Norway issues regulations on exemptions to the new interest deduction limitation rules

Executive summary

The Norwegian interest deduction limitation rules were introduced with effect from 1 January 2014. On 24 April 2014, Norway’s Ministry of Finance issued regulations regarding exemptions to the interest deduction limitation rules. The exemptions apply to situations involving external loans secured by a related party. These situations are summarized below.

Detailed discussion

The Norwegian interest deduction limitation rules state that interest expense would be fully deductible against interest income. Interest expense exceeding interest income (i.e., net interest expense) could be fully deducted if the total amount of net interest expense does not exceed NOK 5 million during the fiscal year or if the interest is paid to a non-related party. Otherwise net interest expense paid to a related party is deductible only to the extent that internal and external interest expense combined does not exceed 30% of taxable EBITDA (earnings before interest, taxes, depreciation and amortization).

The adopted interest deduction limitation rules also generally apply to external loans guaranteed by a related party of the borrower (tainted debt). However, the Ministry of Finance issued regulations according to which the following securities arrangements will not be covered by the interest deduction limitation rules:

- Situations where an external loan obtained by a parent company (the borrower) is secured or guaranteed by a subsidiary (upstream guarantees), provided the borrower directly or indirectly owns at least 50% of the shares in said subsidiary. The subsidiary can be based in or outside Norway. Any form of guarantee or security is covered by this exemption.
• Situations where an external loan obtained by a company (the borrower) is secured by a pledge in the shares of the borrower held by another company.

• Situations where an external loan obtained by a company (the borrower) is secured by a receivable on the borrower held by another company.

Situations where an external loan obtained by a company (the borrower) is “secured” by a negative pledge granted by a company in which the borrower has a direct or indirect ownership interest are not covered by the interest deduction limitation rules.

With these regulations the Norwegian interest deduction limitation rules are complete.

The regulations enter into force immediately and with effect from the same date as the interest deduction limitation rules, i.e., from the income year of 2014. Thus, the adopted provision provides a clarification as to the rules that have already been in force for the last four months.

It is anticipated that a complaint against Norway may be filed before the EFTA (European Free Trade Association) Surveillance Authority as the interest deduction limitation rules appear to be in breach of the freedom of establishment under the European Economic Area Agreement.

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Endnote

1. For further description of the new rules, see EY Global Tax Alerts, *Norway releases 2014 Budget with proposals on new interest deductibility restrictions and reduction of corporate income tax rate* and *Norway’s new Government issues amendments to 2014 Budget*, dated 15 October and 8 November, 2013 respectively.
For additional information with respect to this Alert, please contact the following:

**Ernst & Young AS, Oslo**
- Øyvind Hovland +47 24 00 22 38 oyvind.hovland@no.ey.com
- Aleksander Grydeland +47 24 00 22 30 aleksander.grydeland@no.ey.com
- Kari Augestad-Dyrhaug +47 24 00 29 51 kari.dyrhaug@no.ey.com

**Ernst & Young LLP, Scandinavian Tax Desk, New York**
- Martin Norin +1 212 773 2982 martin.norin@ey.com
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