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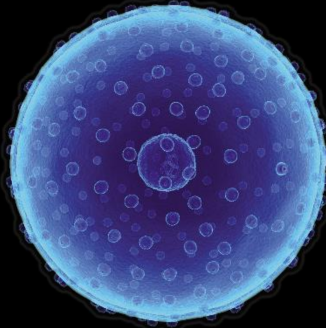

Guidance issued on M&A provisions of the Income Tax Code

Greece's General Secretariat of Public Revenue issued Circular POL. 1057/2017 on 7 April 2017 to provide further guidance and clarifications regarding the application of the merger and acquisition (M&A) provisions of the Income Tax Code ("tax provisions").

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The new circular covers a wide range of issues regarding, *inter alia*, the following types of transactions:

- Transfer of assets in exchange for shares (article 52 of the Income Tax Code);
- Exchanges of shares (article 53);
- Mergers, divisions and partial divisions (article 54);
- Transfer of the registered office of a European Company (SE) or a European Cooperative Society (SCE) from Greece to another EU member state (article 55).

General provisions

The types of Greek legal entity covered by the tax provisions are the *societe anonyme*, the limited liability company and the private company.

Articles 52-55 of the Income Tax Code apply to transactions that were initiated by virtue of a relevant corporate resolution as from 1 January 2014. Only the types of transactions specified above are covered; the tax provisions do not cover other corporate reorganizations (e.g. conversion into another

legal entity type, absorption of a sole proprietorship, etc.). Although the tax provisions apply to partial divisions, there is no corporate law framework for such transactions, rendering the application of the tax provisions a “grey area” in practice.

The procedural aspects and the mechanics of the transaction (e.g. valuation, share-exchange ratio) are determined solely by the corporate law provisions. Previous tax incentives set forth in merger incentive laws (L. 1297/1972, L. 2166/1993) and the law on cross-border transformations (L. 2578/1998) remain in place.

The circular also clarifies that the application of provisions that grant benefits is optional.

Transfers of assets in exchange for shares

- The circular confirms guidance issued under previous merger incentives laws, namely that the assets transferred in exchange for shares must represent a business or a sector of a business that is subject to separate accounting monitoring, and is able to produce its own discernable profit and loss result, although it is unclear for how long a period prior to the transfer such a result is required.

- It is confirmed that participations alone cannot constitute a business sector and that a transfer of assets is not possible when the business sector carved out has negative net equity.

- It is clarified for the first time that real estate assets may comprise a separate business sector provided a relevant management activity also is transferred to the receiving company.

- The tax provisions cover spinoff transactions to both new and existing companies.

- Conversion of a foreign branch into a Greek company is treated as a transfer of assets.

- The transferring company is not subject to tax on goodwill (the difference between the business sector’s value and the value of the shares acquired in exchange) even upon distribution/capitalization, unless this takes place within the first three years following the contribution.

- The receiving company will be subject to tax on the gains realized upon a subsequent transfer of the assets. For this reason, the tax basis for the assets before the transaction carries over to the receiving company. The cessation of operations or a transfer of the Greek permanent establishment (PE) of a foreign company triggers taxation of the gains.

- Tax losses relating to the business sector spun off may be carried forward by the receiving company.

- The spinoff of a loss-making business sector may be challenged as abusive, particularly if the sector spun-off

does not relate to the business activity of the recipient entity.

Exchange of shares

- A share-for-share exchange is, in essence, a contribution in kind by the shareholders of the acquired company, and not a "double sale."

- To apply the tax provisions in the case of multiple shareholders/partners, each must simultaneously acquire shares, and the total shares acquired must represent at least 50% of the shares in the acquired company. It is clarified that the tax provisions also apply where, despite the fact that there is already a 50% majority, the acquiring company opts for an increase in its participation.

- While monetary consideration or treasury shares can be offered as complementary consideration to the shareholders of the acquired company, shares of other companies cannot.

- The circular includes practical examples regarding the scope of the tax provisions. Both the acquiring and the acquired company generally must be Greek and/or EU tax residents.

- For tax benefits to apply, the shareholders or partners of the acquired company should be Greek tax or foreign tax residents, provided the shares (both before and after the exchange) are attributed to a Greek PE.

- After the exchange of shares has taken place, a change of tax residence by a shareholder of the acquired company within a three-year period may be challenged as abusive, unless the shareholder proves it was not aimed at tax avoidance or tax evasion.

- The circular provides for the deferral of income tax and the special solidarity tax on the capital gains from a qualifying transaction. From a tax perspective, a shareholder of the acquired company has a basis in the shares in the acquiring company equal to its basis in the acquired company's shares before the exchange. For accounting purposes, the value of the participation recorded in the books of the acquiring company will reflect the appreciation in value (if any). The capital gains are not taxed at the time of the exchange, but only subsequently when the shares in the acquiring company are transferred by a shareholder of the acquired company. However, the gain that corresponds to any monetary part of the consideration received is taxed at the time of the exchange.

  If the value of the acquired company's shares results in a loss, such loss will not be recognized for tax purposes at the time of the exchange, but only upon the future transfer of the shares in the acquiring company.

  The return of capital by the acquiring company through a share capital reduction ends the deferral and renders the capital gains taxable.

Mergers - Divisions

The circular clarifies the difference between a partial division and a transfer of assets in exchange for shares. In a partial division, the shares of the receiving company are issued to the shareholders of the transferring company, whereas in a transfer of assets in exchange for shares, the shares of the receiving company are issued to the transferring company itself.

Regarding the definition and attributes of a business sector, the circular refers to the guidance provided in the transfer of assets section.

It is clarified that the tax provisions apply to (partial) divisions only where the business sector carved out is located in Greece or in another EU member state and the transferring and the receiving entity are both Greek tax residents, as opposed to a transfer of assets transaction, where the sector can be located anywhere.

Article 54 applies in a case where a Greek receiving company acquires a foreign PE as a result of a transaction in which the acquired assets are located

The tax provisions grant tax deferral on the goodwill (if any) resulting from the transaction. The tax basis of the assets prior to the transaction carries over to the receiving company, and the receiving company must deduct tax depreciation in the same way as the transferring company (same tax rate, same value and method of depreciation).

The receiving entity may carry forward the tax losses of the transferring entity as if no transaction had taken place.

There is no retroactive tax effect for transactions under the tax provisions. The tax year of a newly established receiving company commences upon the registration of the transaction in the company registry (the same rule applies in the case of a transfer of assets).

Any goodwill arising from the cancellation of the receiving company’s (parent’s) participation in the capital of the transferring company (subsidiary) is not taxed, nor is any tax loss recognized. The same applies to the loss, if any, arising from the absorption of the parent company (transferring company) by the subsidiary (receiving company) in a “reverse merger.”

Mergers and (partial) divisions do not give rise to capital gains for the shareholder at the time of the transaction (i.e. the shareholder’s basis in the shares of the acquired company carries over to its new shares in the acquiring company).

Any merger/(partial) division of a company in a loss-making position may be challenged as abusive, particularly if the business activity of the receiving entity prior to the transaction was unrelated.

Transfers of registered office of SE/ SCE

It is clarified that tax deferral on capital gains is granted only in a case where the assets that remain in Greece, after the transfer of the registered office of the SE or the SCE takes place, constitute a PE. Otherwise, any capital gains (e.g. foreign exchange gains, if the only asset is a receivable) are taxed at the time of transfer of the registered office.

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