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Spring is here and the global minimum tax of 15 % has arrived in Slovakia, too. As Slovakia is a capital importing country, the new rules will affect mainly hundreds of subsidiaries of MNEs in Slovakia, but only in a simplified form of the QDMTT (qualified domestic top-up tax) concept, whose basic goal is to calculate the effective tax rate (TOP 1). Our team of tax advisors represents AHK (Slovak-German Chamber of Commerce and Industry) in negotiations with the Slovak Ministry of Finance in this respect and is also preparing a joint seminar.

Slovakia has been facing the pressure of inflation quite successfully, it has the lowest annual inflation rate among the V4 countries, but within the EU, we are ranked 21st. Raising the ECB rate to 3.5 % will not only push these figures slightly up, but for the first time in years, the Slovak tax administration will have to apply penalties under the Tax Procedure Code of more than 10 % of the subsequently assessed amount, as three times the ECB base rate amounts to 10.5 %. In view of the simultaneous expected tightening of active repentance for tax offences (TOP 2), we recommend clients to pay close attention to tax audits.

Good news is that the new Minister of Justice has moved the draft of the new Act on Conversions of Companies further into the legislative process. The planned law should finally enable not only spin-offs as an important form of conversion, but also introduce a new legal form of a private foundation into Slovak law, which is a key tool for long-term sustainability of family businesses from a succession planning perspective (TOP 3). We are pleased to have made a significant contribution to this debate.

An overview of other important topics dealt with in our spring edition of the Newsfilter can be found below:

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TOP 1: PLANNED TRANSPOSITION OF THE 2ND PILLAR TO SLOVAK TAX LAW

In December 2022, the EU adopted the EU Council Directive 2022/2523 on ensuring a global minimum level of taxation for multinational enterprise groups. In particular, this involves the introduction of the global minimum tax at the level of groups with a turnover of over EUR 750 million that have an effective tax rate below 15 %. The aim of the directive is, above all, to prevent the speculative transfer of capital and business to countries with a low level of taxation and thus to prevent distortions of free competition.

The transposition of the directive into the national laws of the Member States is expected by 31/12/2023 with effect from 01/01/2024. However, there are also a few exceptions when the implementation of some articles of the directive can be postponed. Slovakia is one of the countries with significant inflows of foreign investment and capital. Taking into regard the country's position, it is clear that Slovakia's business portfolio contains mainly foreign-owned subsidiaries and a very limited number of parent companies.

The EU has provided a possible exception for such countries (if they have less than 12 parent entities) in the form of a possible postponement of some of the provisions of the Directive, e.g. the introduction of the offensive IIR (income inclusion rule) or UTPR (undertaxed payments rule) by a maximum of 6 years.

Considering the composition of business entities in the Slovak Republic, it is planned to introduce the QDMTT (qualified domestic top-up tax) concept, the basic objective of which is to calculate the effective tax rate and the possible top-up tax at the level of the constituent entity (subsidiary), i.e. to leave the above-mentioned additional tax on low-taxed companies in the Slovak state budget. The offensive IIR rule would shift the additional tax calculated to the state budget of the parent company's country. In addition to the introduction of the QDMTT, it is also planned to make use of an exception in Slovakia - a postponement of the implementation of the offensive IIR and UTPR rules, i.e. they would not be applied at the Slovak level from 01/01/2024.

According to preliminary calculations, the QDMTT rule and the additional top-up tax will affect approximately 1,000 subsidiaries at the level of the Slovak Republic. We recommend that the subsidiaries start communicating within their group and start setting up their IT systems to distribute the necessary data. Even if the constituent entity in the SR does not generate an effective tax rate of less than 15 %, there will be many reporting and notification obligations associated with this legislation to comply with. It is foreseen to introduce a separate form of tax return which will contain a different tax conversion for ETR (effective tax rate) purposes and also possibly different data compared to the traditional corporate income tax return.

Preparation and publication of a separate draft law in the inter-ministerial comment procedure are planned for spring/summer 2023.

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TOP 2: PLANNED CHANGES IN ACTIVE REPENTANCE FOR TAX CRIMES

The Ministry of Justice of the Slovak Republic has prepared a draft law amending Act No. 300/2005 Coll. (Criminal Law) as amended. The draft contains extensive changes and has so far undergone the inter-ministerial comment procedure. The changes will affect, inter alia, the tax area, in particular the provisions on active repentance.

According to the previous wording of the Criminal Law, the perpetrators of selected tax offences could wait for the outcome of the investigation, which either did not reveal their tax crime and even if it did, the perpetrator could avoid criminal liability by paying additional tax and accessories to the extent to which the investigation revealed this criminal activity. Considering these offences are intentional, the law is very soft. For this reason, the time limit for the payment of the tax due and accessories is being shortened to 60 days after the charges have become final and not only after the entire investigation has been carried out.

Regarding the offence of failure to pay wages and severance pay, the period for exercising active repentance is being extended also to 60 days from the date on which the charges become final. The period of 60 days from the commission of the offence for the payment of wages and severance pay, as currently applicable, has proved to be excessively short in practice.

In addition to the changes to active repentance, the threshold of criminality for most tax offences is being raised from the current EUR 266 to the value of the considerable damage (proposal: EUR 5 thousand). Up to this amount, the unlawful conduct will be punished by administrative proceedings. A new category of damage is also being introduced, i.e. damage of an extremely large scale, the threshold for which is at least EUR 1 million. This threshold is used in particular for property and economic offences.

The offence of false testimony and perjury is extended to include the intentional act of false testimony in tax proceedings before the tax authorities. The current qualification of such conduct as an offence, for which only a fine of up to EUR 99 was imposed, has not proved successful in practice.

The definition of damage is being supplemented by shortened, unremitted or unpaid tax or social/health insurance contributions, unduly refunded value added tax or excise duty, unduly obtained or used non-repayable financial contribution, subsidy, grant or other benefits from the state budget, the budget of the EU, the budget administered by the EU, the budget of a public institution, the budget of a state fund, the budget of a higher territorial unit or the budget of a municipality. The reason for the addition is to enable the authorities to claim, in criminal proceedings, the compensation for incurred damage, for example, in tax fraud, subsidy fraud or fraud involving EU funds.

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TOP 3: PLANNED CHANGES TO THE COMMERCIAL CODE

Upcoming changes in conversions of companies

In connection with the transposition of the EU Directive 2019/2121 on cross-border conversions of companies, new terms are introduced into Slovak legislation, which are primarily the division, change of legal form and indirectly the spin-off of companies. The introduction will follows through a separate act - the Act on Conversions of Companies and Cooperatives.

A planned novelty is the introduction of two completely new terms into Slovak law:

spin-off – process corresponding to a partial division, when the company being divided does not cease to exist as in the case of a division and its part is separated into another company. The legislation will apply to both domestic and cross-border divisions;
cross-border change of legal form - a company changes its registered office from one Member State to another and at the same time its legal form changes in accordance with the law of the country of the new registered office.

In connection with this change, a number of legislative changes to both the Income Tax Act and the VAT Act are currently in the comment procedure.

Planned introduction of a new legal form - private foundation

In February 2023, a draft law was published for comments in the legislative process, amending the Act No. 34/2002 on Foundations and the Civil Code.

Despite the fact that neighbouring countries have had regulated the above mentioned processes for a long time, there is no legal tool in the Slovak legal order for the management of assets that could be established to support a private purpose. In foreign countries, these are typical trust funds or private foundations. Thus, there is a lack of an instrument for effective asset management, control and distribution of assets within family businesses. As a result, many family firms have used concepts available abroad.

The effectiveness of the Act is proposed from 01/01/2024. At the moment, parallel commenting on the necessary changes in the Income Tax Act is also underway among experts.

TOP 4: NEW TRANSFER PRICING GUIDANCE

The Ministry of Finance has issued a new Guideline on the Contents of Transfer Pricing Documentation (hereinafter guidance), effective since 01/01/2023, which reflects the latest amendment to the Income Tax Act which we informed you about in the previous Newsfilter.

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The amendment defined the materiality of the transaction (generally EUR 10 thousand, for loans and borrowings the principal amount above EUR 50 thousand), which should also provide a safe harbour for small transactions. The guidance responds to this change by deleting Article 2(8), i.e. the general definition of materiality derived from the accounting rules. In other provisions, however, the guidance continues to use the concept of materiality of a transaction as defined by the Accounting Act or International Accounting Standards, in order to determine the scope of the documentation.

The guidance also specifically addresses the topic of permanent establishment. In addition to the standard documentation requirements, the permanent establishment is required to provide a description of how the capital and financing costs of the permanent establishment are allocated if it claims financing costs as tax deductible expenses.

An important change is the reduction of requirements for small entities. Shortened documentation is required to be maintained by an entity that is not required to maintain full-scope or basic documentation and also claims a tax relief, reports a tax loss, utilizes a tax loss deduction, or does not apply the 15 % tax rate.

TOP 5: ASSESSMENT OF FINANCIAL ADMINSITRATION ACTIVITIES

Two years have passed since the new President of the Financial Administration Jiří Žežulka took office. The Foundation Zastavme korupciu (Stop to Corruption) has analysed the functioning of the financial administration during this period.

The development in the performance of tax audits is generally perceived as positive. Two years ago, up to 41 % of tax audits were directed at inactive companies. From the point of view of recovering any tax due, this meant a waste of time and effort, as the chances of recovering the money were close to zero. This ratio has been reduced to 10 % after two years, because the targeting of audits has changed. Complex audits, which involved a large number of transactions and took weeks, are less common. There is more targeting at specific transactions and problem areas such as long-term loss utilization, large expenses for other services, etc. Tax auditors have a new analytical database to guide them during audits. The application also allows retrospective evaluation of the auditor's actions and contains a database of how similar cases have been handled in the past. In addition to the analysis of VAT recapitulative statements, further data sources are added, for example on vehicles or real estate. An important area of interest for auditors was transfer pricing. Preliminary figures for 2022 show an increase in revenue under this heading of almost EUR 30 million.

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If the result of a tax audit is an extra assessment in a significant amount, taxpayers usually defend themselves by first appealing to the Tax Directorate, and if the decision of the tax inspectors is upheld, they take the case to court. In regional courts, the success rate of the tax administration is roughly 72 %. If taxpayers fail, they can appeal to the Supreme Administrative Court, which they did in over 130 cases last year. There, too, the statistics are 70 % in favour of the tax administration.

A key area where the functioning of the financial administration needs improvement is undoubtedly the personnel policy. The area of risk is employing relatives. A new line has been added to the staff questionnaire where the employee gives information about other family members employed with the financial administration. The primary reason for this is to avoid the relationship of mutual superiority and subordination of such persons, as this is not permitted by law. A separate inspection unit is to be created in the coming months, the proposal for which is part of the legislative package within the amendment of the Criminal Law.

The activities of the financial administration were inspected also by the Supreme Audit Office last year, and numerous weaknesses were found, such as the lack of connectivity of customs and tax IT systems, which resulted in the inability to react quickly enough to possible tax evasion, for example. The Supreme Audit Office also identified the lack of cross-checking.

TOP 6: CORPORATE SUSTAINABILITY REPORTING DIRECTIVE

On 16/12/2022, Directive (EU) 2022/2464 of the European Parliament and of the Council regarding the reporting of corporate sustainability information was published, supplementing and amending the 2014 Non-Financial Reporting Directive. The Directive specifies which sustainability information (environmental, social and human rights and governance factors) should be disclosed and foresees that the verification of the compliance of the disclosed data with the reporting standards should be performed by auditors or accredited independent assurance services providers.

Initially, compliance of disclosures will be confirmed through **limited assurance** (negative form of expression) and subsequently through **reasonable assurance** (extensive procedures, including an assessment of the reporting entity's internal controls and substantive testing; positive form of expression).

The assurance services provider should maintain an assurance file and there should be at least one person within the company who is actively involved in the implementation of assurance on sustainability information reporting, the 'key sustainability partner'. Similar rules to those set out in Directive 2006/43/EC for the appointment and removal of statutory auditors and audit firms should apply to the appointment of the assurance services provider.

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The standards for limited assurance should be adopted by the Commission by 01/10/2026 and for reasonable assurance by 01/10/2028 at the latest. Until the standards are adopted, sustainability data will be reported according to the Committee of European Audit Oversight Bodies (CEAOB).

Assurance on the reporting of sustainability information by statutory auditors would help to ensure the linkage and consistency of financial and sustainability information, which could have a positive effect for users of the information. On the other hand, the Directive also allows Member States to introduce a requirement for independence of the assurance service, i.e. a requirement for separation of the statutory auditor and the assurance services provider.

The rules will be applicable gradually, depending on entity type:

1. In 2025, companies identified by the Directive and the original Non-Financial Reporting Directive (public interest entities with more than 500 employees) shall disclose data for 2024).
2. In 2026, other large companies (which meet 2 of the 3 criteria: turnover > EUR 40 million, assets > EUR 20 million, employees > 250) will publish data for 2025.
3. In 2027, small and medium-sized companies, excluding micro companies, whose securities are admitted to trading on an EU regulated market, will publish data for 2026.
4. In 2029, companies with subsidiaries outside the EU will publish data for 2028.

To illustrate what sustainability information reporting will cover, large enterprises and small and medium-sized enterprises that are public interest entities must include in the management report the information needed to understand the enterprise's impact on sustainability aspects and the information needed to understand how sustainability aspects affect the enterprise's development, performance and position. This includes, for example a brief description of the resilience of the business model and business strategy to risks related to sustainability aspects, the company's plans to make its business model and business strategy compatible with the transition to a sustainable economy and with limiting global warming to 1.5 °C in accordance with the Paris Agreement, a description of the time-bound targets for sustainability aspects set by the undertaking, including, where appropriate, absolute greenhouse gas emission reduction targets for at least 2030 and 2050, a description of the main risks to the undertaking related to sustainability aspects, and indicators relevant to the information to be disclosed. The Directive allows for exemptions from reporting obligations for subsidiaries in certain circumstances.

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For the sake of completeness, we note that the Directive has an impact on existing EU acts in the field of auditing, amending Regulation (EU) No. 537/2014 (on specific requirements concerning statutory audit of public-interest entities), Directive 2004/109/EC (on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market), Directive 2006/43/EC (on statutory audit of annual accounts and consolidated accounts) and Directive 2013/34/EU (on annual accounts, consolidated accounts and related reports of certain types of undertakings).

TOP 7: OECD RELEASES TECHNICAL GUIDANCE FOR IMPLEMENTATION OF THE GLOBAL MINIMUM TAX

On 02/02/2023, the OECD published administrative guidance (Administrative Guidance for the Pillar Two GloBE Rules) to assist individual countries in implementing a ground-breaking reform of the international tax system that will ensure that multinational enterprises (MNEs) will be subject to a minimum effective tax rate of 15 %.

In addition, the implementation package of the 2nd pillar was published by the OECD on 20/12/2022. The published package of publications contained in particular:
- Safe Harbours and Penalty Relief – manual on safe harbours
- GloBE Information Return - public consultation document
- Tax Certainty – publication on tax certainty in the context of the compliance of the implementation of the different GloBE rules

In December 2022, the EU Council Directive 2022/2523 on ensuring a global minimum level of taxation for multinational groups was adopted at the EU level. Many provisions from OECD administrative manuals contained above were left as open issues in the EU Directive, e.g. the safe harbours issue, in particular the possibility to simplify the GloBE reporting and the information contained in order to avoid duplication of reporting of the necessary data at the level of the constituent entity and the parent entity. For example, the discussion of a possible safe harbour, particularly in the initial implementation years, in the form of the possibility of using CBCR reports as the basis for calculating the effective tax rate, is considered significant.

The comments received on the compliance and coordination aspects of the global Pillar II minimum tax from the OECD/G20 Agreement on an Inclusive Framework for BEPS were discussed at a public consultation meeting on 16/03/2023.

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TOP 8: OECD RELEASES MANUAL ON THE HANDLING OF MULTILATERAL MAP AND APA

In February 2023, the Forum on Tax Administration (FTA) published a Manual on the Handling of Multilateral Mutual Agreement Procedures and Advance Pricing Arrangements (MoMA). MoMA was prepared based on questionnaires sent to 19 jurisdictions: Australia, Austria, Canada, China, Colombia, France, Germany, India, Ireland, Italy, Japan, Netherlands, Norway, Poland, Singapore, Spain, Thailand, the United Kingdom and the United States, of which 15 jurisdictions completed it in detail.

All countries agreed on the possibility of launching multilateral MAP and APA procedures, although they admitted that they subsequently encountered complications in the negotiation process.

MoMA summarises the key challenges that arise in multilateral cases:

1. First, there is no clear definition of a multilateral case and a lack of consensus on situations where multilateral solutions would be appropriate.
2. Second, there is no clear agreement among jurisdictions as to the most appropriate legal basis for dealing with such cases, i.e. whether treaty relationships need to exist among all jurisdictions concerned and whether multiple requests are required.
3. Third, several procedural concerns arise, such as the modalities of conducting such procedures, i.e. through multilateral discussions or multiple bilateral discussions and the sharing of information with multiple jurisdictions.

APA statistics published by some jurisdictions such as the United States, Australia, Canada and Japan shows that there are a number of instances where multilateral APAs are being requested and/or entered into.

MoMA states also an ideal timeline for a typical multilateral case, which provides for multilateral MAP and APA cases a mutual agreement between the competent authorities within 36 months from the day or receipt of the complete MAP/APA request. MoMA names also 3 simplified examples of transactions that would generally benefit from multilateral solutions.

TOP 9: ECJ JUDGEMENT IN A CASE ON DAC6

In December 2022, the European Court of Justice released a landmark ruling in favour of two legal profession bodies regarding the attorney-client privilege and obligations that apply under the sixth Directive on Administrative Cooperation (DAC6).

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DAC6 (EU Directive 2018/822) requires intermediaries – such as tax advisors, accountants, banks, and lawyers – to report relevant cross-border tax planning schemes before they are used. The aim is to provide EU member states with more information on the tax planning schemes that intermediaries design and market, so that they can assess whether the schemes facilitate tax evasion and avoidance before they are implemented.

The Directive introduces a reporting obligation on all those who participate in the design, marketing, organization or management of the implementation of arrangements that must be disclosed. However, each Member State may grant intermediaries a waiver from that obligation where it would breach legal professional privilege protected under its national law. In such circumstances, intermediaries are required to notify any other intermediary, or the relevant taxpayer, of their reporting obligations vis-a-vis the competent authorities.

Two lawyers' professional organizations brought actions before the Belgian Constitutional Court. They argued it is impossible to provide information to other intermediaries without breaching the legal professional privilege by which lawyers are bound. The Belgian Constitutional Court sought an answer from the Court of Justice in that regard.

In its judgment, the Court of Justice recalled first of all that Article 7 of the Charter of Fundamental Rights of the European Union protects the confidentiality of all correspondence between individuals and affords strengthened protection to exchanges between lawyers and their clients. In particular, the Court held that "the obligation to notify laid down by the Directive infringes the right to respect for communications between a lawyer and his or her client."

TOP 10: UPDATED EU LIST OF NON-COOPERATIVE JURISDICTIONS FOR TAX PURPOSES CONTAINING ALSO RUSSIA

On 14/02/2023, the Council of the EU updated the EU list of non-cooperative jurisdictions for tax purposes by adding four jurisdictions, namely **British Virgin Islands, Costa Rica, Marshall Islands** and **Russia**. No jurisdictions were removed from the list. With the new additions, the **EU list now consists of 16 jurisdictions**: American Samoa, Anguilla, Bahamas, British Virgin Islands, Costa Rica, Fiji, Guam, Marshall Islands, Palau, Panama, Russia, Samoa, Trinidad and Tobago, Turks and Caicos Islands, US Virgin Islands, Vanuatu.

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The EU list of non-cooperative jurisdictions for tax purposes was established in 2017 within the efforts to promote fair tax competition and address harmful tax practices. Jurisdictions are assessed on the basis of a set of criteria, such as tax transparency, fair taxation and implementation of international standards designed to prevent tax base erosion and profit shifting. Since 2020, the list is updated twice a year. The next revision is scheduled for October 2023.

USEFUL LINKS

Council Directive (EU) 2022/2523 (SK)
Guideline on the Contents of Transfer Pricing Documentation (SK)
Directive (EU) 2022/2464 (EN)
Administrative Guidance for the Pillar Two GloBE Rules (EN)
Manual on the Handling of Multilateral MAP and APA (EN)
ECJ Judgement in a case on DAC 6 (EN)
EU list of non-cooperative jurisdictions for tax purposes (EN)

Authors:


Judita Kuchtová
Tax advisor


Diana Mihályi
Tax advisor and auditor


Kristína Reguliová
Senior tax expert

BMB Partners
Zámocká 34
81101 Bratislava
T +421 2 212 99 000
M bmb@bmb.sk
www.bmb.sk
www.taxand.com