Amendments to Slovak legislation and other topics

Welcome to our January issue of Tax & Legal News. In this issue we have prepared information for you on the following topics:

- **Changes which may affect you in the preparation of income tax returns,**
- **Changes in the corporate income tax return form,**
- **The real estate tax and motor vehicle tax,**
- **Default interest on delayed refund of VAT excess deduction.**

We wish you pleasant reading.

Changes which may affect you in the preparation of income tax returns

In this article we would like to draw your attention to some changes of Act No. 595/2003 Coll. on Income Tax as amended (hereinafter "the SITA"), which were introduced by recent law amendments and may have significant impact on the tax base of taxpayers in Slovakia within filing corporate income tax returns after 31 December 2015 and for tax periods starting on 1 January 2015 at earliest. It should be noted that in case of taxpayers with tax period starting before 1 January 2015, who will file corporate income tax returns after 31 December 2015, it is necessary to assess which changes apply to them.

- **Terminated investments**

If long-term assets were acquired and the termination of the investment is not a damage, the costs for the cancelled investments are included into the tax base on a straight-line basis for a duration of 36 months starting from the month in which the investment and the works were cancelled in the books of the taxpayer.

- **Costs tax deductible upon their payment**

The following items are included into the tax base on a cash basis, i.e. after actual settlement:

- **Compensation payments** paid in line with the Act on regulation in the network industries at the (level of the) debtor,
- **Costs (expenses) of rental:** rental paid to an individual are tax deductible only up to the amount that is attributable to the respective taxable period on an accrual basis,
- **Costs for marketing and other studies**, costs for market research while such revenues are included into the tax base of the creditor after the payment is received,
- **Compensations for intermediary services** – also applies if the intermediary services are based on a mandate and similar contracts, however, only up to a maximum of 20% of the value of the mediated business (the limit is not applied to selected taxpayers explicitly listed in the SITA),
- **Costs (expenses) connected to the payment**

of Slovak sourced income paid to a taxpayer from a non-treaty country and at the same time after the fulfilment of the obligation to withhold withholding or security tax and give notification of this to the tax authorities,

- **Expenses for advisory and legal services:** accounting services, bookkeeping, audit and tax advisory services (code 69.2 of the Statistical Classification of Products); as regards legal services, these include advisory services, representation in various proceedings as well as notarial services (code 69.1),
- **Costs for obtaining norms and certifications:** these are included in the tax base on a straight-line basis during the period of their validity, however not more than 36 months, starting from the month in which the taxpayer paid these costs; costs for obtaining norms and certifications not exceeding acquisition value of EUR 2,400 are included in the tax base at once.

- **Contractual penalties**

Contractual penalties are not tax deductible regardless of their settlement.

- **Expenses incurred by the employer on the taxable income of the employee**

Such expenses (including travel allowances) exceeding the limits specified in the Labor Code or the Act on travel expense reimbursements are considered as tax deductible expenses of the employer provided that they represent taxable income in the hands of the employee.

- **Expenses on the acquisition, technical improvement, use, repairs and maintenance of assets**

Except for certain specific cases (e.g. costs on immovable, costs incurred by employer providing non-monetary income in form of usage of cars for personal purposes to its employees etc.) costs incurred on acquisition, technical improvement, use, repairs and maintenance assets for one´s personal use should be tax deductible in 80% or in demonstrable amount depending on the ratio of their usage for an assurance of taxable income.

- **Membership fees**

Membership fees arising from the voluntary membership in an entity, the purpose of which is the protection of the interests of the taxpayer, is tax deductible in an aggregate of 5% of the taxable base, but not exceeding EUR 30,000 annually.

- **Compensation for the collection of receivables**

Costs incurred with respect to the compensation for the collection of a receivable are tax deductible only up to 50% of the collected receivable.

- **Reserves**

Creation of reserves for unbilled supplies of goods and services, for the preparation and audit of financial statements and annual report and for the preparation of the tax return are tax non-deductible expense.

- **Bad debt provision against to accessories to receivable**

Bad debt provision against to accessories to receivable is considered as tax deductible cost at the earliest in the tax period in which from the due date of receivable (to which accessories relate) the period of more than 1 080 days elapses and provided that the accessories were included in taxpayer's taxable income.

- **Write off of receivables including accessories**

If taxpayer writes off of receivables including accessories, the write off of accessories can be considered as tax deductible cost provided that the creation of bad debt provision against to these accessories would be considered as tax deductible cost (accessories were included into taxpayer's taxable income and from the due date of receivable, to which accessories relate, the period of more than 1 080 days elapsed).

- **Cession (assignment) of receivables including accessories**

If taxpayer assigns (transfers) the receivable including accessories, in case of accessories as tax deductible cost is considered only cost up to income received under assignment which is connected to accessories. Accessories should have been included in taxable income.

- **Expenses on the promotional items**

Promotional items having value per piece not higher than EUR 17 are tax deductible. The specific items cannot be considered as promotional items:

- gift promotional vouchers,
- tobacco products; except for producers of tobacco products,
- alcoholic drinks except for wine up to 5% of the tax base; however, this restriction is not applied for producers of alcoholic drinks.

- **Earning stripping rules**

The interest exceeding 25% of the value of the indicator calculated as the accounting result before tax declared based on the local accounting rules or the IFRS increased by the included depreciation and interest costs, should be treated at Slovak tax residents and permanent establishments of tax non-residents as tax non-deductible. These rules should apply on the related legal entities and does not apply on entities engaged in financial sector. The restriction of tax deductibility of the interest should not be applicable on loans from which the interests are capitalized in compliance with accounting legislation.

- **Tax depreciation charges or rental of vehicles with acquisition value of EUR 48,000 and more**

The specific formula for calculation of adjustment of tax base for vehicles categorised into 29.10.2 should be applied in case of insufficient level of tax base. Insufficient level of tax base is calculated as number of these vehicles and depreciation charges

calculated from limited acquisition value of EUR 48,000 (not applicable to lessor in case of operational leasing) or limited rental of EUR 14,400 per year. A tax increasing item calculated thereof (if any) is a permanent difference since it is not reflected in residual tax value of the respective assets.

- **The tax depreciation charges of rented tangible assets**

The tax depreciation charges of rented tangible assets may be deducted only up to the accrued income from rentals related to the respective tax period.

Tax depreciation charges, which were not applied during the rental period, will be applied starting in the year following the end of tax depreciation period of respective asset, but up to amount of income from rental.

In case that these assets are not rented after ending of depreciation period, but are still used for taxpayer's activities the taxpayer is entitled to claim tax depreciation charges, which were not applied during the rental period, but yearly up to amount of annual tax depreciation charges according to the respective tax depreciation group.

The amount of tax depreciation charges of rented assets included into tax deductible costs of taxpayer who rents these assets during only part of tax period or rents only part of these assets should be determined according to the scope and duration of lease.

- **Tax residual value of selected assets**

Tax residual value of selected assets (e.g. certain cars and buildings included in the tax depreciation group 6) is tax deductible only up to the income from their sale, i.e. a loss from the sale of the selected assets is recognized for tax purposes. However, within calculation of the tax residual value of respective assets sold during the year the taxpayer can apply the tax depreciation charges in the amount corresponding to the number of the whole months, during which the assets were booked or recorded. Such limitation of tax deductibility of tax residual value is not applied in case of technical improvement of rented property classified in tax depreciation group 6.

- **Tax depreciation**

Effective from 1 January 2015 further changes relating to **tax depreciation of assets** were introduced, inter alia, following:

- **The depreciation charges of assets** are tax deductible in the same proportion as used for the tax deductibility of costs incurred on **acquisition, technical improvement, use, repair and maintenance of the respective assets** (please see above).
- **The tax depreciation groups were broadened** to 6 with a maximum tax depreciation period amounting to 40 years. The classification of assets into the tax depreciation groups were changed in certain cases – e.g. the administrative buildings are tax depreciated over 40 years rather 20 years.
- **Accelerated tax depreciation** is possible only in the case of assets included in the 2nd and 3rd tax depreciation group.
- The tax payer is obliged to perform the changes in respect of the tax depreciation method, tax depreciation group, tax period, tax depreciation rate or coefficient also for assets acquired and depreciated before 1 January 2015. The tax depreciation charges applied in the previous tax periods are not affected.

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Changes in corporate income tax return form

On 20 October 2015, the Ministry of Finance of the Slovak Republic issued Guideline No. MF/16772/2015-721 stipulating income tax return form templates. Compared to the last year, several changes have occurred in the following sections:

- Part I. TAXPAYER DETAILS - a new checkbox was added "offsetting the tax license according to Article 46b Section 5 of the Act" and the original field "do not pay license tax" was changed to "non-payment of tax license according to Article 46b Section 5 of the Act".
- Part II. TAX BASE AND TAX CALCULATION – new parts:
  - Adjustments to the tax base or tax loss (e.g. in connection with limiting tax depreciation and annual rent for cars with an entry price of more than EUR 48 000, membership fees, promotional items and etc.),
  - The tax allowance (deduction of expenditure on research and development),
  - License tax credit from previous taxable periods.
- Part III. AUXILIARY CALCULATIONS AND ADDITIONAL DATA TABLES – the change in the structure of individual lines of the tax return form and the change in the title of the point D and the point F.
- Part IV. DECLARATION OF REMITTANCE OF A PORTION OF A LEGAL ENTITY´S INCOME TAX PAID - three lines were removed, which has caused shortening of the entire section and the new checkbox "I agree with sending information (business name, registered office and legal form) to the intended recipient(s) of share of paid tax according to Article 50, Section 8 of the Act" was added.
- With respect to the new tax return form templates new appendices were added:
  - The "Annex to Article 30c of the Act - Deduction of expenses (costs) for research and development and data about Research and Development

projects according to Article 30c of the Act",

- The "Annex to the part IV. – Information about other beneficiaries".

- The original part VII - "Shares on profit (dividends) that are taxable according to Article 51d, Section 3 of the Act" was deleted from the new form.

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The real estate tax and the motor vehicle tax

If you are entrepreneur who used a vehicle for business purposes during the year 2015, or a person who acquired or sold a property during the year 2015, bear in mind that the deadline for filing a tax return for the motor vehicle tax and for the real estate tax is 1 February 2016. Although the legitimate deadline for filing a tax return is 31 January, due to a non-working day the deadline is shifted to 1 February (Monday).

The motor vehicle tax

The entrepreneurs who used a vehicle for business purposes are required to pay the tax liability for the tax period of 2015 by the same deadline as applies for filing of the tax return, i.e. by 1 February 2016.

When talking about the major changes in the law, the motor vehicle tax is to be paid where the entrepreneur is established and not in the municipality where the car is registered. It is advantageous mainly for the companies, which were used to file several tax returns according to the city where the vehicles were registered. From now on, the entrepreneur files only one tax return for all registered vehicles.

The annual tax rate depends on the age of vehicles - the older the vehicle is, the higher rate is used; and the environment-friendliness – the less harmful to the environment is the car, the lower rate is used.

The tax rates are fixed for the whole territory of Slovakia and may be found in the annex to the Act on the motor vehicles tax.

The real estate tax

If you had acquired a property during the last year, you are obliged to file a tax return to real estate tax not later than on 1 February.

The persons are obliged to file a tax return if they acquired (they bought, had a final inspection or inherited) a property; sold a property (if they are no longer registered with the land registry as of 1 January 2016) or in the case when such changes occurred having an impact to assessment of taxes (e.g. the change of land area) within 2015.

We would like to draw your attention to a fact that the tax return is to be filed only if there were changes during the last year, i.e. if you had filed the tax return in January 2015 and nothing has changed with respect to your property, you are not obliged to file a tax return again but the Tax Authorities will send you a payment instruction by May 2016.

The real estate tax rates may be found in regulations published by each self-governed region.

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Default interest on delayed refund of VAT excess deduction

On 21 October 2015, the Court of Justice of the European Union ("CJEU") released a reasoned order in Case C-120/15 Kovozber s.r.o.
This order deals with conditions of a default interest on delayed refund of VAT excess deduction.

The Case

The company Kovozber s.r.o. ("Kovozber") declared a VAT excess deduction in their VAT return for the month of July 2007, filed on 25 August 2007.

On 14 October 2007, the tax authorities started a tax audit to verify the eligibility for refund of the VAT excess deduction. This tax audit was completed on 7 March 2008. The tax authorities recognized the taxpayer's right for refunding the VAT excessive deduction, the amount of which was repaid to the taxpayer on 13 March 2008.

Kovozber held a view that they were entitled to have the funds at their disposal already on 25 September 2007 and not on the expiry of a period of 10 days from completion of tax audit. Therefore, the company applied for payment of default interest calculated from then 31st day after the deadline for filing the VAT return for the relevant VAT period until the date of repayment of the VAT excess deduction.

After rejecting the application by the tax authorities, Kovozber decided to bring legal action before competent national court.

Questions referred for a preliminary ruling

The national court conveyed that the Slovak legislation does not govern awarding default interest on delayed refund of VAT excess deduction and lacks regulation that would define circumstances under which the refund of VAT excess deduction is considered as delayed.

Based on the above, the court referred the following questions to CJEU for a preliminary ruling:

1. Whether the first paragraph of article 183 of EU VAT Directive 2006/112/ES must be interpreted as precluding national legislation which, in determining the conditions for refunding an excess deduction of VAT, makes the award of default interest (on the delayed refund of VAT) conditional on the expiry of a period of 10 days from completion of the tax audit focused on ascertaining the eligibility for the refund;
2. If the answer to the first question 1 is in the affirmative, the national court sought for a ruling on obligations in terms of application of the existing rules based on the domestic legislation.

Reasoned Order

The CJEU admits that Article 183 of the EU VAT Directive does not lay down any obligation to pay interest on a refund of excess VAT or the date from which such interest is payable. On the other hand, the court refers to judgments in cases C-107/10 Enel Maritsa Iztok 3 and C-431/12 Rafinăria Steaua Română. CJEU reminds that it cannot be concluded from that aforementioned fact alone that that provision must be interpreted as meaning that no control may be exercised under European Union law over the procedures established by EU member states for the refund of excess VAT.

When determining the procedures, the EU member states must ensure adherence to the general principles

of VAT. Inter alia, the conditions set cannot undermine the principle of fiscal neutrality by making the taxable person bear the burden of the VAT in whole or in part. In particular, such conditions must enable the taxable person, in appropriate circumstances, to recover the entirety of the credit arising from that excess VAT. This implies that the refund is made within a reasonable period of time by a payment in liquid funds or equivalent means, and that, in any event, the method of refund adopted must not entail any financial risk for the taxable person.

On the other hand, the court acknowledged that EU member states are, with the aim of ensuring proper collection of VAT, required to check taxable persons' VAT returns and the underlying documentation. It follows that the period for refunding excess VAT may, as a general rule, be extended in order to carry out a tax investigation without there being any need for such an extended period to be regarded as unreasonable provided that the extension does not go beyond what is necessary for the successful completion of the investigation.

The CJEU emphasized that a taxable person is at an economic disadvantage if deprived on a temporary basis of funds corresponding to the excess VAT. This disadvantage should be compensated for by payment of interest, thus ensuring compliance with the principle of fiscal neutrality.

The court referred to the national legislation, based on which starting a tax audit results in retention of funds totaling to the amount of excess VAT for a time period, which could be significantly longer than a VAT period equal to a calendar month. Based on this, the CJEU concluded that the national legislation is not compliant with the principle of fiscal neutrality, based on which the refund must be made within a reasonable period of time.

The CJEU made a remark on the domestic law, which allows the tax authorities to start a tax audit any time, even immediately before the deadline for repayment of the VAT excess deduction. In CJEU's view, this enables a significant extension of the time period for refunding the excess deduction, which makes taxable persons exposed to economic disadvantage.

Moreover, the taxable persons cannot foresee the date from which they will again have the funds at their disposal. In such case, the taxable person is, according to the court, entitled to a compensation in form of a default interest. The date on which the excess VAT would have had to be repaid in the normal course of events in accordance with the VAT Directive, should be taken as the starting point when calculating the interest.

As for the conditions for payment of default interest, the CJEU mentioned that it is not within its competence to interpret a domestic law or to apply the EU law. It is up to the national court to verify the adherence to the principles of equivalence and effectiveness in the case at hand or to secure the adherence to these principles. The national court must, within its authority, apply the EU law in its entirety and it is under its duty to give full effect to the EU law.

The CJEU concluded that Article 183 first Section of the EU VAT Directive 2006/112/EC is to be interpreted as precluding national legislation under which the default interest (on the delayed refund of VAT) upon the sum of the refunded excessive deduction is calculated as of the expiry of the 10 days period after the completion of the tax audit.

This ruling can bring hope to the taxpayers as regards their demands for default interest from the funds retained during unreasonably long lasting tax audits focused on verification whether the claim to the refund of the excess deduction is justified, and potentially a perspective of reducing the duration of such tax audits as well.

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In one sentence

The Slovak Financial Directorate released inter-alia the following guidelines and information:

Value added tax

- Guidelines on domestic reverse-charge on supply of construction works in accordance with the Article 69, par.12 letter. j) of the VAT Act
- Guidelines on settlement of the VAT liability upon receipt of the payment from the customer according to the Article 68d of the VAT Act
- Guidelines on VAT deposit
- Guidelines on the application of a reduced VAT rate on selected food products listed in the Annex. 7 to the VAT Act
- Guidelines on the classification of construction works to the section F of the statistical classification of products

Income tax

- Guidelines on payments of corporate income tax prepayments according to the Article 42 of the Income Tax Act
- Information about the publication of the template forms in relation to the income from dependent activities
- Information on consideration of cost for promotional items as tax deductible costs in 2015
- Information on consideration of creation of value adjustments to receivables and write-off of accessories to receivables as tax deductible costs
- Information about changes in taxation of monetary and non-monetary considerations paid/provided by holder to health care provider as of 1 January 2016

Motor vehicle tax

- Information on filing of motor vehicle tax return for the year 2015
- Information on filing of motor vehicle tax return by a taxpayer dissolved without liquidation, in

liquidation or in a bankruptcy and after the death of the taxpayer

- Information on the notification obligation according to the Motor Vehicle Tax Act

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