Sweden:
Proposal to restrict deductions of interest expense revised

On 21 March 2018, the Swedish government presented a revised proposal to restrict the deduction of interest expense and reduce the corporate tax rate. The revisions follow a consultation launched in 2017 that recommended changes to the original proposal (for prior coverage, see World Tax Advisor, 21 July 2017). The proposed measures would implement the EU anti-tax avoidance directive (ATAD I and II) and the relevant recommendations under the OECD BEPS project into Swedish law.


The revised proposal would introduce a general interest deduction limitation rule that would restrict a company’s deduction for net interest expense (the amount of otherwise deductible interest expense that exceeds taxable interest income) to 30% of tax EBITDA. As in the original proposal, the current rules restricting the deduction of interest expense on intragroup debt would be maintained with minor changes, and specific limitations on intragroup hybrid arrangements would be introduced.

The revised proposal also provides for a two-step reduction in the corporate income tax rate: the rate would be reduced from the current 22% to 21.4% in 2019, and then to 20.6% by 2021. The original proposal, which would have reduced the rate to 20% as from 1 July 2018, was rejected.

If approved, the changes would be effective as from 1 January 2019.

Intragroup loans and hybrid arrangements

Under both the original and revised proposals, the current rules that limit the deduction of interest expense on intragroup loans would be modified to disallow deductions of interest expense in situations where a beneficial owner receiving the interest is not located within a country within the European Economic Area (EEA) or a country that has concluded a tax treaty with Sweden, or the interest income is not taxed at a rate of at least 10%. However, even if the deductibility requirements are met, an interest expense deduction would be nondeductible if the purpose of the intragroup loan is exclusively or almost exclusively (defined under the proposal as 90%-95% up to 100%) for the group to achieve a “substantial” tax benefit. Where the loan was obtained to finance an intragroup acquisition of shares, the acquisition would need to be “substantially” motivated by sound business reasons for the interest expense to be deductible.

The revised proposal also maintains the rules in the original proposal that would restrict the deduction of interest expense in certain cross-border hybrid arrangements. A deduction would be disallowed where interest costs that otherwise are deductible in Sweden also may be deducted in another country, or where there is no taxable interest income in another country corresponding to the interest expense in Sweden, and this treatment results from differences in the classification of the payment or in the underlying financial instrument.

General interest deduction limitation rule

According to the revised proposal, a company’s deduction for net interest expense on intragroup and external debt would be limited to 30% of a company’s “tax EBITDA” (instead of 25% of tax EBIT or 35% of tax EBITDA as originally proposed). Tax EBITDA is defined as the company’s taxable income before deductions for net interest expense and tax depreciation on certain assets, interest income, income from Swedish partnerships and foreign legal entities taxed at the level of the owners and changes in the company’s tax allocation reserve. Group contributions made and received would be included when calculating tax EBITDA.

If a company’s taxable result before the deduction of net interest expense is a loss, tax EBITDA would be increased by an amount equal to the tax losses carried forward included in the current year’s taxable result, up to an amount equal to the current year’s tax loss.

The general interest limitation rule would apply to foreign exchange effects (which would be considered interest income or expense) on loans and loan receivables if the currency exposure has been hedged through a derivative. Foreign exchange effects on derivatives where the underlying asset is other than borrowed capital would not be
subject to the limitation rule, nor would the rule apply to foreign exchange effects on accounts receivables and payables.

A safe harbor rule would be introduced (for both intra-EU and non-EU loans), under which net interest expense below SEK 5 million (increased from SEK 100,000 under the original proposal) would be deductible without having to satisfy the general interest deduction limitation rule. For companies that are part of a group, the deduction would be limited to SEK 5 million for the group.

Other rules

- As under the previous proposal, a company that is not able to fully deduct its net interest costs would be allowed to carry forward the excess for up to six years. However, the right to use the net interest expense carried forward would be restricted if there is a change in control of the company.
- Companies with net interest income that are members of a group would be allowed to deduct the interest expense of other group companies. The deduction would be limited to the net interest income of the company, and would be allowed only where both companies are able to exchange tax-deductible group contributions under Swedish tax law.
- The revised proposal does not include rules in the original proposal that would give the leaseholder in a finance lease a depreciation right.
- The revised proposal does not include any limitation on utilizing tax losses carried forward from previous years.

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