comment of table under Question 1. Benefits are granted for a system of group relief under the group taxation concept under which the profit or loss of a group member as computed for purposes of corporation tax is attributed to the controlling company. For losses, the group relief operates cross borders and is also applicable to non-resident subsidiaries. Losses from non-resident subsidiaries can be offset against group income under the condition that they be recovered if offset abroad in a later year. The only condition for group membership is a direct or indirect majority investment in corporation. The group members have to apply for group taxation with the tax authorities. The group has to exist for at least three years. When leaving the group before expiration the member will be taxed as if it had never been a member of the group.

From 2005 onwards interest on loans taken out to acquire domestic or foreign participations will be tax deductible as long as the arm's length principle is considered. Interest will be deductible regardless of whether the involved companies are part of a tax group or not.

On July 1, 2005, the EU Savings directive (Council Directive 2003/48/EC) became effective. The aim of the directive is to enable savings income in the form of interest payments made in one EU Member State to beneficial owners who are individuals resident for tax purposes in an other EU Member state to be made to effective taxation in accordance with the law of the later
Member State. Austria has not applied the automatic exchange of information at the same time as other Member States. Until 2011 a withholding tax shall ensure an effective taxation. The rate will increase progressively from 15% from 2005 to 2007 to 20% from 2008 to 2010 and finally to 35% in 2011. No withholding tax will be deducted in the case of a certificate in the name of the beneficial owner drawn up by the competent authority in his Member State to the Austrian tax authorities.

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

YES, from 2007 onwards partnerships (as considered as a co-entrepreneurship ("Mitunternehmerschaft") and sole traders will have the possibility of retaining earnings in the amount of EUR 100.000,00 with half the average tax rate (please see under § 11 a EStG).

In 2006 the Austrian federal ministry confirmed the administrative practice with respect to capital contributions made by grand parent companies to

Austrian companies which are not subjected to capital duty. Capital transfer tax at a rate of one per cent is imposed on initial contribution of capital as well as other contractual or voluntary contributions in cash or kind to corporations.

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

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)?

For SMEs tax regulation will be granted from 2004 onwards and retained earnings in the maximum amount of EUR 100.000,00 are possible but may be only activated one time for the calendar year, in which the assets have been bought or manufactured, so that such decisions are short-term related. In contrast to these tax regulations decisions on the level of undertaking and business owner are long-term related (please see under § 11 a EStG)[23].

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. According to the withholding tax for capital gains and dividends is the capital yield tax[24] as final tax ("Endbesteuerung") of 25% shareholders of partnerships, of companies, and sole traders as well are taxed on a progression. But this capital yield tax is credited against other forms of income tax. Most of the double tax treaties are reducing this capital yield tax.

[23] Austrian Tax Reform Act 2004 („Abgabenänderungsgesetz" – „AbgÄG" 2004), BGBl I 2004/180.
[24] § 27 subsection 1 para 1 a EStG ; § 97 subsection 1 and 2 EStG.

In a table form:

19 Countries	INCLUDE RELEVANT TAX PROVISIONS IN 2002 AND SUBSEQUENT CHANGES UP TO 2007	
Country Austria	Undertaking	Individual Business owner
Corporate income tax	25%	Up to a maximum of 50%
Income tax	Up to a maximum of 50%	Up to a maximum of 50%
Dividend tax	25%	25%
Dividend credit	N.A.	N.A.
Capital gains tax	25%	Up to a maximum of 50%
If option for Transparent treatment chosen	N.A., concerning switching between income and corporate income tax	N.A., concerning switching between income and corporate income tax

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?

The withholding tax at the rate of 25% for capital gains and dividends is the final tax (“Endbesteuerung”) for partnerships and sole traders.

Profits resulting from business activity that are distributed are subject to a final withholding tax, also at a rate of 25%; this withholding tax rate may, however, be reduced according to Double Tax Treaties from preventing double taxation.

In a table form:

19 Count ries	INCLUDE RELEVANT TAX PROVISIONS IN 2002 AND SUBSEQUENT CHANGES UP TO 2007			
Country Austria	Distributed profits	Retained Profit	Wages/ Salaries to business owner	Loan to business owner
Sale of shares	0% up to a maximum of 50%-	T€ 100 half the average rate from 2007	Please under sec. 1.8.	Please see under sec. 1.8.
Sale of business	0% up to half the average income tax rate	For T€ 100 half the average income tax rate from 2007	Please see under sec. 1.8.	Please see under sec. 1.8.

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, a combination of wages, profit distributions and retained earnings does constitute a tax planning issue that is anticipated by business owners.

However, as already mentioned above, the (mere) possibility of retaining earning is limited to the (maximum) amount of EUR 100.000,00.- and may be only activated one time for the calendar year, in which the assets have been bought or manufactured, so that it does not constitute a tax planning issue (please see under § 11 a EStG).

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?**

It depends whether the business owner is a private owner or a corporate.

Sole traders and partnerships are subject to income tax up to a maximum of 50%, whilst corporations are subject to a corporate income tax at a rate of 25%.

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, because as Austria is so far concerned sole traders and partnerships are subject to income tax up to a maximum of 50%, whilst corporations are subject to a corporate income tax at a rate of 25%.

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?**

NO

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

N.A.

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?

N.A.

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

As already mentioned as from 2007 onwards partnerships and sole traders will have the possibility of retaining earnings in the amount of EUR 100.000,00.- with half the average tax rate (please see under § 11 a EStG).

14.1. Is there a minimum interest rate to be charged for tax purposes?

N0

14.2. How is the interest rate treated for tax purposes for the Undertaking?

N.A.

14.3. How is the interest rate treated for tax purposes for the business owner?

N.A.

14.4. What are the combined tax effects of such a loan compared to a distribution of earnings equivalent in amount?

N.A.

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

NO, description via case study is not applicable.

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

NO, description via case study is not applicable.

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

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

Interest of debt financing on the basis of qualifying bank deposits or bonds are only subject to 25% withholding tax. No withholding tax is levied on interest income from inter-company loans or sources other than banks or bonds. Interest paid by non-resident companies from loans secured by Austrian-sited immovable properties is subject to income tax either under a reduced rate under a tax treaty or the standard corporate income tax rate.

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?

Generally no withholding tax is levied on interest income from inter-company loans or sources other than banks or bonds. Interest derived by non-resident companies from loans secured by Austrian-sited immovable property is subject to income tax by assessment at the standard corporate income tax rate, unless a reduced rate applies under tax treaty.

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)?

YES, the possibility of retaining earnings (which is applicable as from 2007 onwards), for example, is limited to a maximum amount of EUR 100.000,00.- (please see under § 11 a EStG).

18.1. What is the exact calculation method used to implement this incentive and to evaluate the benefits once this incentive is implemented?

The above mentioned possibility of retaining earnings is based on a specific tax regulation, not on a calculation method.

18.2. Are there any other tax provisions favouring increases in own equity?

Basically, the possibility of retaining earnings is a tax incentive that allows minimizing taxable profits. This possibility is only effective since 2007, but it may be assumed that other tax incentives will be developed.

Furthermore, the 2005 tax reform enables a purchaser to benefit from a step-up in basis; formerly, only an asset deal qualified the purchaser to amortize goodwill and deduct hidden reserves. Due to the 2005 tax reform, a part of the acquisition costs of shares in a corporation (provided that the corporation in question is eligible for group membership) will be treated as goodwill. The amount of goodwill is limited to 50% of the acquisition costs of the shares and may be amortised within a period of 15 years. As a matter of evidence, this part of the 2005 tax reform will increase the attractiveness of share deals.

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)?

YES, compensations for the granting of loans or the conveyance of business assets are basically deemed to be business income and not capital or rental and leasing income.

Capital gains from the disposal of an interest in an Austrian partnership are subject to Austrian income tax if the investor is an individual or to corporate income tax if the investor is a corporation.

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?

NO

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

YES, because the possibility of retaining earnings is limited to the amount of EUR 100.000,00.- and may only be activated during the calendar year, in which the assets have been bought or manufactured, whilst losses may be carried forward for an undetermined period of time and are not limited to a certain amount (please see under § 11 a EStG).

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

YES, the possibility of retaining earnings is limited to the amount of EUR 100.000,00, with half the average tax rate (please see under § 11 a EStG).

On the other hand, a capital transfer tax, at a rate of one per cent is imposed on initial contribution of capital as well as other contractual or voluntary contributions in cash or kind to corporations. In 2006, the Austrian federal ministry confirmed the administrative practice with respect to capital contributions made by grand parent companies to Austrian companies which are not subjected to capital duty.

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

YES, the possibility of retaining earnings is limited to a maximum amount of EUR 100.000,00.- and may be only activated during the calendar year in which the assets have been bought or manufactured (please see under § 11 a EStG).

According to debt financing, there is no limitation as regards to a particular amount and losses may be carried forward for an undetermined period of time.

The problem in Austria is that shareholders capital is treated differently as credit capital. In the first case equity yield rates are not tax deductible whereas in the second case there is an interest subsidy. Debt financing of capital gains distribution are tax deductible but not debt financing of redeeming equity contributions.[25]

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

YES, interest expenses are tax deductible unless they relate to tax exempt income. Interest payments to related parties may be qualified as constructive dividend to the extent that the consideration is not at arm's length or the underlying debt is qualified as hidden equity. If a profit is leveraged and the borrowing is directly linked to the dividend payment the respective interest expenses are also not deductible.

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?

N.A.

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

This could lead to insolvency. Therefore the Austrian enterprise reorganisation Act ("Unternehmensreorganisationsgesetz") includes

[25] § 11 subsection 1 numeral 1 KStG; § 8 subsection 2 KStG; the Administrative Court ("Verwaltungsgerichtshof" – "VwGH") 19.12.2006, 2004/15/0122.

financial ratios in order to define when reorganisation of the enterprise is necessary.

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

NO

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

YES, for example, tax on assets (“Vermögensteuer”) and inheritance tax are of particular importance, bearing in mind that in Austria SMEs represent 99,7% and employ 62% of the Austrian industrial economy. Therefore the kind of conveyance and taxation of assets especially for family enterprises are important for the decision in which country will be invested.

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)?

Income tax on dividends and profit is withheld at source at a rate of 25 %.

Private income, such as interest income from saving deposits and credit balances on current accounts (if paid by domestic credit institutions) as well as interest income from interest-bearing securities (bonds and debentures, mortgage bonds, if the interest paying agency is located in Austria) is subject to 25 % withholding tax.

Non-recurring payments of salaries and wages, e.g. 13th and 14th salaries, bonus payments, etc., enjoy a tax-free allowance of EUR 620,-- per year in the aggregate; the exceeding amounts up to 1/6 of the current annual salaries are taxed at a reduced fixed rate of 6 %.

The corporate income tax rate amounts 25% and applies to any corporation. Irrespective of any profits, Austrian corporations are subject to a minimum corporate income tax for every full calendar quarter, at a rate of 5% of one quarter of the minimum statutory amount of nominal or registered capital (i.e, € 1,750.00.- per year for a GmbH, € 3,500.00.- per year for an AG and € 6,000.00.- per year for an SE).

Profits that are distributed are subject to a final withholding tax at a rate of 25%; this withholding tax rate may, however, be reduced according to Double Tax Treaties from preventing double taxation.

In a table form:

19 Countries	INCLUDE RELEVANT TAX PROVISIONS IN 2002 AND SUBSEQUENT CHANGES UP TO 2007	
Country Austria	Private Investment Income	Business Income
2002-2006	Up to a maximum of 50%	25%

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

YES

Dividends are received tax-free on newly issued shares and profit sharing certificates which were purchased under a special expenses benefit.

If the dividend or interest is paid by an agency abroad, there will be no withholding tax. Starting with April 2003 there is flat tax rate of 25 % payable on this income in order to treat Austrian and foreign investment income equally in conformity with the EU regulations.

Individuals who are resident in Austria are liable to Austrian income tax on their worldwide income.

Individuals who are resident outside Austria are exempt or only liable with respect to specific income sources or assets that are situated in Austria.

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, Interest paid by an Austrian debtor is only subject to 25% withholding tax, if the income is derived from qualifying bank deposits or bonds. Interest income from bank deposits and bonds paid to non-residents is exempt from withholding tax, if the personal details of the non-resident recipient are disclosed to the bank or the debtor. A resident individual's dividend income from the Austrian sources is not subject to further income tax, if 25% has been withheld at source. The withholding tax is the final tax ("Endbesteuerung") for the individual shareholder.

Profits resulting from business activity that are distributed are subject to a final withholding tax at a rate of 25%; this withholding tax rate may, however, be reduced according to Double Tax Treaties.

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

YES, for both it could be a tax deductible expenditure, if the business owner and the enterprise finance the assets by loan.

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

NO, they are included in the taxable income of the business owner and there taxed at the standard rate.

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

NO, as sole traders and partnerships are subject to income tax up to a maximum of 50%, whilst corporations are subject to a corporate income tax at a rate of 25%.[26]

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?

NO, capital gains from private assets are not taxed at a lower rate, as – as already mentioned above sole traders and partnerships are subject to income tax up to a maximum of 50%, whilst corporations are subject to a corporate income tax at a rate of 25%.

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

NO, interest expenses from the private sphere are not deductible. If profit distribution is leveraged and the borrowing is directly linked to the dividend payment the respective interest expenses are not deductible, too.

[26] § 22 subsection 1 KStG.

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

NO, because the possibility of retaining earnings (for the amount of EUR 100.000,00.-/ calendar year) is only possible for profits re-invested by the undertaking (please see under § 11 a EStG).

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

NO, because the possibility of retaining earnings (for the amount of EUR 100.000,00.-/calendar year) is only possible for profits re-invested by the undertaking (please see under § 11 a EStG).

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

YES, as already mentioned, tax on assets ("Vermögensteuer") and inheritance tax are of particular importance and relevance for SMEs, bearing in mind that in Austria these represent 99,7% and employ 62 % of the Austrian industrial economy. Therefore, the kind of conveyance and taxation of assets, especially for family enterprises, are important for the decision in which country will be invested.