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WORKING PAPER

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MEETING DOCUMENT

From:	General Secretariat of the Council
To:	Code of Conduct Group (Business Taxation)
Subject:	(Draft) Progress Report by the Code of Conduct Group (Business Taxation) to the ECOFIN Council of December 2018 Annex: Slovakia's exemption of capital gains (SK008)

Delegations will find attached a document in view of the meeting of the Code of Conduct Group (Business Taxation) on 15 November 2018.

Slovakia's exemption of capital gains (SK008)

Below is a description of the regime:

1. Are there any territorial limitations to the activities of the taxpayers concerned by the tax exemption?

There is a territorial limitation. In order to be entitled for benefit, qualifying taxpayers (resident and non-resident taxpayers) are required to *“undertake core functions in the Slovak Republic, manage and bear risks associated with the ownership of shares or interest, and dispose of required staff and material equipment necessary for the performance of these functions”*. It follows that this regime is not ring-fenced.

2. We understand from your notification that both Slovak resident companies and foreign PEs located in the Slovak Republic. Can the foreign PEs of Slovak companies also avail of this regime?

The legislation does not explicitly exclude foreign PEs of Slovak resident companies. However, due to the substance requirement referred to in points 1 and 3 of this document, the exemption would not apply to the foreign PE of a Slovak tax resident.

3. How do you ensure that there is sufficient substance required of the taxpayers that benefit from this regime? In your notification you mentioned a nexus approach for this regime – could you explain how this works in practice?

According to paragraph 2 (b) of the Article 13c, qualifying taxpayer has to *“undertake core functions in the Slovak Republic, manage and bear risks associated with the ownership of shares or interest, and dispose of required staff and material equipment necessary for the performance of these functions”*. Compliance with this rule will be subject to tax audit.

4. Does the Slovak Republic have a holding company regime and if yes could you elaborate on it and how it interacts with this regime?

Slovak Republic has not introduced holding company regime.

5. In your notification you outlined the three principal conditions to qualify for the exemption – are there any further secondary conditions to avail of this regime?

There are no further secondary conditions.

6. Could you outline any anti-abuse measures relating to this regime?

There are no specific anti-abuse measures designed for this regime. In general terms, there are various anti-abuse measures in Slovak tax legislation, for example GAAR (Tax Code), TAAR and CFC rules (Income Tax Act, CFC rules will be effective as of 1 January 2019). Additionally, interest on loans for the acquisition of shares and business shares are not recognized as tax-deductible expenses, so the principle of symmetry is met.

7. Please describe the administrative procedure to benefit from the tax exemption.

There is not a particular administrative procedure (e.g. specific tax ruling or license). If qualifying taxpayers meet all conditions set out in Article 13c of the Income Tax Act, they do not include such an exempted income in their annual tax declaration.

Section 13c

- 1) Income exempt from tax includes the income from the sale of shares of an incorporated company or from the sale of ownership interest of a member of the limited liability company or limited partner in limited partnership or from similar business organisation abroad after fulfilment of the conditions under paragraph 2, of taxpayer according to Section 2(d) (2) and taxpayer according to Section 2(e) (3) with permanent establishment (Section 16(2)) except of the taxpayer trading with securities under special legislation.⁸⁸⁾
- 2) The exemption under paragraph 1 shall be applied if
 - a) the income from the sale of shares and from the sale of ownership interest is not earned before expiry of 24 consecutive calendar months from acquisition of direct ownership interest of no less than 10% in the share capital of the business organisation according to paragraph 1; and
 - b) the taxpayer undertakes core functions in the Slovak Republic, manages and bears risks associated with the ownership of shares or interest, and disposes of required staff and material equipment necessary for the performance of these functions, and in calculation of the tax base proceeds according to Section 17(1) (b) or (c).
- 3) The tax exemption does not apply to the sale of shares of an incorporated company and from the sale of ownership interest in a business organisation according to paragraph 1 which is in liquidation, bankruptcy, or restructuring proceeding. The tax exemption does not apply to the sale of shares and the sale of ownership interest if the taxpayer according to paragraph 1 is in liquidation.
- 4) In accordance with paragraph 2(a), the day of acquisition of direct ownership interest in the share capital of the business organisation according to paragraph 1 means the day of
 - a) payment of the monetary contribution;
 - b) payment of the contribution in kind which must not be later than the date of registration in the Business Register; equal procedure shall be undertaken for the recipient of the contribution in kind where the recipient sells shares or ownership interest acquired as individually invested financial assets¹⁾ or as a part of the contribution in the form of an enterprise or a part thereof;
 - c) conclusion of the procurement process being
 1. the day of registration of shares in the evidence of central depository register or in the evidence of the central depository member;^{74bf)}
 2. the day of transfer by endorsement and handover of the share in physical form;^{74bg)}
 3. the effective date of a written agreement on interest transfer to limited liability company and limited partnership;^{74bh)}
 - d) registration in the Business Register through which merger, consolidation, or separation of business organisations according to special legislation^{74bi)} takes effect for the legal successor of the taxpayer dissolved without liquidation, provided that the taxpayer sells shares or ownership interest acquired by the taxpayer dissolved without liquidation; equal procedure is undertaken by the taxpayer that acquires shares or ownership interest in the legal successor upon dissolution of the taxpayer without liquidation;
 - e) registration in the Business Register in the event of relocation of the registered office to the territory of the Slovak Republic.^{74bj)}
- 5) In accordance with paragraph 2(a), the day of acquisition of direct ownership interest in the share capital of the business organisation according to paragraph 1 does not include the day of

- a) conclusion of an agreement covering transfer of shares or ownership interest in future or after meeting other agreed deferral conditions , or conclusion of other similar agreement or contract;
- b) purchase of an option; or
- c) acquisition of pre-emptive right.

The footnotes 1, 74bf through 74bj and 88) shall read as follows:

1) Act No. 431/2002 Coll. on Accounting.

74bf) Section 22 of Act No. 566/2001 Coll., as amended.

74bg) Section 21 of Act No. 566/2001 Coll., as amended.

74bh) Section 115 of the Commercial Code.

74bi) Section 69a and 256 of the Commercial Code as amended.

74bj) Section 26(2) of the Commercial Code.

88) Act No. 566/2001 Coll. as amended.

Act No. 385/1999 Coll. as amended.

Section 19

Tax Expenses

- 2) The following tax expenses may be deducted only to the extent and subject to the terms and conditions set out in this Act:
 - f) expenses (costs) equal to the aggregate of input value of shares and the aggregate of input value of other securities under Section 25a in the tax period, in which they are sold, up to the aggregate proceeds from the sale thereof, except for
 - 1. bonds, the selling price of which is not lower by more than the interest accrued on the bonds included in the tax base up to the date of sale or the maturity date of the bond;
 - 2. taxpayers, which undertake trading with securities under special legislation,⁸⁸⁾ and which may deduct the expense (cost) incurred on acquisition of securities up to the amount accounted for as an expense (cost);
- 3) Also the following items shall be treated as tax expenses:
 - u) interest paid on loans and credits used for acquisition of shares of an incorporated company or ownership interest of a member of a limited liability company or limited partner in limited partnership or a similar business organisation abroad of a taxpayer according to Section 2(d) (2) and taxpayer according to Section 2(e) (3) with permanent establishment (Section 16(2)) in the tax period in which the shares or ownership interest are sold, provided that the taxpayer does not meet the conditions for tax exemption according to Section 13c in such a tax period ; this shall not apply to the taxpayer which trades with securities under special legislation.⁸⁸⁾

Section 52zn

Transitional Provisions to the Regulations Effective as of 1 January 2018

- 17) The provision of Section 13c in version effective as of 1 January 2018 shall be applied to the income from the sale of shares or ownership interest acquired prior to 1 January 2018; for which the condition of paid up direct ownership interest in share capital in the amount of 10% and registered in the Business Register has been met, provided that for purposes of fulfilment of the condition under Section 13c (2) (a) the period of 24 consecutive calendar months shall begin as of 1 January 2018. As for the taxpayer with the tax period of a business year, the provision of Section 13c in version effective as of 1 January 2018 shall be applied to the income from the sale of shares or ownership interest acquired before the end of the tax period immediately preceding the tax period which began after 31 December 2017; for which the condition of paid up direct ownership interest in share capital in the amount of 10% and registered in the Business Register has been met , provided that for purposes of fulfilment of the condition under Section 13c(2)(a), the period of 24 consecutive calendar months shall begin as of the first day of the tax period beginning after 31 December 2017.
- 18) The provision of Section 19(2) (f) (1) in version effective until 31 December 2017 shall apply to the sale of shares acquired no later than on 31 December 2017, and for the taxpayer with a tax period of business year, it shall apply to the sale of shares acquired by the end of the tax period immediately preceding the tax period beginning after 31 December 2017 which does not meet conditions for the tax exemption according to paragraph 17 and Section 13c.