Amendments to the Slovak legislation and other topics

Welcome to our February issue of Tax & Legal News. In this issue we outline information on the following topics:

- New treatment of overdue liabilities from a corporate income tax perspective,
- OECD released an initial draft of revised guidance on transfer pricing documentation,
- Tax deductibility of costs for expired goods,
- European Commission approves new regional aid map 2014- 2020 for Slovakia,
- Crime of obstruction of tax administration.

We wish you a pleasant read.

New treatment of overdue liabilities from corporate income tax perspective

One of the major changes, brought about for most entities by the amendment of the Income Tax Act effective as of 1 January 2014, is the change in the taxation of overdue liabilities relating to tax deductible costs or accounted for as a decrease of revenues (e.g. due to rebates provided).

The new amendment unifies the time rules regarding the increase of the tax base by the amount of overdue liabilities with tax deductibility rules for bad debt provisions. According to the amended Article 17 (27) of the Income Tax Act, a gradual increase of the tax base shall vary from 20% to 100% of the nominal value of the outstanding liability (or outstanding part) depending on the overdue:

a) 360 days, the tax base shall be increased by at least 20 % of the nominal value of the outstanding liability (or outstanding part thereof);

b) 720 days, the tax base shall be increased by at least 50 % of the nominal value of the outstanding liability (or outstanding part thereof);

c) 1080 days, the tax base shall be increased by at least 100 % of the nominal value of the outstanding liability (or outstanding part thereof).

In this context, it is important to note that the maturity of liabilities cannot be extended for tax purposes.

Furthermore, according to new Article 17 (32) of the Income Tax Act, if the tax base was increased by 100% of the nominal value of the outstanding liability (or outstanding part thereof) and the liability (or outstanding part thereof) was paid, the tax base can be reduced by the amount of the paid liability in the tax period, in which the liability was paid. The current wording of the Income Tax Act does not directly address situations where liability has been settled after the income tax base was increased by less than 100 % of the nominal value of liability (or outstanding part thereof).

If the liability has become time-barred or extinguished, the tax base shall be reduced by the amount of the booked revenue in the tax period, in which the revenue is booked. According to the Civil Code, the general imitation period is three years and pursuant to the Commercial Code, it is four years.

The new legal treatment may require more detailed monitoring of overdue liabilities than until the end of year 2013, when only liabilities overdue more than 36 months impacted the tax base.

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OECD released an initial draft of revised guidance on transfer pricing documentation

On 30 January 2014, the Organisation for Economic Cooperation and Development (OECD) released the discussion draft on transfer pricing documentation and country-by-country reporting (Discussion Draft) pursuant to Action 13 under the Base Erosion and Profit Shifting (BEPS) Action Plan. The Discussion Draft of the guidance is intended to replace Chapter V of the current OECD Transfer Pricing Guidelines. Public comments on the Discussion Draft are requested on or before 23 February 2014.

The Discussion Draft proposed a two-tiered approach that would present global master file with local country files. The master file would provide information about the global operations of multinational entity group (MNE group) and local country file that would document the material transfer pricing positions of the local taxpayer with its foreign affiliates. The master file is proposed to include also country-by-country reporting of information regarding the group's global allocation of profits, taxes paid, and other indicators of the location of the group's economic activity among countries in which the group operates.

To ease compliance burden, the Discussion Draft recommends updating the comparable financials on an annual basis and comparable sets would be refreshed every three years as long as the operating conditions are unchanged.

The OECD recommends the preparation and submission of the master file in English and preparation of the local file in the local language; relevant parts of the master file should also be translated into the local language. At the moment the Slovak Tax Authorities usually require master files to be submitted in the Slovak language. Changing this approach in the future would further reduce the compliance burden.

We will keep you updated on further developments in this area

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Deductibility of costs of expired goods

In the recent months we have noted that tax audits challenge the deductibility of costs relating to expired stock more often. According to our experience, the approach of the Tax Administration is in this case mostly negative. The Tax Authorities consider the moment, when the maximum durability or use-before period is exceeded as an event of irreparable damage to the goods as the goods are not allowed to be sold or to be repaired so that they would be appropriate again for human consumption. According to the tax authorities, the costs relating to the expired goods are to be considered as damage, which is not tax deductible pursuant to Article 21 Section 2 Letter e) of the Act no. 595/2003 Coll. on Income Tax.

The above opinion is based on incorrect interpretation of definition of damage which is stated in Article 26 Section 6 of the Act no. 431/2002 Coll. on Accounting and from several decisions of the Supreme Court of the Slovak Republic. The decisions were based on wording of the law, which was no longer effective as well as on different factual background and therefore such conclusions should not be generally applied.

In case of tax audit we will be glad to assist you and protect deductibility of the expired or obsolete stock. In case of failure in the first instance proceedings our Tax and Legal department would be glad to represent you in the appellate proceeding and/or in court proceedings.

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European Commission approves new regional aid map 2014- 2020 for Slovakia

The European Commission approved the new regional aid map on 2014-2020 for Slovakia on 22 January 2014.

The new regional aid map defines the regions of a Member State eligible for national regional investment aid under the EU state aid rules and establishes the maximum aid levels for companies in the regions of an EU member state.

The regional aid map divides Slovakia into 4 regions and the below table compares the current state aid intensity ceiling with the ceilings to be applicable as of 1 July 2014:

	Current regional aid ceiling	New regional aid ceiling
Bratislava region	0%*	0%
Western Slovakia	40%	25%
Central Slovakia	50%	35%
Eastern Slovakia	50%	35%

*0% effective as 1 January 2009

The maximum intensity of state aid for small and medium enterprises may be increased by 20% and 10% respectively. Note that the Ministry of Economy has set the intensity ceilings in most regions (okres) on a lower level, so the above reduction may not have an adverse impact. However this question should be addressed on a case by case basis.

Please note that you can still apply for aid on the basis of the current ceilings. However the application process needs to be completed by 30 June 2014.

We anticipate that the current Investment Aid Act will be amended in order to align with all changes under the EU state aid legislation which will also take effect as of 1 July 2014. We will inform you as soon as we have the new draft.

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Crime of obstruction of tax administration

With the effect from 1 October 2012 the amendment to Act No. 300/2005 Coll. the Criminal Code has introduced a new special crime of obstruction of tax administration.

Attempts to avoid tax duties from the side of taxpayers were the reason behind the adoption of the new criminal offence definition.

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Especially in those situations, when the taxpayer gained suspicion that the tax authorities had identified circumstances, which might lead to additional tax liability or refusal to recognise a claim for excess deduction. Subsequently, the taxpayer cut off communication with the tax authorities, submission of information necessary for correct determination of tax, fulfilment of its obligations, or receipt of mail from tax authorities.

The new crime is based on penalizing repeated breach of tax law rules. The crime of obstruction of tax administration is committed by a person who *(i) states untrue or seriously distorting information about facts crucial for correct determination of tax duty in documents submitted in the course of tax administration, (ii) amends, damages or destroys documents required for correct determination of tax duty, (iii) does not fulfil his notification duty stipulated by law, or (iv) does not fulfil his duty imposed on him in a tax inspection, in spite of having been convicted for the same crime during the past twelve months. Under convicted for the same crime is to be understood a person who had been imposed a penalty for a similar act or another measure for an offence or other similar delict (save for expunged penalties or measures).*

Obstruction of tax administration occurs most commonly in practice through acts against the accounting of a taxpayer; in particular that a taxpayer does not keep accounts properly, falsifies accountancy or destroys accounting records.

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In one sentence …

- The Slovak Ministry of Finance issued a list of valid and effective international treaties based on article 2 letter x) of the Act No. 595/2003 Coll. as amended (i.e. a list of contractual states, in the case of which the increased 35% withholding tax rate and 35% security tax rate will not apply). The list is only informative before 1 March 2014 and may not be complete yet; you can find it here: http://www.finance.gov.sk/Default.aspx?CatID=9501
- The Slovak Financial Directorate released the following guidelines and notifications:
  - Guideline on claiming the input VAT deduction by foreign persons registered for VAT purposes according to Article 5 of the Slovak VAT Act via VAT return filed after 1 October 2012,
  - Guideline on application of Article 69 Section 12 Letter h) and i) of the Slovak VAT Act,
  - Information on the Amendment to the VAT Act effective as of 1 January 2014.
- With respect to the new obligation of the VAT payers to file the VAT Ledger Statement (to be filed for the first time by 25 February 2014 for January 2014) the Slovak Financial Directorate released the following guidelines:
  - Guideline on filing the VAT Ledger Statement,
  - Guideline on stating the VAT identification number of the customer or of the supplier in the VAT Ledger Statement,
  - Guideline on reporting the acquisition of goods from another EU Member State in Slovakia in the VAT Ledger Statement,
  - Guideline on reporting the correction invoices in the VAT Ledger Statement.
- VAT rates applied in the EU Member States. The European Commission released a report listing the value added tax (VAT) rates applicable in the EU Member States as at 13 January 2014. You can find this here: http://ec.europa.eu/taxation_customs/resources/documents/taxation/vat/how_vat_works/rates/vat_rates_en.pdf
- Public consultation on VAT legislation on public bodies and tax exemptions in the public interest. The European Commission, in line with an initiative to create a simpler, more efficient and more robust VAT system in the EU, invited all interested parties to submit their contributions in response to the questions raised in the consultation paper „Review of existing VAT legislation on public bodies and tax exemptions in the public interest". The closing date for sending contributions is 25 April 2014. You can find the consultation paper here: http://ec.europa.eu/taxation_customs/resources/documents/common/consultations/tax/public_bodies/consultation_document_en.pdf
- New Civil Code, Act on Business Corporations and Act on Private International Law became effective in the Czech Republic from 1 January 2014. The new private law code has materially changed existing legal regulation (e.g. personal rights, contractual types, bona fide protection), as well as introduced new legal institutes (e.g. superficies solo cedit, new concept of a thing).

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