CE Tax&Legal Highlights
April 2018

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Czech Republic

R&D Tax Deduction
Regional Court: Clinical Trials of Medicaments Classified as Research

We would like to provide additional information on legal disputes concerning R&D deductible items, this time in the area of clinical studies. In late February, the Regional Court in Hradec Králové issued new judgments cancelling the ruling of the Appellate Financial Directorate (the "AFD"). Below is a summary of the key findings.

The Company won two legal disputes with the AFD pursuant to judgments 31 Af 53/2016 - 52 and 31 Af 52/2016 – 60. The Company sought the cancellation of the ruling whereby the AFD rejected the Company's appeal against additional corporate income tax payment assessments for the taxation periods of 2011, 2012, 2013 and 2014 whereby the assessments were confirmed. The subject matter of the dispute included the AFD's ruling stating that the Company did not carry out research and development in line with Section 34 (4) of the Income Taxes Act.

The Company is a registered medical facility conducting clinical studies predominantly of phase III, ie systematic testing of medicaments on patients to demonstrate and verify the healing powers of the medicament and identify side effects. This includes the testing of already-developed medicaments following the completion of clinical testing phases I and II, according to the assignments of the Company's clients.

The AFD concluded that the Company had been engaged in an activity classified as the provision of services to a third party without own research as it only recorded the results of individual patients included in the project in relation to the administered medicaments. Moreover, the AFD believes that the administered medicaments did not represent an outcome of the Company's research and development activities and, as a result, this service did not include the element of own research. The AFD thus concluded that the Company's activities in the respective projects did not include an appreciable element of novelty and the Company was not exposed to the risk and uncertainty arising from research and development.

Nevertheless, the Regional Court did not agree with this conclusion and confirmed the Company's opinion that the activity in an R&D project consisted of seeking new findings regarding the effectiveness of medication and was performed by qualified professionals, which brought new findings on the healing powers of the respective medicament. What is more, the Regional Court also agreed with the Company's opinion that as such, the Company's performance of medical research entails the risk of failure of such research. This risk lies in the fact that it may come out during the clinical study that the testing practitioner incorrectly assessed the effects of administered medicaments and, as a consequence, failed to identify the danger for human health.

Therefore, the Company is not engaged in a mere routine activity solely including the record-taking of the results. The Regional Court believes that the Company's activities met the definition of research and development.

The Regional Court observed an unlawful assessment of the matter by the AFD in terms of substantive law and returned the case for further proceedings. The AFD subsequently filed a cassation complaint against the judgment at the Supreme Administrative Court. **This judgment is one of the few judgments at the level of regional courts which agreed with the taxable entity, observing that the definition of R&D activities and costs reported in a tax return was met.**

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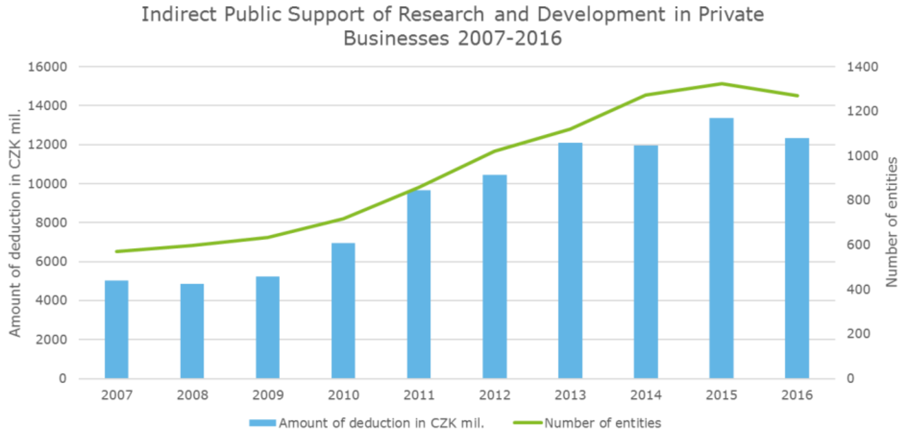
Current Trends in the Area of Deduction

As we have informed you in previous articles, R&D tax deductions are increasingly more often examined by the tax administration. The growing number of audits, which often result in legal disputes, leads to uncertainty among taxpayers. It is therefore questionable whether the setup of the deduction aimed at supporting research and development is the only accurate solution and whether it is time to consider an adjustment thereto, also considering the fact that the area has not been modified since 2005.

A decrease in the number of entities using the R&D tax deduction between 2015 and 2016 as well as a decrease in the aggregate costs reported by businesses as part of the R&D tax deduction in the same period proves the growing uncertainty among companies engaged in research and development in the Czech Republic arising from the tax administration's approach to the audit of tax deductions. This is alarming especially due to the fact that the decrease was recorded for the first time since 2005 when the R&D tax deduction was incorporated into legislation and also with regard to the boom in the Czech economy at present.

The figure below clearly depicts the statistics of applying the R&D tax deduction using the data of the Czech Statistical Office.



	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Amount of deduction in CZK mil.	5 017	4 857	5 246	6 931	9 665	10 435	12 090	11 954	13 351	12 337
Number of entities	570	596	632	716	859	1 021	1 120	1 271	1 322	1 268

Source: Czech Statistical Office

We consider it problematic that formal project elements are currently preferred to the fact whether the company conducts research and development. Rather contradictory statutory requirements placed upon the research and development project documentation pose another issue. This includes, on one hand, the definition and approval of research and development activities prior to their commencement when the taxpayer does not (and cannot) have detailed solution descriptions as well as a sufficiently accurate and detailed definition of activities, including their timing, budget, staffing etc, on the other hand.

The current setting and practice bring about a great deal of uncertainty and disputes regarding the project commencement, factual definition of project activities and the onset or clarification of research and technical uncertainty.

Inspiration for potential changes in the setup of R&D deduction may be found abroad. In many countries having the R&D deduction in place, R&D projects are only processed retrospectively, subsequent to the termination of the respective taxation period and the relevant development task. This change could resolve persistent disputes between businesses and the tax administration concerning the definition of the term "project solution commencement". Furthermore, it could enable tax payers to specify in greater detail how exactly project activities were realised in the respective period which could ultimately be beneficial for the tax administration in assessing eligible activities.

The latest information indicates that the financial administration is considering certain changes in the setup of R&D deductions. Let us hope that these changes will support research and development in the Czech Republic, contribute to the more-transparent assessment of R&D activities and direct attention to the actual substance of the issue rather than to the fact whether or not companies are really engaged in research and development. Greater transparency in R&D deduction is important for both companies operating in the Czech Republic and businesses considering the establishment of new or expanding existing R&D centres in the CE region and contemplating in which CE country the centre should be located. The transparency of individual support regimes in the relevant countries is one of the key factors in this decision-making process which is crucial for whether or not the Czech Republic will be selected.

In view of the Czech Republic's efforts to support primarily investments with high added value, it should be essential for all of us that the R&D deduction setup become more transparent for businesses.

We will keep you updated on further developments in future dReport issues.

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New treaty with Turkmenistan

Implementation of the new Double Taxation Treaty with Turkmenistan will start on 1 January 2019

On 27 March 2018, the Double Taxation Treaty between the Czech Republic and Turkmenistan came into force. The wording of the Treaty is expected to be published in the Collection of International Treaties shortly. The provisions of the Treaty should be applied as follows:

- In respect of income and property taxes, the Treaty will be applied to income paid or credited as of 1 January 2019 or later.

- In respect of withholding tax, the Treaty will be applied to income paid or credited as of 1 January 2019 or later.

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Courts Have Once Again Sided with Entrepreneurs in Respect of Payment Security Orders

The Supreme Administrative Court has again confirmed that it makes sense to defend yourself against the practices of the financial administration. In its latest ruling on the AB Chemitrans case, the court ruled that tax or related accrued interest and fees can only be recovered by distraint after the appellate proceedings have been concluded, which also applies to situations where the tax was subject to a payment security order. The ruling may significantly affect the existing practices relating to payment security orders and the performance of tax distraints.

In general, it applies that if the tax authority makes an additional tax assessment based on a tax audit, the additionally assessed tax is payable within 15 days of the delivery of the ruling on the appeal. Therefore, the tax authority is not allowed to collect the tax until after the appellate proceedings have ended when the payment assessment comes into force. However, if the tax is secured by a payment security order in advance, the tax authority has so far believed that the additional payment assessment may constitute grounds for a tax distraint as early as on the date it is delivered, ie regardless of the appeal filed. At that moment, the payment security order ceases to be effective, with the tax authority proceeding to perform the distraint and recovering the tax payable based on a payment assessment. However, in its latest ruling on the case of the Moravian company AB Chemitrans, the Supreme Administrative Court ruled that additionally assessment tax may only be recovered by distraint until after the appellate proceedings have ended with legal effect, which also applies to situations where a payment security order has been issued in the case in hand.

The legal opinion may have several practical implications. First, it may be inferred that payment security orders do not cease to be effective until after the appellate proceedings have ended with legal effect. Therefore, if, in the meantime, the appellate body or court revokes the payment security order for unlawfulness, the tax authority will be forced to refund the secured amount. The ruling may also affect the unlawfulness of the tax distraints already underway. In this regard, the issue of interest on unlawful acts, which the tax authority should pay to companies in situations like these, will also come into play.

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News in Immigration
Changes in the Ukraine Regime Project

The Ukraine regime was officially launched in August 2016. The Ukraine regime simplifies the hiring of employees from this country. It is intended for direct employers operating in the Czech Republic in the field of production, services or the public sector. Temporary help from Ukraine can help bridge the time when the Czech Republic's unemployment rate is critically low and companies currently lack 240,000 workers.

- Starting from 1 May 2018, the quotas will increase from 9,600 applications per year, i.e. 800 applications per month, to 19,600 applications per year, i.e. 1,600 applications per month (family members are not included in the quota).
- When filing a collective application for 50 or more people, it has been required since 1 February 2018 to demonstrate that the intention has been discussed with current employees and that approval of the mayor of the municipality where the foreigners will be accommodated after arriving in the Czech Republic has been obtained.
- As part of the increase in the number of accepted applications in the Ukraine regime, there is a concurrent increase in the capacities by the Ministry of Foreign Affairs at the Czech Consulate in Lviv.
- **Starting from 1 May 2018, applications for employee cards will be filed via the Lviv visa centre.** The visa centre will be created following the increase in the Ukraine regime quota. At present, a selection process for the external provider of the visa centre services is being conducted. Applications filed via the visa centre will entail a new fee for application processing. The fee is not expected to exceed EUR 20.

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The Mongolia Regime and the Philippines Regime

Other special programmes are intended to provide companies with temporary help to overcome the period of lack of employees. The Mongolia and Philippines regimes has been introduced with effect from 1 May 2018. They focus on countries whose labour force has continuously been a centre of interest of Czech employers.

The regime as such should serve for targeted and selective acceptance and processing of applications for employee cards by citizens of Mongolia and the Philippines who will perform work activities in the Czech Republic in the area of production, services or the public sector (on job positions CZ ISCO 4-8).

- The targeted and selective nature means that similarly to the Ukraine regime, the other states regime can include only a specific employer that meets the regime's criteria, together with a specific future employee or employees.
- Decisions on the applications for inclusion in the regime will be made by the Ministry of Industry and Trade (MIT) based on a recommendation from the Czech business representation or the CzechInvest Investment and Business Development Agency. The annual capacity for this project is 1,000 applications from each of the above countries (i.e. approximately 85 applicants per month per each country).
- Employee card applications will be accepted by embassies in Ulaanbaatar and Manila. After the monthly capacity of the respective embassies is filled, application acceptance will be suspended. Unlike the Ukraine regime, applications for the other country regime will not be put in an endless line. The applicants will be able to register several weeks in advance.
- The regime is intended only for direct employers that have been active in the Czech Republic for at least two years in the area of production, services and the public sector, that employ at least 10 people, have no payables to the state and have been persistently unable to fill an available job position from Czech labour market resources. The job position where the applicant included in the regime by the employer would be employed must correspond to the employer's business activity.

The regime also allows filing a "collective application" for 30 or more applicants, with the employer having to complement the application with a sworn statement that it will cooperate with the Centres for the Support of the Integration of Foreigners in the region, a sworn statement about having discussed the intention with employees in line with Section 280 (1) of Act No. 262/2006 Coll., Labour Code, and a statement of the mayor of the municipality where the foreigners will be accommodated after arriving in the Czech Republic.

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Changes of conditions for filing an employee card application in Lviv

More than three quarters of Ukrainian employee card applicants are accepted via the government project. The Ministry of Foreign Affairs of the Czech Republic decided to end the so-called live queue and to introduce instead electronic registration via a dedicated e-mail address. All citizens can make a request for assigning a date in this way on their own and free of charge. One of the main reasons for this new setup was to eliminate intermediaries who abused the existing system. The registration does not take place via the Consulate General but via the Ministry of Foreign Affairs headquarters, so that the Consulate General cannot be accused of changing the order.

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Transposition of the EU directive

The reports on the transposition of Directive 2004/114/EC and Directive 2005/71/EC showed a variety of flaws and the need to perform several changes. For the sake of clarity, the EU decided to rework both directives and replace them with a new one.

For this reason, the European Parliament and the Council approved on 11 May 2016 Directive 2016/801/EU on the conditions of entry and residence of third-country nationals for the purposes of research, studies, training, voluntary service, pupil exchange schemes or educational projects and au pairing (hereinafter "Directive 2016/801/EU"). EU member states have until 23 May 2018 to enforce legal and administrative regulations necessary to achieve compliance with this Directive. The primary changes will concern particularly the provisions on long-term residence permits for study purposes and the definition of the term "studies". The main changes are summarised below.

- Introduction of long-term residence for the purposes of job seeking or initiation of business activity. This residence purpose will be intended for university students after the end of their studies in the country and for research workers who have completed their research activities. In these cases they will be allowed to remain in the territory of the Czech Republic for up to 9 months in order to look for employment or initiate business activity. However, this permit will not automatically mean the granting of the right to access the job market or to initiate business activity.

- Obligation to attend adaptation and integration courses. The efforts for the integration of foreigners residing in the territory of the Czech Republic in the long-term will no longer be on a voluntary basis only – the element of limited and corresponding obligation will be introduced: the conditions for residence in the country will include (in certain cases) the obligation to attend an introductory adaptation and integration course for new arrivals within one year of receiving their Czech residence permit. The amendment introduces this obligation due to the identified necessity to inform foreigners especially about their rights and obligations as soon after their arrival in the Czech Republic as possible.

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Hungary

The Hungarian Tax and Customs Administration is now suable for minor irregularities

The category of reimbursement of damages in administrative powers is extended due to the change of approach caused by the new administrative procedure. On average, 20-30 lawsuits are filed against the Hungarian Tax and Customs Administration (NAV) for damages annually. However, this number could be higher, as there is a way for businesses to win cases against the NAV.

The actions of the NAV may even cause damage to companies. For example, the tax authority often freezes a company's bank accounts and inventories and blocks its operations as early as the beginning of the inspection as a precautionary measure. In such cases, enterprises tend to contend such cases; still, they usually do not even consider filing for damages against the NAV.

The tax authority may be successfully sued for damages if it is proved that the damage was caused due to exercise of executive power or lack thereof due to its own fault, and if the damage could not be counteracted by appeals or in an administrative lawsuit.

However, it is not enough to have a court decision which overturns the case or calls for a new procedure; it also has to be proved that the damage was caused by the NAV's grossly erroneous legal interpretation, or the administrator's breach in bad faith or with gross negligence, or extremely irrational evaluation or ignorance of evidence.

Before the new code of administrative procedures entered into force, the standpoint on cases where the NAV caused the damages by a minor infringement only was uncertain. The reason for this is that in such cases, infringement was not established by the administrative courts in lawsuits against the NAV's decision, as the meaningful ruling of the case is not affected by minor irregularities.

However, the new code of administrative procedures settles this issue. In tax litigation cases, not only claims approved by the administrative courts can serve as a basis for claiming for damages against NAV, but also rejected claims, if a procedural infringement was ruled by the court as not affecting the case, i.e. minor.

The risk of a potential damage caused by the NAV is highest in the case of precautionary measures; freezes of bank accounts and inventories of companies; blocking of cargo and vehicles during EKAER inspections; prolonged disbursement of reclaimed VAT; and false information. If a company considers the NAV to have caused damages by its actions, the current legal environment provides for more opportunity for indemnification. The indemnification of damages attributed to NAV might lead the tax authority to act in a way that its actions do not cause unnecessary damages to enterprises.

Unexpected option of legal remedy in adjudicated tax litigation cases

In an increasing number of cases involving the tax authorities, it is found that the resolutions issued by the tax authority against companies contained formal errors.

The Curia of Hungary has recently ruled such resolutions void. It is uncertain how many cases might be affected by the Curia's decision, but its interpretation is likely to question the legality of numerous non-appealable resolutions, which might result in great tax savings for businesses. In this special edition of our newsletter, we would like to draw your attention to options of legal remedy resulting from the Curia's decision.

According to the Curia's decision, the tax authority's resolution becomes void if it was not issued in accordance with the legal regulations concerning form and competence. In the Curia's opinion, the decision-making process should be repeated in these cases. The decision is likely to affect numerous resolutions, resulting in great amounts of tax savings for businesses in cases of non-appealable adjudicated tax litigations. Savings result from the fact that the tax authority must consider the five-year limitation time of the tax assessment right during the new decision-making process. This often causes a situation where the tax authority cannot or can only partly assess tax liability of companies.

Even though the tax authority does not have an official opinion about how this time limit is enforced in the case of decisions repeated due to nullity, tax administration rules suggest the aforementioned interpretation.

The way in which non-appealable adjudicated cases can be disputed again can only be decided in light of the specific cases.

As the options of legal remedy resulting from the Curia's decision are only available for a fixed period, we recommend that those clients against whom the tax authority has recently assessed tax liability of a major sum should arrange discussions with our experts in order to make the most of the available options of legal remedy.

Making money from Bitcoin? It's time to think about taxes!

Investment options based on blockchain technology have become increasingly well-known in Hungary in the past few years. Approximately tens of thousands of early investors, day traders and miners in Hungary are informed about the latest developments, promising projects and "pump trends" on a minute-by-minute basis through lots of terabytes of information on Twitter, Facebook, or Telegram. Deloitte Private focuses on taxation issues concerning cryptocurrencies. The company's director dr. Gábor Baranyi has summarised the main risk factors.

In the almost unfilterable information noise, the average Hungarian crypto-investor has only recently begun to actively deal with the taxation on their investments. The question is not simple, as in the case of cryptocurrencies, it is not even clear what the expression means when translated into the language of law.

Fortunately, numerous international examples are available, many of them exceptionally progressive. Cryptocurrency is considered as a simple commodity by the Canadian legal system, while it is seen as a foreign currency in Switzerland. German law puts it in the category of "private money". The Court of Justice of the European Union regarded crypto-money as some kind of foreign currency in a ruling on the VAT treatment of the trade of cryptocurrencies.

In the Hungarian law, however, there is not yet any specific regulation on the legal standpoint on cryptocurrencies.

As with many other areas of technology, it is typical in the case of cryptocurrencies that it is especially hard for legislators to keep up with the speed of development. However, this lack of regulation indirectly poses great risks relating to the tax treatment of the generated profit for judicial bodies and the investors involved.

The tax authority's positions which were issued in 2015 based on individual enquiries have already been published and evaluated on several platforms. The position of the authority is briefly that the profit generated from investment activities as a private individual is considered so-called "other income" due to the lack of specific regulations, and as such, it requires the payment of almost 30% tax. In the case of wealth earned from "coins" that are "mined", a similar tax ratio is expected. For comparison: in the case of an exchange rate gain from shares, besides the 15% PIT, only a limited rate of health tax might arise. When considering the detailed rules regarding the settlement of expenses, it becomes clear that the tax treatment of cryptocurrency investments is especially unfavourable for private individuals.

If the activity is carried out by a business instead of a private individual, the tax burden is smaller (9% corporate income tax and potentially 2% local business tax). Most investors, however, do not keep their crypto-savings in businesses, and passing on existing crypto-investments to a company poses serious taxation problems.

In countries where the legal treatment of cryptocurrencies is in a more evolved state, this is often coupled with favourable tax treatment. Estonia, for instance, indicated its intention at the end of 2017 to feature among the global leaders in blockchain-based initiatives through its supportive legal, tax and service environment. Favourable regulations exist in many other countries, such as Germany, Denmark, or Slovenia.

Many people try to escape the infamous Hungarian taxes and additional administrative obligations (i.e. tax advance assessment, or preparation of tax returns and continuous keeping of tax records) through the increasing number of investment schemes. However, the level of reliability and sophistication of these is quite low in most cases, which often entails further taxation and legal risks.

In relation to the tax treatment of crypto-exchange trade, one often comes across solutions trying to "optimise" Hungarian tax liabilities through complicated schemes involving foreign elements. However, we advise against such dubious and unreliable schemes, as they often lead to fake solutions only. Moreover, nowadays the tax authority sees through these techniques thanks to the information exchange systems operating between the tax authorities of different countries.

What is more, international "wangles" typically create further, often foreign tax liability and extra expenses for the investor. However, with conscious planning, taxation risks can be minimised in a legal way, without any kind of "fishy business" abroad.

In conclusion, the more complicated system is created for our crypto-investments, the greater the chance of a flaw in the planning, and then the investor's situation becomes even worse than before. Therefore, it is worth connecting the leveraging of the opportunities technology has to offer with planning that minimises risks.

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Latvia

The Constitutional Court has declared the Article 12.3 and the Article 12.5 of the Law On Value Added Tax insofar as they do not ensure the return of VAT overpayment to the taxpayer within a reasonable time, as not complying with the Article 105 of the Constitution of the Republic of Latvia.

According to the contested norms, the period during which VAT overpayments are returned to the taxpayer may range from approximately one month to one year and even longer.

This means that, according to the contested norms, VAT overpayment may also be returned to the taxpayer after a deadline that cannot be considered as reasonable. Such a transfer of VAT overpayment return period could be considered as complying with the principle of the neutrality of VAT, if the law would provide for the taxpayer compensation of the taxpayer's financial loss, resulting from such delay, with late payment interest.

However, compensation for the financial burden resulting from the transfer of VAT overpayment return period late payment interest is not provided in the contested norms of the Law On Value Added Tax. Consequently, the contested norms creates for the taxpayer a financial burden, which is not compensated. This means that the impugned norms do not comply with the principle of VAT neutrality.

Consequently, the restriction of fundamental rights established in the contested norms is not proportionate and the contested norms are to be declared as not complying with the Article 105 of the Constitution of the Republic of Latvia.

The Applicant asked for the contested norms to be recognized, insofar as they limit the right to return VAT overpayment within a reasonable time, as not complying with the first, second and third sentences of the Article 105 of the Constitution of the Republic of Latvia.

According to the Applicant's opinion, the damage, which takes the form of a financial burden and which arises from the transfer of the term of the return of the overpaid tax defined in the contested norms, is higher than the benefits that the society derives from the country resource savings resulting from this transfer. Consequently, the restriction of the taxpayer's fundamental rights, established in the contested norms, is not proportionate.

The Constitutional Court came to conclusion that the contested norms create the restriction of the taxpayer fundamental rights set forth in the first three sentences of the Article 105 of the Constitution of the Republic of Latvia.

The Constitutional Court also establishes that the restriction of fundamental rights established in the contested norms has a legitimate aim - the protection of the welfare of society and that the means chosen by the legislator are suitable for achieving the legitimate aim.

The Constitutional Court acknowledges that there are no more lenient means that would ensure the same amount of state resources savings as it is provided, if the state does not need to make a significant part of administrative activity at all.

According to the contested norms, the period during which VAT overpayments are returned to the taxpayer may range from approximately one month to one year and even longer. This means that, according to the contested norms, VAT overpayment may also be returned to the taxpayer after a deadline that cannot be considered as reasonable. Such transfer of VAT overpayment return period could be considered as complying with the principle of the neutrality of VAT, if the law would provide for the taxpayer compensation of the taxpayer's financial loss, resulting from such delay, with late payment interest. However, compensation for the financial burden resulting from the transfer of overpayment return period late payment interest is not provided in the contested norms of Law On Value Added Tax. Consequently, the contested norms create for the taxpayer a financial burden, which is not compensated. This means that the contested norms do not comply with the principle of VAT neutrality.

Consequently, the restriction of fundamental rights established in the contested norms is not proportionate and the contested norms are to be declared as not complying with the Article 105 of the Constitution of the Republic of Latvia.

The contested norms have already expired since January 1, 2013, when the Value Added Tax Law entered into force. However, contested norms can still be applied to the already initiated, but not closed administrative proceedings, based on the legitimacy of the State Revenue Service decisions adopted on the basis thereof.

The Cabinet of Ministers approved amendments to the Law on Taxes and Duties with a view to improving the legal framework for transfer pricing documentation

The transfer pricing documentation requirements contained in the draft law will be more specific compared to the current general requirements. As a result, taxpayers will have a clearer regulatory framework and, when preparing transfer-pricing documentation, the taxpayer will be able to rely on law regulation more than on OECD transfer pricing guidelines, as it mostly takes place at the moment.

The transfer pricing documentation is a set of documents prepared by the taxpayer to substantiate that the transaction price (value) of an associated foreign entity corresponds to the market price. The statutory provision will decrease the possibility of shifting corporate profits to a country with more favourable tax treatment by manipulating the value of transactions.

The requirements of the transfer pricing documentation revised by the amendments to the law are suited to the current situation in which more and more companies in the same group of companies, each of them residing in a different country, are involved in the provision of the same service or supply of the same goods. In such cases, transfer pricing documentation needs to provide information on the entire business group's overall economic activity. Transfer pricing documentation will consist of two parts: global documentation (information for the entire group as a whole) and local documentation (information about a particular transaction, including price calculation).

At the same time, the thresholds at which taxpayers are required to make transfer-pricing documentation are increased. This will reduce the administrative burden for smaller transactions. In turn, transfer pricing documentation for transactions between Latvian associated companies will have to be prepared only when requested by the State Revenue Service. Therefore, transfer-pricing requirements will apply to a smaller range of taxpayers.

The amendments to the law also includes other changes, including that the competent authority of the mutual reconciliation procedure is the State Revenue Service and amendments also intends to improve the separate components of the tax audit legal framework.

The Committee of the Cabinet of Ministers has conceptually supported the draft of the Residential Tenancy law

The Committee of the Cabinet of Ministers on April 23, 2018 conceptually has approved the draft of the Residential Tenancy Law, which will be a new regulation in the residential real estate market and will promote the creation of qualitative and affordable rental apartments, will offer a new solution to the ongoing long litigation processes, as well as promote investments in the rental real estate sector.

In order to reduce the shadow economy, the new draft law prescribes registration of all rent agreements in the Land Register, thus providing publicly available and reliable information on concluded rent agreements that will protect both tenants and new real estate owners. It is important to emphasize that registration of a rent agreement in the Land Register will be free of charge, thus not creating additional costs for the lessor and the tenant. Simultaneously, registration of a tenancy agreement in the Land Register will allow the elimination of fictitious rental agreements as well as protecting honest tenants in the event of a change of lessor.

The new draft law will also significantly accelerate the settlement of disputes between the lessor and the tenant and will reduce the associated costs. The current law provides the settlement of all disputes in court. With the new law, by making appropriate amendments to the Civil Procedure Law, there is offered an uncontested execution of obligations in certain cases (in cases where there is no dispute) - the tenant will be obliged to leave the rented residential space if the term of the lease has expired and new agreement will not be reached, if there is a rental payment debt, as well as in the event of the sale of real estate, if the rental agreement is not registered in the Land Register. At the same time, such a solution will significantly reduce the risks for potential investors to invest in the building of new rental real estate.

Significant changes are prescribed in terms of the term of the lease agreement - the lease agreement can no longer be concluded for an indefinite period. The rent agreement will only be concluded for a certain period of time, and upon expiry of the term, the tenant will be obliged to leave the living space, unless a new rental agreement is concluded with the lessor. Same as before, a tenant will be able to cancel the contract without any special reason by notifying the lessor in advance; while the lessor will still be able to withdraw the contract only in cases and within the time limits specified by the law.

The rights of the tenants' family members will also be affected - members of the family will no longer enjoy an independent right to use the living space, thus the members of the family will no longer be jointly and severally liable for the obligations arising from the rent agreement. Only in the event of the death of the tenant, family members are entitled to request a new rent agreement without changing the terms of the previous rent agreement.

With a view to protecting the tenants' interests more effectively, the draft law stipulates that the lessor will be able to increase the rent payment only if the rent agreement will specify the principles and procedures for raising a rent payment.

In accordance with the transitional provisions rental agreements that were concluded prior to the entry into force of the new law shall be registered in the Land Register within 5 years from the entry into force of the law.

Within two years from the entry into force of the law, the lessor and tenant who currently uses the living space on the basis of the lease agreement concluded with the previous lessor, must conclude a new rental agreement

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Lithuania

The court clarified the relation between personal data and the company's interest

The Supreme Administrative Court of Lithuania stated that the formal notice of professional e-mail's monitoring at work is not necessary if the employee must understand it taking into account the nature of his/her position.

This case is relevant to the General Data Protection Regulation, which comes into force on 25th May, by which it is mandatory for employees to be informed about the monitoring of professional e-mail in written form.

The Centre of Registers initiates the development of a virtual company's prototype

The Centre of Registers announces that the necessary legal changes will be clarified and the virtual company's concept will be constructed.

Virtual companies would be subjects of Lithuanian jurisdiction and would have to pay taxes in Lithuania without the obligation to submit financial statements. The aim is to create a legal form that allows to fully develop the blockchain and DLT (Distributed Ledger Technology) businesses in Lithuania. The main innovation would be the transition to a legal entity's (virtual company's) stock market based only on blockchain technology.

The court ruled that employee must compensate for disclosure of commercial secrets

The Supreme Court of Lithuania ruled that the employee is liable for disclosure of commercial secrets and has an obligation to compensate damages.

The court clarified that the employee's obligation to protect confidential business secrets originated from the contract of confidential information concluded with the company. The fact that the information provided to third parties was publicly available does not invalidate the information's commercial value for the company's business.

New rule regarding conflict of interests applicable to the head of the company

The Supreme Court of Lithuania examined the situation in which the CEO having its professional duties was also engaged in individual activities and provided the same services as the company.

The court stated that the CEO should give priority to the interests of the company and avoid a situation when personal interests are in conflict with the interests of the company. If it is needed for a CEO to carry out the same activities as the company carries, the CEO must obtain a consent of the shareholders.

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Poland

No Revolution in the Labour Law. PiS not to support the bills proposed by the Codification Committee

The spokesperson of the Law and Justice (PiS), Beata Mazurek, said today that PiS will not support the new labour law bills proposed by the Codification Committee. This basically means that there will be no revolution in the labour law.

However, it still remains to be seen whether some of the proposed solutions will be gradually introduced to the current regulations, which — doubtlessly — despite numerous amendments are obsolete in the light of the new economic reality and require further changes.

It should be recalled that in mid March, after 18 months, the Labour Law Codification Committee finished work on new individual and collective labour law bills. Among the proposed solutions were:

1. deemed employment status in relationships with natural persons, restrictions on civil-law contracts concluded by business entities, self-employment limitations;
2. limitations regarding fixed-term employment contracts and introduction of new types of contracts such as casual or seasonal employment contracts;
3. introduction of the obligation to give reasons for the termination of every type of employment contract, with the possibility of exemption for small businesses provided that they offer additional monetary benefit;
4. changed notice periods;
5. possibility of a partial waiver of salary by an employee;
6. introduction of salary accounts, possibility of adapting the working hours of the company in the collective labour agreement, high adoption of the opt-out clauses with regard to overtime; and
7. exclusion of employers hiring up to 20 employees from the provisions concerning protection against dismissal set out in the group dismissal act.

As far as the existing legislation and the rulings of the Supreme Court are concerned, the proposed solutions were often revolutionary. It is also a well-known fact they were not satisfactory to the trade unions and employers' organisations, despite the fact that their representatives participated in the works of the Codification Committee. Even certain members of the Committee voted against the bills, which also received unfavourable public perception.

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Solutions and Systems to Monitor Abusive Practices. How can the entities operating in the financial market avoid heavy fines?

Financial market participants are obliged to comply with the Regulation (EU) No. 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse ("MAR"). The objective of the regulation is to prevent market abuse in the form of market manipulation and determine measures to prevent manipulative strategies. MAR is followed up by Directive 2014/57/EU of the European Parliament and of the Council of 16 April 2014 on criminal sanctions for market abuse ("MAD").

Both legal acts provide for heavy fines for entities which fail to comply with the regulations. The fines, however, may be avoided, if certain regularities within an entity have been successfully detected.

The goal of MAR is to guarantee market transparency, protection of the financial market integrity and building of trust in the market. Article 2 of MAR describes the general scope of the Regulation identifying financial instruments admitted to trading on a regulated market, MTF, OFT etc. The provisions dealing with market manipulation (Articles 12 and 15 of MAR) apply also to benchmarks and may be used with reference to interbank transactions.

MAR and MAD, and as a result the Act on trading in financial instruments, which has been amended as appropriate, provide for heavy sanctions for failure to comply with MAR regulations and requirements by entities operating in the financial market. Article 183 of the Act states that the person engaging in financial market manipulation faces a fine of up to PLN 5 000 000 or imprisonment from 3 months to 5 years or both these sanctions. The persons liaising with them face a fine of PLN 2 000 000.

Under Article 173.4 of the Act, the Polish Financial Supervision Authority may impose an additional fine of up PLN 10 364 000 or to an equivalent of 2% of the total annual income disclosed in the last audited financial statements for a financial year, if it is more than PLN 10 364 000, on a legal person which fails to comply with the obligation to maintain systems and procedures in order to prevent and detect insider trading and market manipulation practices and attempted insider trading and market manipulation practices. As shown above the fines are substantial. It is the obligation of every entity subject to MAR to take all possible measures to mitigate the risk of such fines.

It should be emphasised that MAR defines "market manipulation" very broadly. Under MAR, manipulation in a financial market is every unlawful act carried out both by an entity operating in the market dedicated to the trading in financial instruments and by its employees or managers, provided that it has been determined that the goal of such acts was to impact the instruments themselves or the ratios underlying the pricing of the instruments (e.g. benchmarks).

Article 15 of MAR directly prohibits engagement in or attempted engagement in market manipulation by any person. This is an unconditional prohibition applicable to all market participants trading in financial instruments.

No entity may ever be certain that one or more of persons within their employment does not commit some form of abuse. If such event takes place, the persons will be punished, however, a question arises whether the system used to the monitoring of such behaviour in a given institution does not have gaps that make the abuse possible.

Pursuant to Article 16 of MAR market operators, investment companies operating a trading venue and anyone professionally arranging transactions are obliged to put in place and maintain effective solutions, systems and procedures to prevent and detect insider trading, market manipulation and attempted insider trading and market manipulation. Failure to put in place solutions and systems to prevent such abusive practices results in heavy fines imposed on a market participant trading in financial instruments.

The fines may be prevented by ensuring high quality of the systems used to monitor transactions and behaviour related to and affecting the traded instruments. Under recital 30 of MAR "Where legal persons have taken all reasonable measures to prevent market abuse from occurring but nevertheless natural persons within their employment commit market abuse on behalf of the legal person, this should not be deemed to constitute market abuse by the legal person".

In examining whether measures are "reasonable" one should in the first place consider the status and size of the market participant as in practice the requirements imposed on banks, which are institutions of public trust, are higher than those imposed on investment companies. This does not mean that the latter may attach less weight to preventing abusive practices.

Every market participant trading in financial instruments is obliged to ensure effective detection of abusive practices. To achieve that appropriate systems of monitoring orders and transactions must be put in place. Not only must such systems be established inside an entity, but they also must be regularly reviewed by external advisors, who — provided they specialise in forensic auditing and use appropriate technological solutions — can detect any gaps in the system which may have left serious abuse undetected. Verification may take the form of an analysis of sample documentation or internal communication of a given entity.

Article 176f of the Act states that while imposing a fine the Polish Financial Supervision Authority takes into account the circumstances referred to in Article 31.1 of MAR. These are: (i) the gravity and duration of the infringement; (ii) the level of cooperation of the person responsible for the infringement with the competent authority, without prejudice to the need to ensure disgorgement of profits gained or losses avoided by that person, (iii)previous infringements by the person responsible for the infringement; or even (iv) measures taken by the person responsible for the infringement to prevent its repetition. Therefore all preventive measures taken by a given entity, which show that the highest professional standards are maintained, are taken into account.

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How to get ready for FATCA and CRS reporting for 2017

No later than on 2 July 2018 reporting financial institutions should send to the Head of the National Revenue Administration information about reportable accounts for 2017.

The information should be submitted in line with clearly defined procedures — XML Schema (i.e. files with rules how the submitted data should be structured).

To report data for 2017 Polish financial institutions should use the CRS-1(1) form for CRS reporting and FAT-1(3) for FATCA reporting. Valid XML formats are published on the web page of the Central Repository of Electronic Document Models on the ePUAP platform.

The CRS-1(1) has not changed since last year, but a new FAT-1 format has been published by the Ministry of Finance for 2017. For example, compared to FATCA reporting for 2016, this year FAT-1(3) requires that the type of the Polish financial institution be given ("FileCategory"). On the other hand, "Report for Non-Participating Institutions" has been removed.

As far as the second change is concerned, there were doubts over the method of completing FAT-1(3). Despite the fact that the part devoted to reporting payments to non-participating institutions has been removed (the requirement to report such payments was in force only with respect to 2015 and 2016), the XSD/XML formats still include the "*FATCA103 Non-Participating FFI*" category for the holder. Therefore it may be uncertain whether "*FATCA103 Non-Participating FFI*" should be abandoned altogether for the account holder type or whether financial institutions must keep reporting payments to non-participating FFI. In order to help Polish entities comply with FATCA and CRS requirements, the Ministry has published additional explanations how to complete the elements of XML schema (for FAT-1(3) and for CRS-1).

For CRS reporting it should be checked which non-EU states have joined the automatic exchange of information (i.e. they have become the participating countries) and therefore their tax residents should be included in the reporting for 2017. The list of participating countries, also for the year 2017, has been published by the Minister of Development and Finance in Monitor Polski.

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Romania

Major changes to the Tax Code

Law no. 72/2018, Government Emergency Ordinance no. 18/2018, Government Emergency Ordinance no. 25/2018 amended recently the Tax Code on profit tax, income tax, withholding tax ("WHT"), microenterprises regime and Value Added Tax (VAT).

The Tax Code's major changes introduced by the Law 72/2018 for approval of the Emergency Ordinance no. 25/2017 refer to:

Corporate income tax

A 30% deductibility threshold applied to the net loss of alienated receivables from a CIT perspective. Thus, the 30% limit shall apply to the value of the sale price less the value of the alienated receivable.

The net loss for the assignee who now transfers a receivable is the difference between the sale price and the acquisition cost of the receivable.

- In addition, the changes address the situation of credit institutions, assigning (partially) provisioned or off-balance sheet receivables. More specifically, the amendments state that 70% of the difference between the value of the alienated receivable and the sale price should be treated as items similar to income.

Income tax

The exemption of the income tax and social security contributions for medical services provided under a subscription, borne by the employer, is no longer applicable only to those defined as per Law 95/2006 on healthcare reform. Therefore, the costs with the voluntary health insurances and medical services provided under a subscription, borne by the employer in the limit of EUR 400/ year/ employee are not taxable from an income tax and social security perspective.

Similarly, medical services provided under subscriptions, borne by the employee are deductible when calculating the income tax base in the limit of EUR 400/ year/ employee, regardless if they are defined or not as per Law 95/2006 on healthcare reform.

The wording regarding medical subscriptions was amended also for the provisions of income from independent activities.

VAT exemption threshold increases

As of 1 April 2018, the VAT exemption threshold for small enterprises will increase from RON 220,000 (EUR 65,000) to RON 300,000 (EUR 88,500).

The following transitional measures are applicable until 31 December 2018:

Set up date of the company	Threshold to be considered
By the end of 2017	RON 220,000 – if exceeded between 1 January – 1 May 2018 RON 300,000 – if exceeded after 1 May 2018
1 January – 1 May 2018	RON 220,000 – if exceeded until 1 May 2018 RON 300,000 – if exceeded after 1 May 2018
After 1 May 2018	RON 300,000

Taxable persons registered for VAT purposes considering the RON 220,000 threshold until 1 May 2018 can ask for deregistration, provided that, at the time of request, the new exemption threshold of RON 300,000 has not been exceeded.

Withholding tax

The deadline for submitting the annual informative return regarding the income obtained by non-residents (D207) is until 31 January (including) of the current year for the expired year, according to Emergency Ordinance no 18/2018.

Micro-enterprise tax

Certain amendments have been brought to the micro-enterprise tax through Emergency Ordinance no. 25/2018. Thus, such entities may opt to apply the corporate income tax regime if they meet certain conditions.

Common set of rules for calculating taxable profits (CCCTB), voted by the European Parliament

On 15 March, the European Parliament voted in favor of plans establishing a common consolidated corporate tax base (CCCTB), namely a common set of rules that companies operating in the EU can use to calculate taxable profits.

European Parliament legislative resolution of 15 March 2018 on the proposal for a Council directive on a Common Consolidated Corporate Tax Base (CCCTB) and on the proposal for a Council directive on a Common Corporate Tax Base (CCTB) refer to:

Introduction of a common corporate tax base (i.e. CCTB), which is one set of rules to calculate companies' taxable profits in all EU countries. Initially, the rules would be mandatory for groups of companies with a consolidated turnover exceeding EUR 750 million. The threshold of mandatory application of the directive will be reduced subsequently from EUR 750 million to zero, over a maximum period of seven years.

Introduction of a common consolidated corporate tax base (i.e. CCCTB), which would introduce rules for consolidation, formulary apportionment and a "one-stop shop" for tax administration.

Under the new regime, companies would calculate their tax bills by adding up the profits and losses of their constituent companies in all EU member states. The resulting tax would then be shared between member states, depending on where the profits were generated.

Some of the most important amendments brought have been highlighted below:

Important amendments to CCTB

Introduction of the digital permanent establishment definition and several provisions to the permanent establishment specifically for digital economy;

Exceeding borrowing costs should be deductible for a maximum of **10%** of EBITDA or for a maximum amount of **EUR 1,000,000;**

Limitation of the carry-forward period of the exceeding borrowing costs and tax losses to five years;

Introduction of new R&D provisions by replacing the super-deductions with a tax credit for expenses in respect to staff, subcontractors, agency workers and freelancers;

Removal of the provisions for cross-border compensation of tax losses between subsidiaries;

Changes to the controlled foreign companies' provisions;

Definition of new terms such as: "economic substance", "letterbox company", "royalty costs", "transfer prices", etc.

Important amendments to CCCTB

CCCTB's provisions shall be applied simultaneously with those of CCTB's and not in a subsequent phase, as it has been initially proposed;

Ensuring a level playing field in the EU and mitigating the administrative burden and costs for SMEs;

Monitoring and publication of the effective tax contribution of SMEs and multinationals;

Modifying the apportionment formula by adding a fourth factor, 'data' factor;

Ensuring a smooth transition to CCCTB for Member States; tasking the Commission to propose to allocate a part of CCCTB revenue to the EU budget and proportionally reduce their contributions.

Other aspects

The deadlines for the adoption and publication of the provisions of the Directive for the Member States shall be 31 December 2019 and their application from 1 January 2020.

European Commission directives proposed on taxation of companies in the digital economy

The European Commission proposes two solutions on a long-term and on a short-term for taxation of companies with significant digital presence.

The European Commission intends to structurally change the concept of a permanent establishment (PE), in order to prevent companies operating within the EU digital services industry, from not paying or paying a tax too low on the profits earned within the country where the value of services is created, as a result of the lack of physical presence in the country where the services are performed.

Since structural changes are needed on the long-term and the implementation process is lengthy, the Commission has proposed as an intermediate solution the taxation of the gross revenues derived from digital services.

Interim tax on digital services

The European Commission is proposing a 3% digital services tax on the gross revenue resulting from the supply of certain digital services characterized by user value creation:

Online placement of advertising;

Sale of collected user data; and

Digital platforms that facilitate interaction between users that then can exchange goods and services directly via the platform.

Given the specific information EU member states would need in order to levy the digital services tax, additional reporting requirements would need to be imposed. In this respect, a single EU-wide payment and reporting portal would be established, based on the one-stop-shop model currently used for VAT purposes.

Thus, businesses would be required to self-assess the tax liability and pay it on an annual basis.

Longer-term structural changes to taxation of digital services

The proposal would extend the current PE rules for digital businesses operating across borders where at least one of the following conditions is fulfilled during a tax year:

Revenues from digital services provided to users located in a member state exceed EUR 7 million;

Number of active users of digital services located in a member state exceeds 100,000; or

Number of business contracts for digital services concluded by users located in a member state exceeds 3,000.

The definition of digital services would follow that used for VAT purposes under the EU VAT directive.

According to the European Commission, the structural tax changes to the PE concept should eventually be included in the proposal for a common consolidated corporate tax base (CCCTN) in order for such taxable profits to be allocated in proportion of the share of activity of an EU member state. Moreover, EU member states would also have to implement the rules on digital PEs and profit allocation for corporate income tax purposes.

In order to prevent tax avoidance, certain “Anti fragmentation” rules would be introduced.

Profit allocation

The profit allocation rules relating to digital services would be aligned with the OECD transfer pricing guidelines. The basic assumption would be that profits should be taxed where value is created. In terms of digital services, the commission intends to relate value creation to the location where the buyers of the digital services are established and data is collected and processed. Consequently, additional criteria for profit allocation would be developed, focusing specifically on digital services.

In order to apply the proposed directives, all member states should unanimously approve them. It is rather unclear when the measures would effectively be introduced, but as noted above, the Commission aims for an effective date of the interim measures starting with 1 January 2020.

ECOFIN Agreement for the tax intermediaries' directive and for revising the list of non-cooperative jurisdictions

According to the agreement, tax intermediaries are obliged to report structures including cross-border transactions.

The new directive will provide EU tax authorities with information about cross-border arrangements in relation to individuals, companies and other entities by requiring intermediaries, such as tax advisors, accountants, banks and lawyers, who design and promote tax planning schemes for their clients, to report to the tax authorities in the country in which they are resident any cross-border tax planning arrangement they design or promote that contains specific broadly defined criteria ("hallmarks").

That EU member state will then share the information with all other member states on a quarterly basis. Intermediaries that do not comply with the transparency measures will be penalized.

The directive will be formally adopted during the next EU council meeting on 25 May 2018, and, once adopted, it will generally apply as from 1 July 2020, with limited retroactive effect.

Decision of the Court of Justice of the European Union (CJUE) on time limits for claiming VAT refunds

VAT can be reclaimed after the statute of limitation period has expired.

On 21 March 2018, the Court of Justice of the European Union (CJEU) gave its decision in case C-533/16 Volkswagen AG concerning the rejection to refund VAT due to the expiry of the statute of limitation period.

Background

Between 2004 and 2010, the Hella Companies established in Slovakia supplied Volkswagen AG (VW), a company established in Germany, with moulds for the manufacture of lights for motor vehicles. They did not include VAT on the invoices as they considered them VAT exempt.

In 2010, the Hella Companies realized that the transactions were not being carried in accordance with the Slovak law and issued new invoices to Volkswagen AG, charging the VAT due for the entire period.

For the VAT paid, VW submitted a refund claim to the Slovak tax authority. The tax office partially upheld that application and ordered a refund of VAT for the acquisition of goods carried out from 2007 to 2010. However, it dismissed the application insofar as it related to the period from 2004 to 2006, due to the expiry of the limitation period of five years provided for by Slovak law.

The CJEU was requested to rule whether VW has the right to deduct VAT charged several years after delivery of the goods, when the limitation period provided for the exercise of that right has expired before the application for a refund was submitted.

Arguments of the CJEU

As per the CJEU, the right to deduct VAT has to be exercised during the period when it occurred, namely once the VAT becomes due. At the same time, a taxable person can deduct VAT even if it did not exercise the right during the period in which the right arose.

However, the possibility of exercising the VAT refund right without any temporal limit would be contrary to the principle of legal certainty.

Even though the supply of goods at issue was carried out during 2004 to 2010, the Hella Companies did not make an adjustment of the VAT until 2010 when they drew up invoices including the VAT and paid the VAT to the state.

In these circumstances, it was objectively impossible for VW to claim VAT refund as it had neither been in possession of the invoices nor aware that the VAT was due.

Moreover, Volkswagen did not show a lack of diligence and there was no abuse or fraudulent collusion (with the Hellas companies).

Therefore, a limitation period that began from the date of supply of the goods and expired before the correction of the VAT position cannot cancel VW's right to recover the VAT.

Our views

This decision may change the existing laws from Romania.

Currently, a taxable person can deduct VAT after the right arose, but not exceeding the 5 years statute of limitation period. The only exception is the VAT assessed during tax audits. The suppliers are entitled to issue correction invoices after the tax audit and the beneficiary is entitled to deduct the corresponding VAT, even if the limitation period has expired but within 1 year from the date when the corrected invoice is received.

Based on this decision, it can be argued that the VAT recovery right can be exercised after expiration of the statute of limitation period (even for VAT not resulted from corrections after a tax audit). The circumstances of each case will be decisive; they will have to be in line with the points raised by the CJEU: late charging of the VAT by the supplier/objective impossibility of the customer to recover the VAT, diligence of the customer, non-existence of an abuse/fraud.

It would be interesting to see the time limits for exercising such VAT recovery. If the Romanian law changes, it may that the existing 1-year rule is extended.

In this context, we expect the decision of the CJEU in case C-8/17 Biosafe. The AG stated in her opinion to that case that the right to deduct the VAT arises when the invoice showing the correct VAT amount is issued and therefore, the statute of limitation should consider that date. If the CJEU follows this opinion, it would result that the 5-year statute of limitation period would need to take into account the date when the correct invoice is issued.

Opinion of the Advocate General of CJUE on the VAT exemption for transactions concerning payments

VAT exemption denied for instructions to transfer money.

On 21 March 2018, Advocate General (AG) of the CJEU gave his opinion in the case C-5/17 DPAS Limited.

In brief, the AG considers that the VAT exemption for payments does not apply to instruction to pay (direct debit of a bank account for a patient that is paying his/her dentist). The fact that the instruction is essential to make the transfer of money is not sufficient to achieve that VAT exemption.

Background

DPAS provides dental plans to dentists and supplies dental plan administration services to patients (including insurance and payment management).

The operational model was as follows:

Pursuant to a direct debit mandate, DPAS instructed the bank to transfer the agreed amount from the patient's account to DPAS account.

DPAS then requested the bank to on-transfer the money to the dentist's bank account but withhold its service fee.

Starting with 2012, DPAS changed the structure of its services with the aim of preventing its services becoming subject to VAT based on CJEU's decision in case C-175/09 AXA.

In that case, the CJEU ruled that the services offered to dentists by AXA Denplan qualify as 'debt collection' and are therefore subject to VAT.

The change of the structure of the services consisted of the following:

DPAS concluded contracts not only with the dentists (creditors) but also with the patients (debtors).

The activities performed by DPAS remained unchanged though and DPAS clearly communicated that nothing will effectively change.

It seems that DPAS aimed to argue that its services cannot be debt collection as they are not provided to the creditor (owner of the debt) but to the debtor.

The UK court judging the case asked the CJEU if:

The transfers instructed by DPAS to the banks on behalf of the patient are covered by the VAT exemption for payments.

Such services can be excluded from the scope of taxed debt collection (and hence, be exempt) because they are performed for the debtor rather than the creditor.

Arguments of the CJEU

The AG looked at the traditional CJEU on the VAT exemption for payments: the decisive criterion for applying the VAT exemption is the changes of the legal and financial situation of the parties involved.

By contrast, the supply of a mere physical, technical or administrative service which does not result in the legal and financial changes characteristic to the transfer of money is not exempt from VAT.

DPAS is asking/instructing a payment to a bank and not actually executing the payment, i.e. debiting/crediting the bank accounts.

As such, DPAS's involvement is prior to the transfer of the money from one bank account to the other.

Therefore, such services cannot be VAT exempt even if DPAS's *involvement is essential to* performing the payment.

Moreover, in DPAS case, there are no difficulties to determine the taxable amount (this is the difference between the amounts collected from patients and the amounts transferred by DPAS to the dentist and the insurer). The purpose of the VAT exemption for financial services is to overcome the difficulties connected with determining the taxable amount and the amount of VAT deductible.

Lastly, AG takes the view that the restructuring of the contractual arrangements by DPAS in 2012 does not reflect the economic reality, which is decisive for VAT. Moreover, DPAS recognized this fact when communicating that nothing would effectively change further to the restructuring. In addition, the AG finds irrelevant who is the recipient of the services, i.e. the dentists (creditors) or the patients (debtors) are the formal recipients of the service. The economic reality of the service is the same.

Our comments

If the CJEU follows the AG's Opinion, the VAT exemption for transfers/payments would become even more limited. This is in fact the trend of the CJEU's case law of last years.

The only exempt services would be those involving actual making of the payment. Other activities intervening in the payment chain, before or after the debit/credit of the account, will be taxed.

Some companies might be quite happy with the outcome, i.e. those performing services to retailers, which benefit from VAT recovery right and generally do not have VAT as cost. Such companies may increase their VAT recovery.

The case law in the field may become even more relevant with the advent of the Revised Payment Services Directive (PSD 2) which will bring more parties to the table.

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Slovakia

The Ministry of Finance's Opinion on "Digital Permanent Establishment"

The Ministry of Finance of the Slovak Republic (hereinafter the "Ministry of Finance") published its opinion on the definition of a permanent establishment on a digital platform.

The opinion addresses the provisions on the origination of a permanent establishment valid from 1 January 2018 where recurrent intermediation of transport and accommodation services, including via a digital platform, is also considered as a permanent establishment and performance of an activity at a permanent location. Pursuant to this regulation, a taxpayer with a limited tax liability may have a permanent establishment in Slovakia, regardless of whether the Slovak Republic has concluded a double taxation avoidance treaty with the taxpayer's home country. The legislation is a response to new forms of business carried out in the Slovak Republic via digital platforms without the operator's physical presence (a taxpayer with a limited tax liability) in Slovakia.

Digital platform operators who have a permanent establishment in the Slovak Republic are required to register as a taxpayer in accordance with Article 49a (5) of the Income Tax Act (ITA) and Article 67 (1) of the Tax Administration Act (The Tax Code). If a taxpayer does not have a permanent establishment under the ITA, but receives income pursuant to Article 16 (1) (e) (10) of the ITA, ie receives remuneration for the provided intermediary services, providers of transport and accommodation services have a secondary obligation, ie to deduct the tax at source pursuant to Article 43 of the ITA from the payments for the intermediation paid, transferred or credited to the taxpayer with a limited tax liability in the amount in which this remuneration is tax-deductible pursuant to Article 19 of the ITA. The obligation to withhold tax lasts until the registration of a permanent establishment. The collection of withholding tax applies to any income under Article 16 (1) (c) or Article 16 (1) (e) (10).

For a joint payment for several types of service, the taxpayer must allocate the payment by service as appropriate in accordance with the available underlying documents (eg for discount portals).

If such transport and accommodation services were intermediated before 1 January 2018, the amended legislation valid from 1 January 2018 will not apply to them, regardless of whether they are paid in 2018.

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Amendment to the Labour Code, amending Act No. 595/2003 Coll. on Income Tax, Act No. 461/2003 Coll. on Social Insurance and Act No. 580/2004 Coll. on Health Insurance

The National Council of the Slovak Republic adopted an amendment to the Labour Code, amending the Income Tax Act, the Social Insurance Act and the Health Insurance Act. The main changes include the determination of income considered as a wage, the remuneration of employees for work on public holidays and weekends, and the taxation method for such employee income.

The National Council of the SR adopted an amendment to the Labour Code, which introduces several changes to employee wage entitlements:

- Wage benefit for work on Saturdays – according to the amended Labour Code, in addition to the standard wage, employees are entitled to a wage benefit of at least 50% of the minimum hourly wage for work on Saturdays. If the nature of the work requires work on Saturdays, a lower wage benefit may be agreed (at least 45% of the minimum hourly wage).

- Wage benefit for work on Sundays – in addition to the standard wage, employees are entitled to a wage benefit of at least 100% of the minimum hourly wage for work on Sundays. If the nature of the work or the employer’s operating conditions require work on Sundays, a lower wage benefit for work on Sundays may be agreed (at least 90% of the minimum hourly wage).

- Wage benefit for night work – the wage benefit for night work was increased from 20% to 40% of the minimum hourly wage. Employees performing high-risk work are entitled to a wage benefit for night work of at least 50% of the minimum hourly wage. If the nature of the work or the employer’s operating conditions require work at night and an employee does not perform high-risk work, a lower wage benefit may be agreed (at least 35% of the minimum hourly wage).

- The definition of “wage” in the Labour Code has been extended: wage includes any financial performance that an employer provides to an employee for work during the summer holiday period or during the Christmas holidays.

The amendment to the Labour Code resulted in amendments to certain provisions of the Income Tax Act, the Social Insurance Act and the Health Insurance Act.

Income Tax Act

With respect to income from dependent activities, income exempt from income tax includes financial performance that an employer provides to an employee for work during the summer holiday period. The maximum amount of exempt income is EUR 500 in aggregate from all employers. If the paid financial performance is at least equal to the employee's average monthly salary and the employee's employment (state employment) relationship with the employer as at 30 April of the relevant calendar year has lasted for at least 24 continuous months, the tax base (partial tax base) will include only income exceeding the exempt amount. This provision will first apply to the amount of financial performance under separate regulations paid in June 2019.

A financial performance that an employer may provide to an employee for work during the Christmas holidays is also tax exempt. The maximum amount of exempt income is EUR 500 in aggregate from all employers. If the paid financial performance subject to the exemption is at least equal to the employee's average monthly salary and the employee's employment (state employment) relationship with the employer as at 31 October of the relevant calendar year has lasted for at least 48 continuous months and the financial performance for work during the summer holiday period was paid to the employee for the relevant taxation period, the tax base (partial tax base) will only include income exceeding the exempt amount. This provision will first apply to the amount of financial performance for work during the Christmas holidays paid to an employee in December 2018, provided that in June 2018 the employee received a financial performance for work during the summer holiday period that was at least equal to the employee's average monthly salary.

Social Insurance Act

An employee's assessment base includes the financial performance provided to the employee for work during the summer holiday period, which was provided to the employee during the 2019 and 2020 calendar years, and the financial performance for work during the Christmas holidays provided to the employee during the 2018 calendar year.

Health Insurance Act

If an employee received a financial performance for work during the summer holiday period or the Christmas holidays from multiple employers in an amount exceeding EUR 500, in the annual reconciliation of insurance premiums the employee's assessment base for each employer who participated in this financial performance will increase on a pro-rata basis depending on the amount of the financial performance.

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